The Opportunity for High Yield in Asia

Bryant Edwards, Latham & Watkins
Asia High Yield Has Grown Steadily, with US$39 Billion Issued Last Year
Although Growing, Asia Trails the European and US HY Markets, Which Issued US$98 Bn and US$190 Bn in 2011
Underweight? While Asia’s GDP Exceeds US GDP, Asia HY Issuance is a Fraction of US Issuance. Why?

Asia HY Volume Compared to Asia GDP

Asia GDP as % of US GDP

Asia HY as % of US HY

19%

108%
During the Last Three Years, China Has Led the Rule 144A Asia High Yield Market, Followed by Indonesia
Two Things About Chinese HY: First, Highly Concentrated in Real Estate
Second: Chinese HY Structures Are Structurally Subordinated, With No Onshore Credit Support
Sound Familiar? The First Generation of European HY Was Concentrated in One Sector: Cable and Telecom

Use of Proceeds of First Generation European HY (1997-2000)

- Cable & Telecom Buildout
- M&A
- Refinance Bank Debt
- General Corporate
- LBO
And It Was Structurally Subordinated, With No Credit Support From Operating Assets
HY Investors in European Cable and Telecom Almost Totally Wiped Out

% of Original High Yield Claim Recovered in Cash or New Debt

- FLAG
- Grapes
- Versatel
- Marconi
- NTL
- Energis
- Jazztel
- Netia
- Level 3
- TIW
- McLeod

European Structures

US Structures
While Senior Secured Bank Lenders in Europe Recovered Slightly More Than US Senior Secured Lenders . . .
Holders of Senior European Bonds Recovered Only 20% - 40% of the Average Recovery of Senior US Bonds
Investors Boycotted European HY - By 2003, Industry Responded With New Structure

- CD&R Fund VI
  - 100% owned
  - Investment vehicles
    - 76.7% owned
    - JPMorgan Partners Co-Investors and Other Co-Investors
      - 23.3% owned
      - Brake Bros Limited Partnership
        - 100% owned
        - Holding Companies
          - 100% owned
          - Management Investments (on-going program)
            - Brake Bros Finance PLC
              - 100% owned
              - Intercompany Loan
                - Brake Bros Acquisition PLC
                  - 100% owned
                  - Senior Facilities
                    - Senior-Subordinated Guarantee
                      - Second-Priority Shares Pledge
        - Brake Brothers Limited
          - Operating Subsidiaries
            - Senior-Subordinated Guarantee
              - Pledge of Intercompany Loan
Will China Change the Rules?
The Wall of Money: Demand For Asia Local Currency Bonds Has Exploded

Local Currency Bond Sales in Asia (ex. Japan)

So far in 2012, US$520.93 bn of Asia local currency bonds sold
Prices on Asia Local Currency Bonds Have Risen as Yields Declined

At 29 Oct 2012, the average yield on Asia local currency bonds had dropped to 4.05%.
China May Not Be Able to Rely on its Banks to Continue to Fund Growth. Then What?

• In 2008, China announced a 4 trillion yuan stimulus package to combat the financial crisis.

• However, between 2009-10, Chinese banks actually lent 17.5 trillion yuan—mostly to SOEs of local governments.

• On June 22, Fitch Ratings said that the bad loan ratio could exceed 15%