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Friday, May 8, 2020

MARKETS

	Thursday	Change
STI	Closed	-
KL COMP	Closed	-
NIKKEI 225	19,674.77	+55.42
HANG SENG	23,980.63	-156.85
SHENZHEN B	835.22	+1.21
DOW (10.30am EDT)	23,967.68	+303.04

DAILY DIGEST

As food and beverage merchants hunt for alternatives to the food delivery apps and their steep commissions, on-demand logistics startup Lalamove could be about to get its big break.

PHOTO: LALAMOVE

TOP STORIES / 3

Regulators on both sides of the Atlantic have spent the better part of three years trying to kill the London interbank offered rate. Now, they're looking to it once again to underpin hundreds of billions of dollars in loans as they seek to rescue their economies.

BANKING & FINANCE / 8

China's iron ore imports in April rose 13 per cent from a month earlier on robust demand from steelmakers as downstream sectors started to emerge from lockdowns aimed at containing the coronavirus epidemic.

INDUSTRY / 9

The number of Americans filing for unemployment benefits topped three million for a seventh straight week, signalling little relief in sight for the economy since the coronavirus began closing restaurants, factories and offices from coast to coast in mid-March.

GOVERNMENT & ECONOMY / 14

Some VCs, PEs in a spot as investors dodge capital calls amid pandemic

Certain investors with severely impacted businesses facing tight liquidity

BT EXCLUSIVE

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AS businesses and investment portfolios take a hammering from the economic impact of the novel coronavirus, venture capital and private equity firms might have to cope with a surge in investors failing to participate in capital calls.

"Certain types of investors in particular, such as high net worth individuals and family office investors that have businesses severely impacted by Covid-19 will have less cash-on-hand available to invest," said Jason Nelms, a partner who specialises in fund formation at law firm Morrison & Foerster.

These liquidity issues could be an obstacle for fund managers or general partners (GPs) wanting to deploy capital to investment targets identified during the novel coronavirus pandemic.

A number of VC firms in the region are already having trouble calling for capital from limited partners or investors, despite having binding commitments in hand, several sources have told *The Business Times*.

It is likely that more investors will begin to default on their capital contribution obligations, industry players say.

"Looking at past recessions, there were many incidents of limited partners (LPs) such as banks not being able to fund capital calls as their own balance sheets were weak. These LPs needed the cash for their own business needs rather than funding investments, and the same may happen now as some LPs are themselves badly affected," said Chua Boon Ping, chief executive of SPH Ventures, an LP in some VC firms in China and the US.

"Although LPs are binded by strong contractual remedies – such as the forfeiting of all amounts an LP has already invested in the fund – to prevent defaults on capital commitments, it is very rare for a GP to take LPs to court for violating the contract by not paying in capital, in order to avoid reputational risks and expensive disputes," said Morrison & Foerster's Mr Nelms.

"In the same vein, many GPs are hesitant to call capital in order to avoid aggravating LPs who may not think this is the right time for calling and deploying cash," he added.

Mr Nelms noted that even though many LPs might still have the financial capacity to meet their capital contribution obligations, they may not want to do so in this current climate of uncertainty. Some types of LPs may also be willing to break their contracts and walk away rather than meet their funding commitments, especially if it involves a new fund that only raised a small amount of cash so far.

"However, consistent with past market crises, we expect that the vast majority of LPs will take a long view and continue to meet their obligations. Both GPs and LPs have strong incentives to work together to find mutually beneficial solutions," Mr Nelms added.

Clearly, VC firms that have cash on hand, or had called for funds prior to the Covid-19 crisis, are now in a stronger position.

Mr Nelms says many general partners are also hesitant to call capital as limited partners may not think this is the right time for calling and deploying cash.

Funds with more institutional LPs are also likely to face fewer capital call issues, as these LPs tend to have more experience with alternative asset classes like venture capital. They are typically more conservative during allocation and provisioning, and often have more buffer capital on hand, said Lim Kuo-Yi, managing partner of VC firm Monk's Hill Ventures.

Also, LPs with a long established private markets portfolio should have a well-balanced cash flow situation, said Suvir Varma, a senior analyst at Bain and Company.

On the other hand, funds that are dominated by a major non-institutional investor; such as family offices, corporates or high net worth individuals might face more pressure during this time, industry players say.

"However, most funds tend to have a diversified LP base, where a single LP does not account for more than 10 to 20 per cent of the fund. There should be enough other investors at the table who are able to step up and cover that shortage, such that investments can still be made," Dr Lim said.

Chua Kee Lock, CEO of Vertex Holdings said venture capital firms could keep investors in the loop about upcoming commitments and give them a heads-up if possible, which will result in greater understanding both ways.

Generally, once a capital call is made, VC firms will give LPs 14 to 21 working days to send the money in.

"A few months back, we informed our LPs three weeks before the capital call was made to prepare them ahead of time. We also gave an additional two weeks for LPs to get the capital ready, which made it a smoother process for them," said Mr Chua.

"The best practise for GPs is to communicate regularly their capital call needs and invest at a steady pace so that LPs can manage the capital calls," said Mr Chua of SPH Ventures.

Transparency is also key when it comes to communicating with investors. Mr Chua of Vertex said that reaching out to investors early on to share their analysis on portfolio companies in light of the crisis - addressing what the challenges were and what to expect - helped the firm manage investors' expectations, and get everyone on the same page.

According to a Bain and Company report released last Wednesday, LPs are also looking for advanced notification of capital calls from GPs and forward-looking guidance to inform their cash flow analysis, especially during a downturn.

"However, more often than not, capital calls have exceeded distributions, affecting some LPs' ability to make new fund commitments," the report added.

"There may be push back from LPs in future and GPs may have to slow down their investment pace, since initial public offerings (IPOs) and trade sales are unlikely to happen any time soon. LPs need GPs to return capital to them before they can commit to a new fund," said Mr Chua of SPH Ventures.

In the short term, some LPs might look to, at best, maintain, or even reduce their exposure to private markets, said Dr Lim.

Mr Varma said: "Some LPs have short term liquidity needs due to their pension or other obligations. As such, it is possible that some of those LPs will be prudent with their allocation to private markets at the moment, until they are more certain what their net cash flow positions will be."

However, it might still be too early to predict if LPs will cut investments significantly in the longer term as the value of their private market holdings do not get adjusted that frequently.

"They will probably wait for fund managers to report adjustments in their assessment of the state of the businesses before looking at the entire portfolio again," Dr Lim added.

"LPs with long-term experience investing in private equity know that the long-term returns from the asset class have exceeded returns from all of their other asset classes. That's why we have seen a gradual shift towards more allocation to the private markets in the last decade," said Mr Varma.

Dylan Chong in his tailor shop, Dylan & Son. BT PHOTO: YEN MENG JIIN

Can Singapore's next-gen tailors make the cut?

A BUSINESS suit is a rare sighting on the streets of Singapore. Smart casual (emphasis on casual rather than smart) is the name of the workwear fashion game. And to be fair, a jacket can be unbearable in our humidity and heat.

Still, a new generation of tailors has enjoyed a revival in recent years, riding on a fresh wave of demand for snappy dressing and things bespoke. That is, right up until Covid-19 took all bets off the table. Singapore's next-generation tailors talk about the challenges facing their niche trade, in Brunch this Saturday in *The Business Times Weekend*.

Marsha Vande Berg is bullish about globalisation. The corporate luminary, formerly CEO of the Pacific Pension and Investment Institute who now sits on the boards of numerous companies and non-profit organisations, is similarly optimistic about sustainability. She tells The Raffles Conversation why.

Despite the doom and gloom surrounding the impending global recession, stock markets appear to be making their own conclusions. Our Chart View columnist warns that things might be looking up in the markets, but investors should exercise extreme caution.

What the Covid-19 crisis has also shown is that those investments we take to be safe as houses are not as protected as they seem. Insights from the CFA Society Singapore looks at how Singapore Reits will fare.

With economies preparing to restart, what does the future hold for hospitality, one of the worst-hit sectors? In the Broad View, major Asia-Pacific hoteliers give their take.

In football, The Finish Line rounds up how leagues in Europe are planning to make a valiant bid to finish the 2019/20 campaign. And in our Health page, a look at the ongoing Covid-19 crisis as a chance to re-examine, realign and re-energise our values, our priorities and our prowess.

ASEAN BUSINESS

Asean economies should tackle structural issues during Covid-19 slump

Lack of progress on AEC, supply chain inefficiences among issues to address

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WHILE Covid-19 has put a pause on investment activities in the region, there are a number of structural issues that Asean economies can and should tackle even as they grapple with the virus fallout.

Jeff Pirie, executive director, Corporate Finance Advisory, Deloitte Southeast Asia & Singapore, said this pause in investment activity could last from six months to a year, after which we may see a resurgence in merger and acquisition activity.

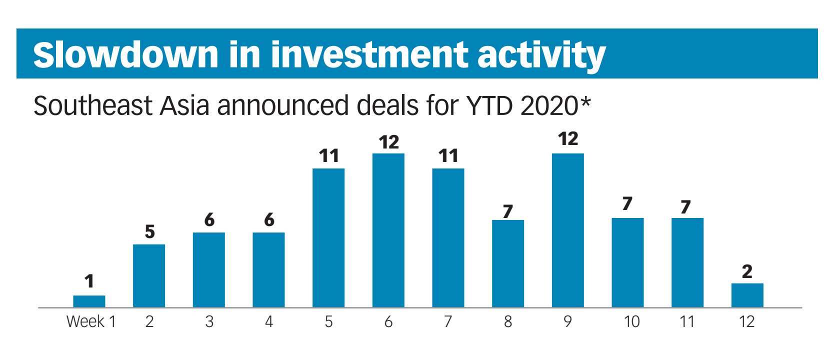
According to data from Mergermarket, Southeast Asia recorded 80 inbound and domestic deals in Q1 this year compared with 88 deals the same period last year.

David Wijeratne, Partner, PwC Growth Markets Centre was also optimistic.

"In the near past, Asean has shown strong signs of stability which should help post a robust recovery in investments once the current situation stabilises," he said, noting that as per the 2019 Asean Investment Report, the region registered all-time high figures for FDI in 2018 (US$ 155 billion), having witnessed a steady rise since 2016 and new investment records being seen for Cambodia, Indonesia, Singapore and Vietnam.

But executive director of the EU-Asean Business Council, Chris Humphrey said those same numbers are a cause for concern.

"The region has been riding a wave of good news for the last few years, certainly since the last financial economic downturn in 2009 ... but something like (Covid-19) comes out of the blue, it can deflate your balloon quickly," he said.



One of the key issues highlighted by the association is the lack of progress on the implementation of the Asean Economic Community (AEC).

The EU-Asean Business Council published a paper in late March calling on Asean to realise the vision of the AEC, to remove non-trade barriers (NTBs) and trade more with itself.

"Progress on the Asean AEC continues to be painfully slow. The much talked about promise of a 'single market and production base' as set out in the original AEC Blueprint 2015 has failed to materialise; the dream remains a dream and if anything is further away than ever before," stated the report.

According to the EU-Asean Business Sentiment survey which was released in September last year, 88 per cent of respondents said they expect to increase their trade and investment in Asean in the next five years, up from 75 per cent in 2018.

It is worth noting that while these figures reflect pre-Covid-19 sentiments, issues including perception of unfair competitive practices from local/regional actors have continued to increase (77 per cent said they believe they face unfair competition at least occasionally, up from 62 per cent in 2018).

More than half (54 per cent) of the respondents said there are too many barriers to the efficient use of regional supply chains in Asean. Of those who already use regional supply chains, 80 per cent said they would increase usage if barriers were removed.

Indeed, even as Asean aims to remove NTBs to trade, 78 per cent of respondents said there are too many barriers, up from 63 per cent in 2016.

PwC's Mr Wijeratne agreed that NTBs remain an issue and "must be considered a priority" by Asean governments to improve investments.

Deloitte's Mr Pirie added that the current situation "provides an impetus" to redouble efforts to meet the 2025 goals for the AEC.

"Of course, such efforts have to take a back seat until we transition to the next 'normal'. As that state becomes clearer, it will likely be recognised that a more integrated Asean will be more resilient as a whole," he said.

Marc Philipp, Management Consulting Leader, PwC South East Asia Consulting added that moving forward, end-to-end connected supply chains will become imperative for market success, not just for large-scale customers but also medium and smaller suppliers.

Using digital solutions to connect various data sources across the value chain participants in real time will enable companies to move towards more autonomous, self-managing supply chains, he noted.

"Unfortunately companies in Asean are lagging behind peers in other APAC countries when it comes to digitalising its operations. This is an area that will require accelerated efforts to take advantage of market opportunities and remain a preferred investment destination for multi-nationals worldwide."

Even as consultants look further out for a rebound in interest in the region, Enterprise Ireland (EI), which is the Irish Government's trade and innovation agency, notes that Asia remains a bright spot for Irish companies.

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