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opinion

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Asian High Yield on a supercharge

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About this time last year, bond markets in Asia had kicked off on a buys note. Many market players harboured hopes for a good year; I had especially set my sight on Asian High Yield issuers – referring to issuers who have a credit rating below "BBB" or "Baa" – were on a supercharge trajectory.

And 2017 closed on a high note; it was a landmark year for Asian primary bond markets, with Asia ex Japan issuance volumes reaching US$1.3trillion – slightly higher than the year before and setting a new record as the highest ever for the region. As I had expected too, the High Yield segment stands out, with Asia ex Japan G3 issuance volumes topping US$66 billion in 2017 (a new historical high) and up 175% from the year before. This contrasts with the broader High Yield segment globally which saw a more modest 34% growth from 2016.

That the Asian High Yield G3 markets managed a new record was not quite a surprise. We saw markets open on a tear in 2017, with issuers tapping the market repeatedly throughout the year. This market enthusiasm was mostly driven by near-record low yields and abundant investor liquidity. We saw High Yield spreads (such as the Barclays EM High Yield Index) grinding to some of their tightest levels at the end of 2017, demonstrating strong investor demand and improving risk appetite for the segment. At the same time, emerging markets bond fund flows stayed positive for much of 2017, and we continued to see heavily oversubscribed issuances throughout the year.

Regionally, Greater China accounted for the lion's share of the market, with US$51bn of issuances and accounting for 77% of total volumes. In line with a broader trend among Chinese issuers, offshore transactions were the main driver of volumes, boosted by the resurgence of approvals from Chinese regulators such as the National Development & Reform Commission (NDRC), and the tightening liquidity conditions onshore.

South Asia and ASEAN also registered good growth, with US$5.3 billion (138% growth) and US$6.1 billion (175% growth) in volumes, respectively. Notably, we saw a greater geographical diversity among the ASEAN issuers in 2017. Traditionally, Indonesian issuers accounted for a significant majority. In 2017, however, we saw High Yield issuers such as Malaysia's Press Metal Aluminium and Singapore's Oxley Holdings also tapping the G3 markets.

Sectorally, real estate issuers continued to dominate, accounting for US$31billion in volumes last year (or 46% of total volumes). This number was boosted by jumbo offerings from Chinese issuers such as China Evergrande (over US$8 billion) and Kaisa Group (over US$2 billion).

Commodity names, particularly those from Indonesia, also re-entered the market. Supported by the recovery in coal and oil prices, the market saw issuances from miners such as Indika Energy, ABM Investama, Bukit Makmur Mandiri Utama (BUMA), and oil & gas explorers such as Medco Energi.

While the commodities sector growth was slightly more tepid in India, we nonetheless saw repeat issuers such as Vedanta Resources tapping the markets for US$2billion in bonds last year. A bright spot was the renewables space, which saw repeat issuers such as Greenko, as well as maiden issuers Azure Power Global and ReNew Power Ventures, successfully tapping the market.

Interestingly, 2017 also saw a significant number of High Yield transactions pulled or postponed, with a whopping 15 (mostly Chinese) debut names failing to cross the line in the last quarter, such as Inner Mongolia BaiTou Steel, Sawit Sumbermas Sarana and Concord New Energy Group. Despite the supportive market conditions, investors continued to be selective in the face of abundant issuance supply – an important lesson for would-be issuers.

Given supportive market conditions, we are hopeful that a number of themes will continue in 2018.

Strength of the “Asian bid”: we expect Asian investors to remain a stable source of liquidity, having grown in significance over the past few years. According to Debtwire, 75% of Asia ex Japan High Yield US Dollar bonds were allocated to Asian investors in 2017, up from 53% in 2014. US investors, in contrast, were allocated only 10% last year, compared with 24% in 2014. Clearly, Asian liquidity has enabled issuers to move away from the traditional US investor base in the last few years, thereby achieving greater investor diversity. During this time, Asian investors have gained familiarity with the domestic Asian names, which is helped further by the fact that Asian bonds pay higher yields on average compared to those issued in the West, given the rates environment.

China will continue to drive volumes: Initiatives such as One Belt One Road will also start to bear fruit, with more issuances from sectors related to power and infrastructure coming to market. M&A related funding in the retail, consumer and pharmaceutical sectors may increase as Chinese companies look abroad for growth in 2018. If the onshore rates environment persists, we can expect High Yield issuers (particularly real estate names) to continue refinancing their existing debt offshore.

The potential for Asian High Yield bond market is immense. Whereas China will continue to drive growth, ASEAN has room for more growth. Countries like Vietnam have yet to tap the G3 High Yield market while more could be expected from Singapore, Malaysia and the Philippines. The global investor demand remains exceptionally strong in the meantime. Already, in the first two weeks of January, we have seen almost three times the issuance volumes versus the same period last year. If this momentum keeps up, 2018 will easily be another record year.

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