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2023 Q1
Debt Markets in Motion

Debt & Capital Advisory

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CEO & CFO summary

Public markets have been severely impacted by **uncertainty and volatility** as a result of COVID-19, the Russia-Ukraine conflict, rising interest rates, sovereign defaults, and a Chinese property crisis that spilled into Asia's largest economy. Despite a backdrop of such macro volatility, Asian debt markets have continued to weather the storm and proved their **adaptability and resilience**.

Looking ahead through 2023, China's reopening and the expected end of US rate hikes should provide **a more stable backdrop** in this emerging debt market.

1. **China's reopening**: We see growth and recovery supported by China's reopening being reflected in credit availability and local interest rates in Asia. Demand shifts in supply chains, technology transfers, commodities, services and tourism will be at the front of the minds of investors.

2. **Hard currency debt**: Significant US dollar strengthening and a relatively strong RMB has forced borrowers to focus inwards and solve for more local currency being needed to service existing debt.

3. **Short durations & floating rates**: In a rising interest rate environment, investors prefer to limit their exposure to long duration and fixed interest risks. We believe this trend will continue as lenders try to keep their portfolio flexible until the economic situation further stabilizes.

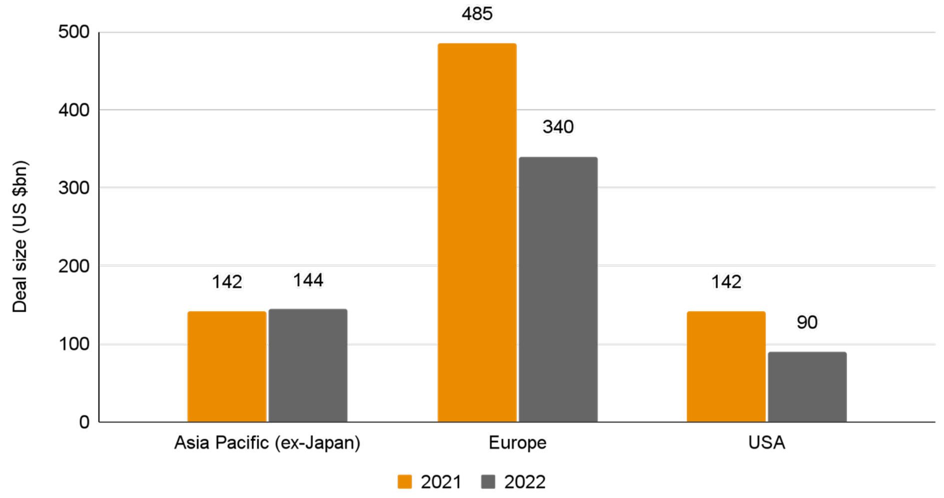
4. **Resilient Asian market**: Asia is a diverse region consisting of developed and emerging markets with varying banking sector sophistication and capital market maturity. We saw robust transactional volume from Japan and Southeast Asia in the face of global volatility. Looking ahead to 2023, we expect demand across the region to bounce back across core markets.

5. **Robust ESG demand despite downturn**: We saw sustainable financing hold up well in Asia last year, in the face of global volatility. Issuance was driven by strong local demand, offsetting the fall in the cross-border markets. We expect the process of de-carbonisation to continue to drive sustainability investments in Asia. All of the opportunities we see have to address ESG front and centre as they set out their financing plans. Increasingly this goes beyond carbon alone.

6. **Syndication challenges:** We notice a theme of uncertainty that is prevalent in this region relative to more established markets. This often presents extreme challenges when coordinating banking groups in syndicated environments across borders. We expect this will continue to evolve.

Hot topic: Environment, Social & Governance (ESG)

Chart 1: Regional ESG bond issuance 2021 vs 2022



Source: Refinitiv

Stable **issuance** of ESG bonds in **Asia Pacific (APAC)** defied a global drop in demand, with the region contrasting heavily with 30% volume declines in Europe and the US.

59.3% of Asia Pacific ESG bond issuance originated in China, with buyers attracted by the nation's **steadier domestic interest rates and significant investment in the "Green Agenda".**

Despite most ESG bond issuance occurring in developed **East Asia**, rapid issuance growth in nations like the **Philippines** signals increasing appetite for sustainable debt products across Asian emerging markets.

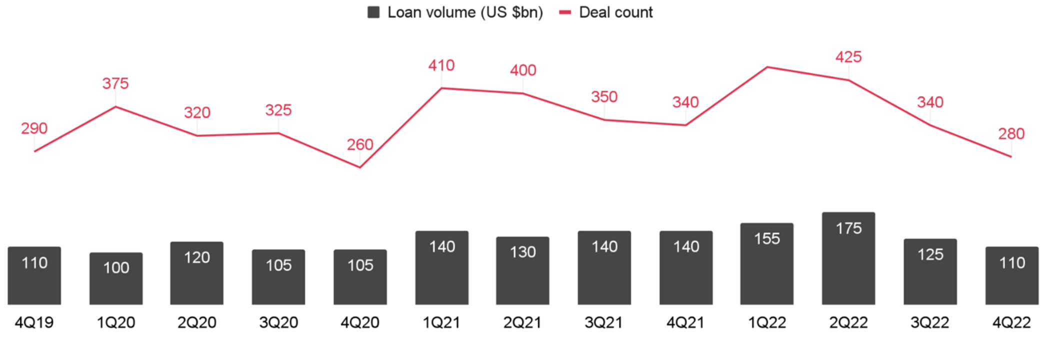
Investors continue to express concerns regarding greenwashing in the market due to **unambitious targets, immaterial KPIs, and small penalties.**

China's pledge to **double their wind and solar** capacity by 2030 is expected to drive more investors into the carbon transition bond market.

ESG bonds and loans are expected to continue their rapid growth in 2023 thanks to **strong local demand** and an upcoming pipeline of **de-carbonisation projects.**

2022 in review

Chart 2: Asia Pacific loan volume and deal count (ex-Japan)

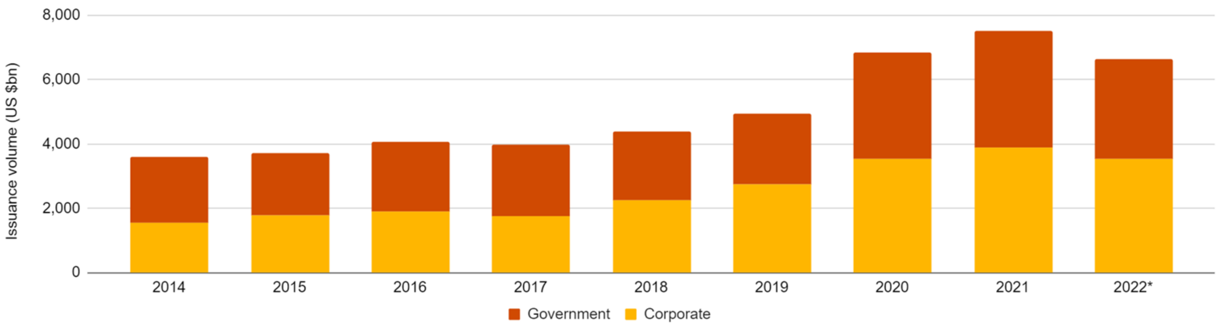


Source: LoanConnector

2022 represented an improvement over 2021 in Asian debt syndication, with lending increasing 3% YOY to US$548bn. 3-4Q lending saw a nose-dive in volume, with creeping recession concerns reducing capital redeployment into certain regions and industries.

Southeast Asia saw strong lending growth, with lenders targeting state-owned or quasi-sovereign enterprises for their perceived safety. Asian IGs faced increased competition on the back of dollar appreciation and higher US treasury yields. With a shaky Chinese real estate market, Asian HYs saw unprecedented outflows as underlying concerns of security enforcement and sovereign defaults scared off bondholders.

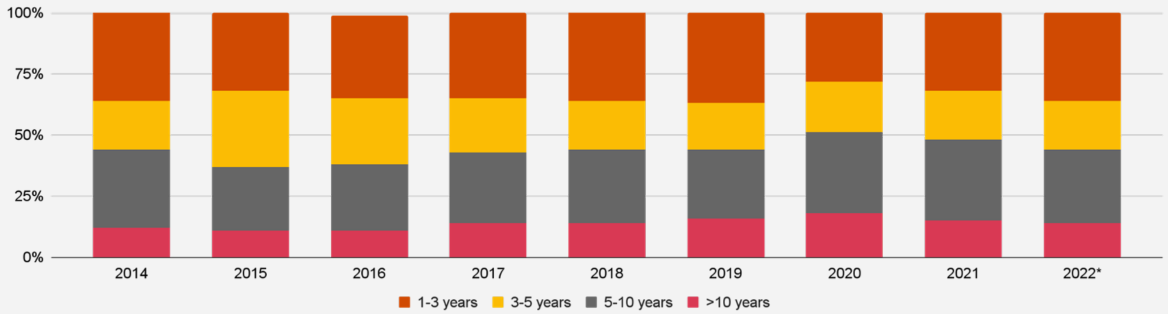
Chart 3: Asia Pacific local currency bond issuance



*Source: Asia Bonds Online, Asia Development Bank | *1H2022 annualized to represent FY2022*

Markets are evolving

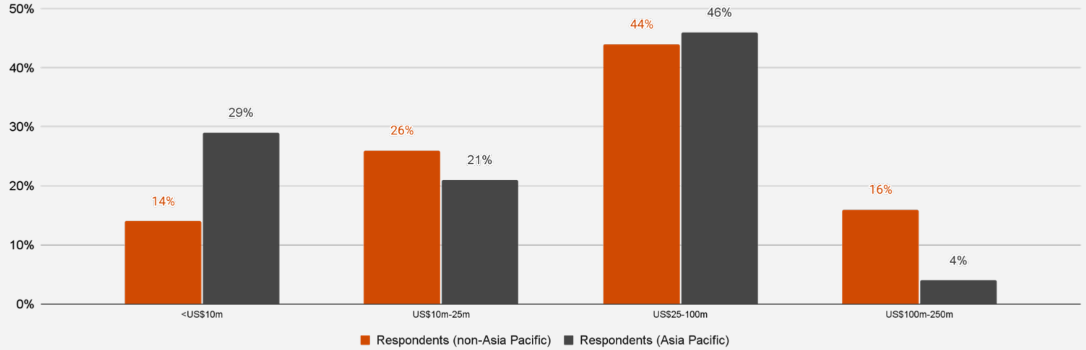
Chart 4: Hong Kong SAR local currency corporate bond maturity profile



*Source: Asia Bonds Online, Asia Development Bank | *1H2022 annualized to represent FY2022*
Note: Hong Kong SAR bond maturities used given the city's position as an Asian financial hub

Complexity is increasingly becoming a key theme in Asia Pacific debt capital markets as more economies access global capital. Investors are focusing on traditional issues of liquidity and cash flow, but also regional geopolitical and local currency risks. The rise of non-banking financial entities in Asia (e.g. private credit) stand to redefine the small- to medium-cap debt universe. Increasing amounts of short-maturity bonds indicates investors' anticipation of higher interest rates against the backdrop of US tightening. All these factors require experience and resilience to navigate this fast and constantly-evolving capital landscape.

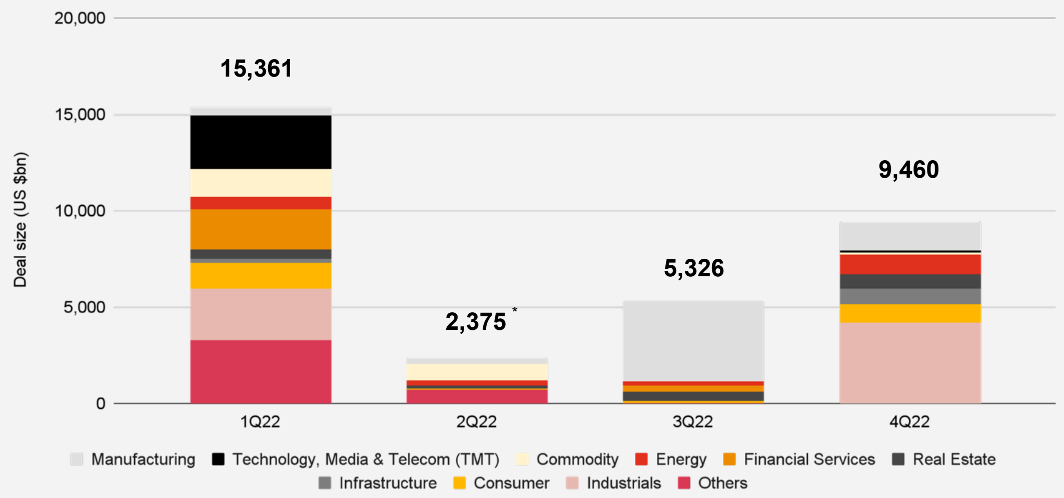
Chart 5: Typical private credit target loan size



Source: Alternative Credit Council

What we are seeing in APAC

Chart 6: Deal Composition by Sector



Source: PwC analysis

** Note: Excluding US$15bn sovereign debt in June*

Industrials (21%), Manufacturing (20%) and TMT (9%) were the key constituents in our 2022 deal flow.

Industrials was the largest source of deal volume at US$6.92bn, with deals in diverse sub-industries such as aviation, diamond polishing, and industrial machinery.

The Ukraine-Russia conflict brought unique disruptions to the commodity and energy sectors, with borrowers looking for sizeable financings amid the broader supply chain and energy price context.

The fall in deal size seen in 2Q22 was driven largely by the **beginning of hostilities between Ukraine and Russia** in February and the beginning of rapid global fiscal tightening.

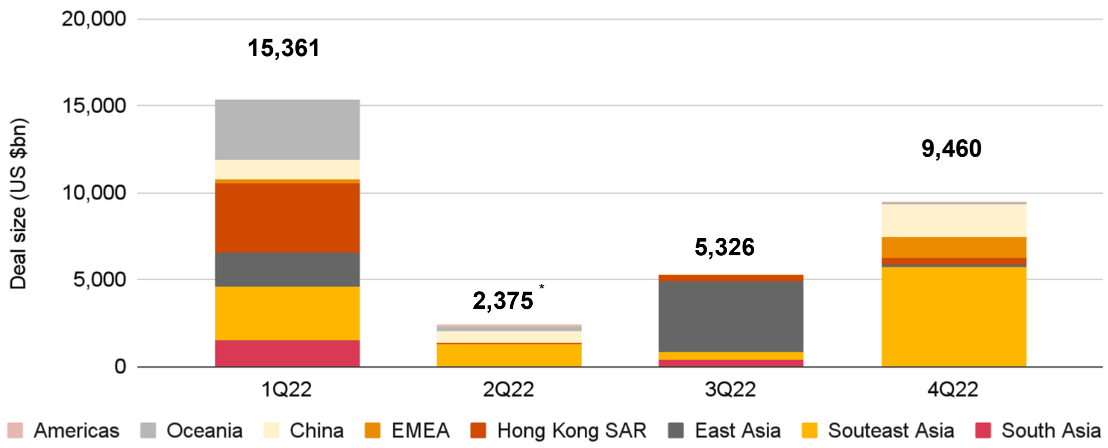
The TMT and infrastructure sectors were particularly attractive to investors, **representing potential for steady and predictable cash flows.**

We saw a number of real estate entities seeking financed, but **investor appetite was lacking** in light of current volatility in the industry.

We notice a regional theme prevalent across all sectors where coordinating banking groups in a syndicated environment is an extreme challenge.

What we are seeing in APAC

Chart 7: Deal Composition by Geography



Source: PwC analysis

** Note: Excluding US$15bn sovereign debt in June*

Asia Pacific investors are more wary of currency fluctuations amid a strengthening dollar, with 63% seeing a negative impact in 2023 versus 61% in EMEA and 39% in the Americas.

China's plan to dial back the **"Three Red Lines" policy** is expected restore confidence in a real estate sector struggling from the effects of lockdowns, although we expect international investor concerns over enforcement rights to linger.

We saw healthy transactional volume and investor appetite from countries like **Japan, Australia, Singapore and South Korea.**

Japan's weak Yen and low inflation are expected to continue driving deals in the future, with Japanese capital providers continuing to dominate the market.

Inflationary pressures are expected to be **less severe in Asia**, with China experiencing an inflation rate of 2% compared to 8% in the US.

India and Southeast Asian economies are expected to fare far better than their North Asian counterparts as the regional **tourism industry recovers.**

Typical debt value in our major segments:

Industrials

Debt size: US$20m-1,400m

Energy

Debt size: US$15m-1,000m

Commodities

Debt size: US$40m-700m

Manufacturing

Debt size: US$90m-2,500m

Infrastructure

Debt size: US$100m-800m

TMT

Debt size: US$100m-1,800m

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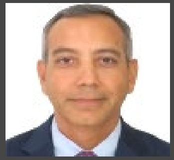

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