Olympus credit team spins out, gets OMERS backing

Asian Venture Capital Journal | 28 January 2021

Olympus Capital Credit has rebranded as Orion Capital Asia, with OMERS replacing Olympus as the firm's equity partner. The strategy is unchanged, with COVID-19 helping to drive deal flow

When searching for a new sponsor, autonomy was of critical importance to the team at Orion Credit Capital Asia, a middle-market private debt player that spun out from Olympus Capital Asia last year.

"There are groups with large credit businesses in Europe and the US and don't have a presence in Asia. For them, we were a logical fit. But we were reluctant to pursue that option because we wanted to retain our independence," says Nitish Agarwal, Orion's CIO.

"I have seen firsthand, coming from global banks, how important it is to have local decision making. We didn't want to become a small offshoot of a large US or European firm, so we only worked with parties where we were not going to become employees of that institution."

Ares Management took the ownership route last year, when it snapped up a controlling stake in SSG Capital, which at the time had $6.2 billion in assets under management. Orion cannot claim that kind of scale – it has raised one fund and several separately managed accounts (SMA) and issued more than $1 billion in loans – but given the scarcity of independent middle-market private debt platforms in Asia, there was plenty of investor interest.

The team went with Ontario Municipal Employees Retirement System (OMERS), a Canadian pension plan with C$109 billion ($85 billion) in assets, because it was willing to put in capital while scrutinizing from afar. Orion has given up a stake in the GP in return for an SMA mandate and a commitment to its next fund. This vehicle is expected to launch in the second quarter of 2021.

According to Agarwal, OMERS has set up similar sponsorship arrangements in private equity and infrastructure, but not in private debt. Orion also represents its first deal of this type in Asia across all asset classes. "Growing our investment footprint in Asia is a strategic priority for OMERS and this investment is an important initiative in achieving our goals," Ashish Goyal, a senior managing director at the pension system, said in a statement.

Building a book

Olympus entered the credit space in 2013, allocating a portion of its third pan-regional private equity fund to the nascent business. From the outset, the private equity and credit divisions operated independently of each other, with dedicated teams.

Explaining what motivated the initiative, Daniel Mintz, founding managing director of Olympus, cited the impact of the Basel III requirements, the euro zone crisis, the Volcker Rule, and hedge funds focusing on liquid investments post-global financial crisis. Basel III is as relevant now as it was then, having increased the cost of lending for commercial banks. Of those that were willing to do business with smaller borrowers – credit risk concerns are often a deterrent – many are pulling back.

The Orion team jumped into this underserved market, offering structured loans of $20-100 million with two-to-three-year maturities. It participates in senior, subordinated and junior debt, provides acquisition financing for entrepreneurs and private equity sponsors, and dabbles in special situations. India, Southeast Asia, and offshore China – companies that operate in China but are based in territories like Hong Kong, Singapore, or the Cayman Islands – became the core markets.

The strategy is unchanged, though COVID-19 has arguably accentuated the opportunity set. Private debt providers across the region reported a surge in demand in the early months of the pandemic as revenue-starved businesses sought financing to support ongoing operations. Debt capital markets were largely inaccessible, banks retreated even further, and equity was only available at knockdown valuations. Once deemed too expensive, private debt became an attractive proposition.

Local nuances

"The number of opportunities has grown because of the pandemic, but there are also more localized reasons for rising activity," says Agarwal. "In India, funding is limited because everyone is trying to deleverage, so good mid-cap companies are struggling to get their existing debt refinanced. At the same time, liquidity is tight because the NBFC market is shut for wholesale lending."

Problems in the non-bank financing company (NBFC) space started in late 2018 with the collapse of Infrastructure Leasing & Financial Services (IL&FS). A liquidity crisis ensued as banks – the main source of capital for NBFCs – turned off the taps. Some groups have closed completely, while others decided the economics of wholesale lending were too challenging and are now focusing on areas like consumer lending and housing finance.

"It only worked for NBFCs with 4-5x leverage on your funding. For wholesale lending, with that kind of leverage, it's a very risky model," says Agarwal. "Now people are going down the fund route, using AIFs [alternative investment funds] for wholesale lending. AIFs cannot borrow from banks, so the investor base is more like that of foreign funds. However, they are relatively small."

With less risk capital available, pricing should go up, but this has been mitigated by falling funding costs because of falling interest rates and currency hedging costs. Orion is underwriting to mid-teens IRRs, much like the NBFCs, though it can now target better risk credits. Previously, this segment was dominated by the NBFCs, with funds targeting higher risk, higher return distress and special situations opportunities.

The Orion team – which currently numbers 11, almost all based in Singapore – continues to be active in Southeast Asia because it sees little like-for-like competition in the private debt space. The perennial challenge is whether they are comfortable with the risk. Meanwhile, in offshore China, there is growing interest from groups looking at cross-border deals.

These groups are private equity sponsors as well as corporates. Financing leveraged buyouts has been 40% of Orion's business historically and more capital raised by middle-market managers means increased deal flow. “Leverage normally comes from banks, but there is always a unitranche, a mezzanine piece, or a refinancing available,” Agarwal adds.