



IPAF – Pepper Presentation

June 2021

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Profile of Speakers



Ravi Manchanda

Co-Head of Principal Investments – ASEAN & India

- Ravi has over 38 years' experience in South East Asia, Europe and USA as a senior banker and financial services expert.
- Ravi's was also previously CEO of Westpac Singapore amongst other senior management roles in the past.
- He was instrumental in supporting Westpac Singapore exit its portfolio and business
- Advised on a number of Corporate restructurings in Malaysia and portfolios sell-down and restructurings
- Prior to Westpac, Ravi was also with Deutsche Bank and Standard Chartered in the region and has an extensive banking network across Asia.

t +65 6813 3213

m +65 9005 6908

e rmanchanda@pepper-global.com

www.pepper-global.com



Chi-Nang Kong

Co-Head of Principal Investments – ASEAN & Greater China

- Chinang is a senior executive banker and advisor, specializing in financial services and M&A.
- Previously, as the leader of Deloitte's Portfolio Lead Advisory Services business in Asia he has advised banks, globally renowned funds and government agencies in the region on a variety of loan portfolio strategies and transactions.
- He has extensive experience in supporting and advising banks with non-core exits and sale of portfolios including the design of programmatic exits and creation of non core units
- He was also in a senior position with Lloyds Banking Group where he was on the executive committee that designed and delivered the deleveraging of the bank

m +65 9430 3330

e cnkong@pepper-global.com

Introduction

Overview

Pepper Group Summary

Majority owned
by leading global
investment firm

KKR

Lending
Servicing
Advisory

WHO WE ARE

Pepper Group is a global leader in credit-focused alternative solutions. We are specialists in Lending, and Asset Servicing across multiple sectors.

Our diversified funding strategy allows us to respond quickly to market needs with flexible, competitive propositions.

LENDING ASSETS

\$15.6b

TOTAL CUSTOMERS

1.2 million⁺

OUR SERVICING RATINGS

UK: Above Average
S&P: 2018

SERVICING ASSETS TOTAL ASSETS

\$48.5b

\$64.1b

IRE: Above Average
S&P: 2018

AUS: Strong
S&P: 2018

Overview

Where we operate

Ireland Est 2012	Asset servicing
United Kingdom Est 2013	Residential mortgages - firsts & seconds Asset servicing
Spain Est 2013	Point of sale finance Personal loans
South Korea Est 2013	Point of sale finance Personal loans Asset servicing
China & Hong Kong Est 2015	Personal loans Credit cards Asset Servicing
Australia & NZ Est 2000	Residential mortgages Auto & equipment finance Asset servicing
India Est 2019	Asset servicing
Cyprus, Greece Est 2018	Consumer finance Auto and equipment finance Asset servicing
Japan Est 2020	Asset servicing
Singapore Est. 2019	Regional Head Quarters
Indonesia¹ Est 2021	Consumer Finance Asset Servicing



(1) Pepper's Indonesian business is in the process of being established and is not currently in operation.

Overview











What drives our expansion into new markets?



Measures undertaken and hidden danger

Measures taken to counter the impact of COVID – fiscal stimulus and regulatory forbearance

To combat the potential negative impacts of COVID on the banking sector, governments across Asia have unveiled record fiscal stimulus packages. Other key measures taken by the banking regulators include loan moratorium and regulatory forbearance such as assigning zero RWA weight on certain risk cohorts.

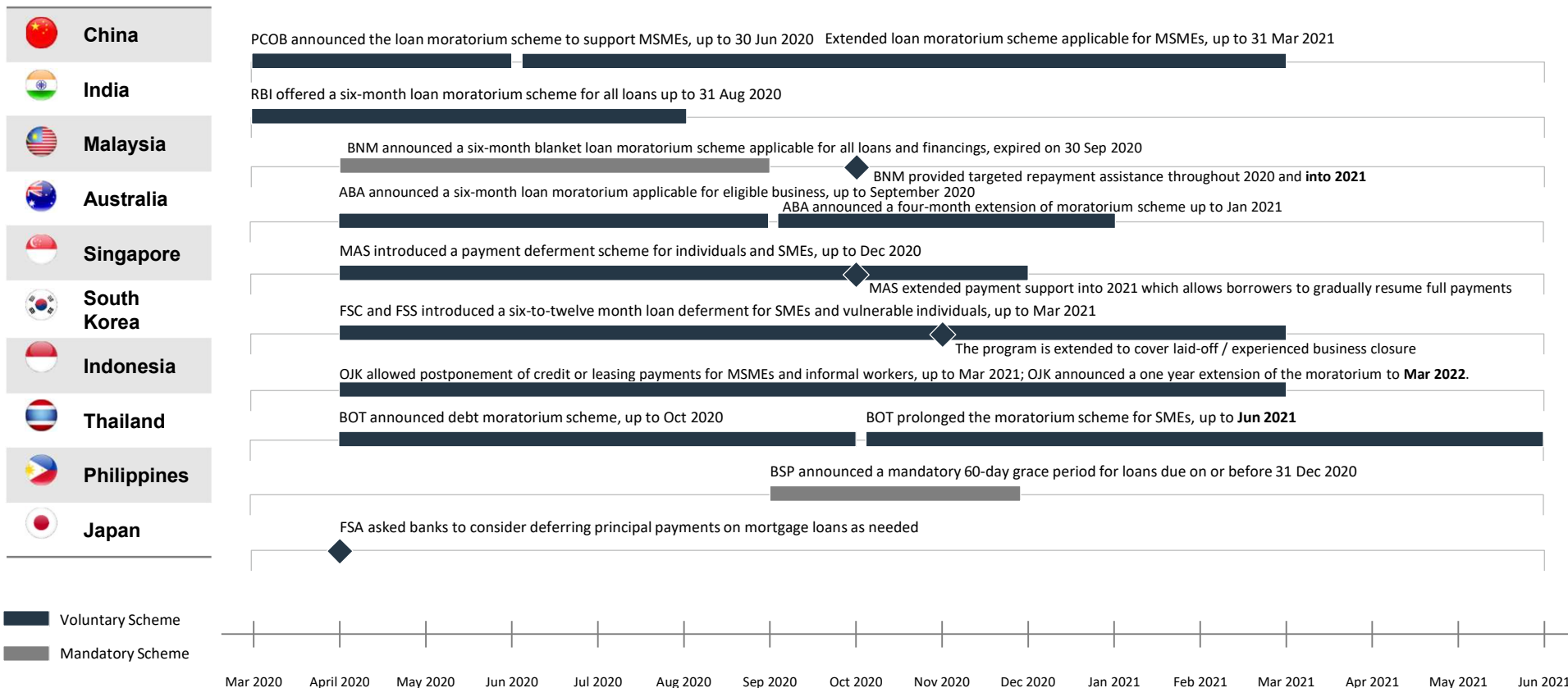
Country	Size of the fiscal stimulus	Easing credit classification / IFRS 9 staging criteria	Lowering reserve requirement / capital requirement	Deferring implementation of Basel III	Allowing zero weight on loans guaranteed by government/public schemes
 Japan	JPY 234.2tr/ USD 2.2tr 46.0% of GDP	✓			✓
 Singapore	SGD 100.0bn/ USD 73.6bn 19.7% of GDP	✓		✓	
 Australia	AUD 273.2bn/ USD 197.9bn 14% of GDP	✓	✓	✓	
 Thailand	THB 1.5tr/ USD 48.1bn 9.6% of GDP	✓			
 India	INR 9.5tr/ USD 126bn 7.1% of GDP	✓	✓	✓	✓
 Malaysia	RM 72.0bn/ USD 17.3bn 4.9% of GDP	✓	✓		
 China	RMB 4.6tr/ USD 677.5bn 4.5% of GDP	✓	✓		
 South Korea	KRW 61.8tr/ USD 55bn 3.4% of GDP	✓		✓	
 Philippines	PHP 595.6bn/ USD 12.3bn 3.1% of GDP	✓	✓		✓
 Indonesia	IDR 438.2tr/ USD 29.8bn 2.8% of GDP	✓	✓		✓

Source: Central Banks, IMF Policy Tracker of Policy Responses to COVID-19 <https://www.imf.org/en/Topics/imf-and-covid19/Policy-Responses-to-COVID-19>, accessed on 9 October 2020

Measures taken to counter the impact of COVID – loan moratorium

Although there is an end date to the moratorium schemes, banks are highly encouraged by the regulators to provide additional payment supports to borrowers impacted by the pandemic. IMF also summarises key policy responses to COVID-19 on their website which we think is invaluable.

Country



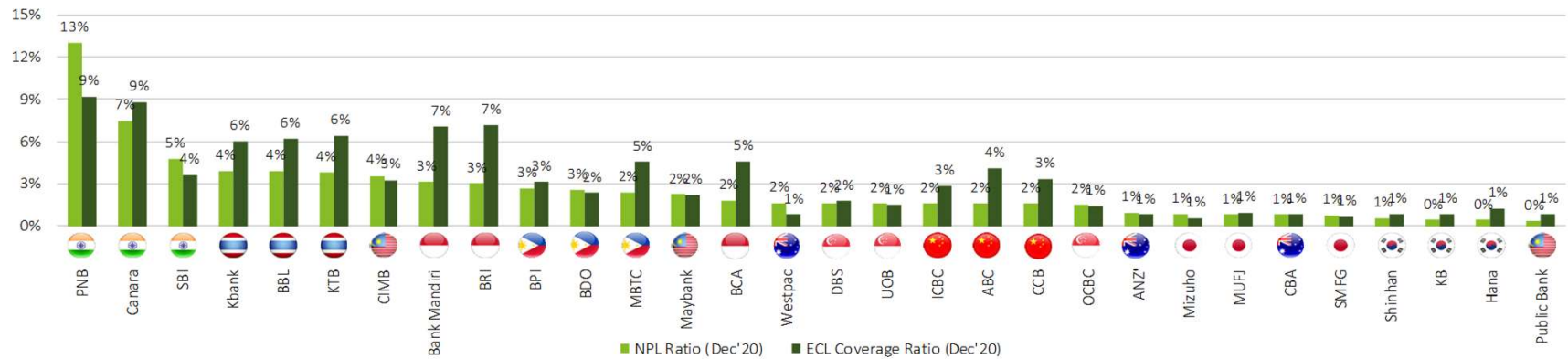
Source: Central Banks, IMF Policy Tracker of Policy Responses to COVID-19 <https://www.imf.org/en/Topics/imf-and-covid19/Policy-Responses-to-COVID-19>, accessed on 13 April 2021.

Provision level has increased

Due to the forward-looking nature of IFRS 9, impairment has increased across major banks in Asia during the year, which resonates with the trends observed in Europe. Some countries, such as the Philippines and Indonesia, are expecting a worse asset quality deterioration than the others, as indicated by the huge jumps in provision and NPLs.

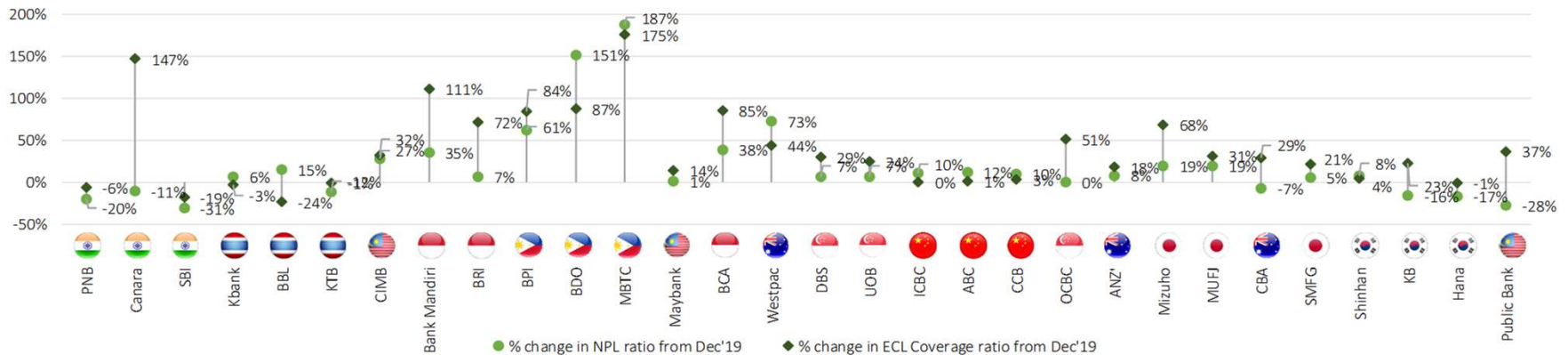
NPL Ratio vs Coverage ratio as at Dec 20

TOP Banks – NPL Ratio vs. ECL Coverage Ratio as at Dec'20



NPL Ratio and Coverage ratio change From Dec'19 to Dec'20

TOP Banks – % increase in NPL Ratio and ECL Coverage Ratio from Dec'19 to Dec'20

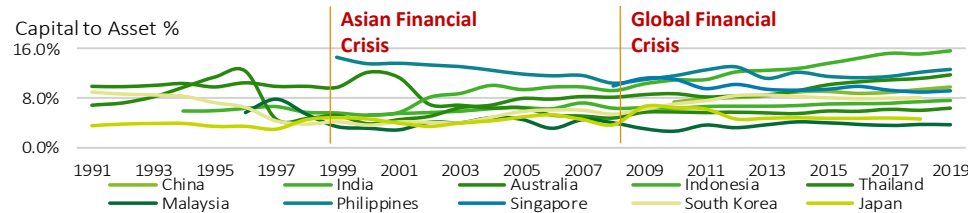


Source: Published financial reports by banks as of December 2020. *Published financial reports by banks as at September 2020.

The emergence and treatment of latent credit risk will vary

Government interventions, especially the loan moratorium schemes and regulatory forbearance, have been a source of significant uncertainty in ECL estimation and stage allocation, with much of the credit risk impacts from the crisis still to occur.

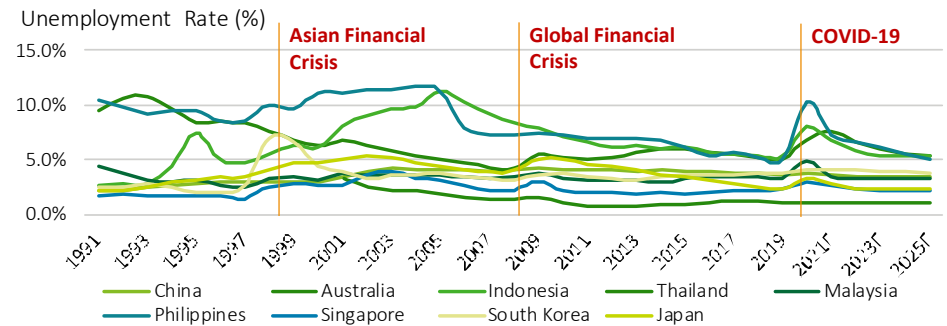
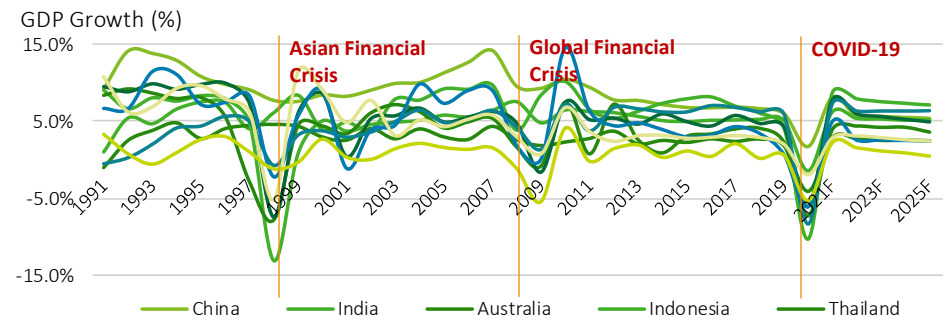
Asian banks are in general better capitalised...



What is hidden...

- Asia has only recently adopted IFRS 9 with some countries yet to follow. Albeit that some good progress has been made, there are still concerns about certain weaknesses in processes, including the inputs and criteria used for staging.
- Due to lack of guidance and uncertainties in recoveries amid the economic downturn, the implementation of ECL model will become even more challenging for the banks.
- Credit risk on lenders' balance sheets is latent, with government support schemes sustaining both retail and corporate borrowers. The moratorium and easing staging criteria in effect would delay the recognition of problem loans, therefore true asset quality of banks and the real number of NPLs might be hidden.
- As the stimulus measures unwind, there could be an increase in bad loans, with Stage 3 loans starting to emerge in Q4 2020 and Q1 2021. A focus on Stage 2/3 triggers for prompt classification and judgement for macroeconomic scenarios are required post-moratorium to cope with uncertainty in ECL estimates.
- As predicted by IMF, the economic fundamentals could be more severely hit by COVID than the Global Financial Crisis in 2008. It is critical to take into consideration the potential impacts when modelling and assessing credit risks.

The economy might be worse hit than previous crises...

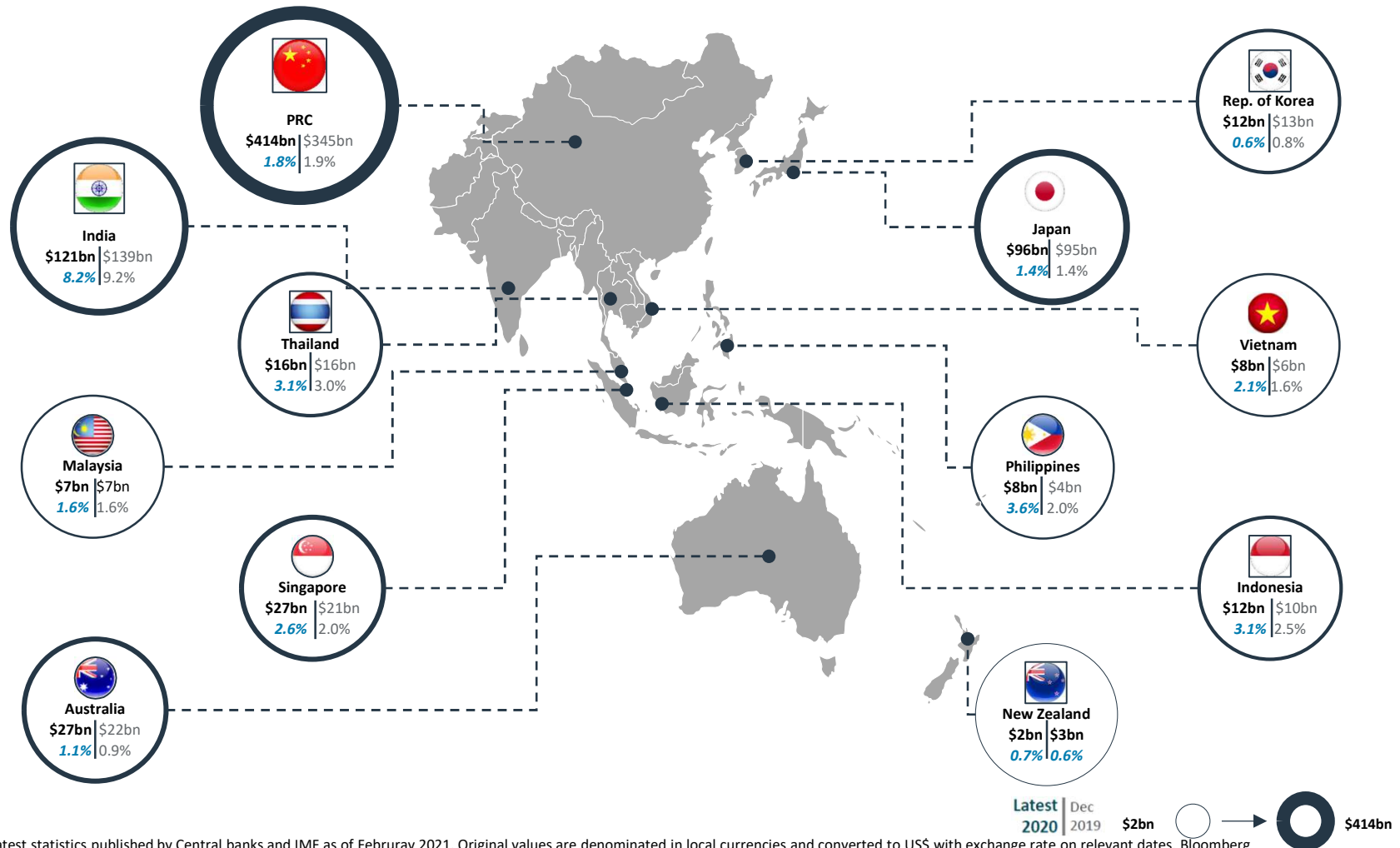


Source: IMF World Economic Outlook, October 2020

Asia NPL Market Landscape

APAC NPL Market Landcape – NPL stock

NPLs held by banks institutions amounted to over c.\$775bn in APAC by end 2020 (\$704bn – 2019), which do not include distressed assets held by AMCS and non-deposit-taking institutions – real levels could be higher. Fitch projects NPLs will double on average across 14 APAC economies* by 2022.



Source: Latest statistics published by Central banks and IMF as of February 2021. Original values are denominated in local currencies and converted to US\$ with exchange rate on relevant dates, Bloomberg

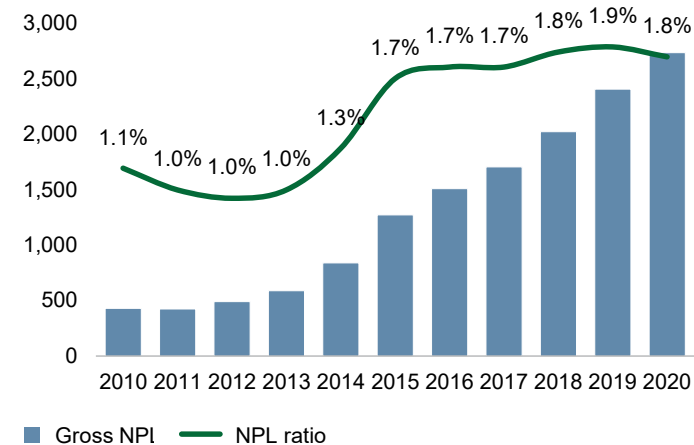
* The 14 economies include Australia, Bangladesh, People's Republic of China (PRC), Hong Kong, China, India, Indonesia, Japan, Republic of Korea, Malaysia, Philippines, Singapore, Sri Lanka, Thailand and Vietnam

Key Markets - China

Chinese NPL market has been developing rapidly in the past few years with foreign investors shifting their focus to the region

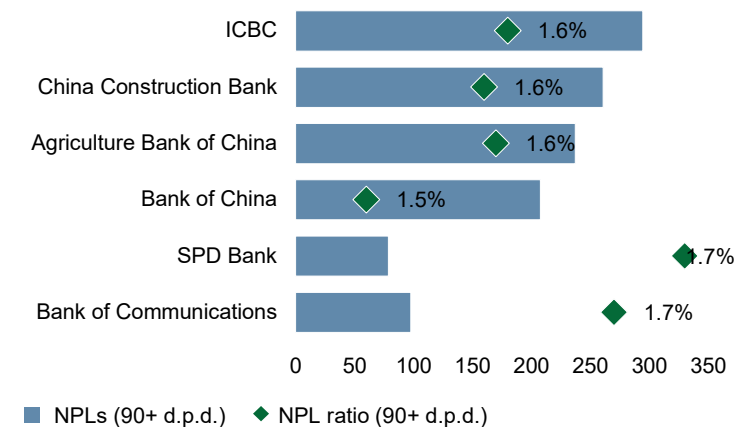
NPL Market Characteristics	
Key figures	<ul style="list-style-type: none"> NPL Stock: USD \$414bn NPL Ratio: 1.8%
Market size	<ul style="list-style-type: none"> Large stock of NPLs - It continues to expand with NPL ratio rising steadily from 1.3% in 2013 to 1.9% in 2020.
Recent Activity	<ul style="list-style-type: none"> Foreign involvement in AMCs – Oaktree Capital set up a wholly owned entity in Beijing seeking direct access to the Chinese NPL market in February 2020. Later in the year, the first licensed AMC with foreign involvement was also set up in Hainan Province by a subsidiary of the Hong Kong-based New World Development. Regulatory change on transfer of consumer NPL portfolios – PBOC initiated a pilot program in 2020 where the participating banks can sell their retail NPLs (secured or unsecured) to licensed AMCs and AIC. The banks participating in the pilot program include six major banks and twelve national joint-stock banks. Record NPL ABS in 2020 – According to Bloomberg China, the total issuance of NPL securitisation products recorded at RMB 28.1bn in 2020, the highest since the approval of the NPL securitisation pilot programme in 2016. 60% of the issuance was completed in Q4 2020.
Servicing	<ul style="list-style-type: none"> Fragmented servicing market – There is a lack of well-established nationwide servicers. Foreign buyers are either building up their own in-house team or partnering with local servicers. However, finding strong local servicers of scale who can perform to international standards remains a key challenge.
Legal Framework	<ul style="list-style-type: none"> Matured legal framework for NPL market – China has been developing relevant regulatory policies for NPL resolution since the establishment of the big four state-owned AMCs. Enforcement timeline may vary – Typical enforcement timeline is around two years, which will vary in different provinces. In spite of a progressive enhancement of the legal framework over the recent years, the enforcement proceedings could exceed the statutory time limits.
Other Challenges	<ul style="list-style-type: none"> Limitation on NPL buyer - Foreign investors are not allowed to acquire NPL portfolios directly from bank, while they only have access to secondary market as over 90% of portfolios go to national AMCs in the primary market Bid-Ask spread – Competition from local investors has driven up prices over the last three years or so, thus limiting foreign investor activity. We expect this however to correct itself.
Outlook	<ul style="list-style-type: none"> Hotspot in Asia NPL market - The growth in the Chinese NPL market is expected to continue

Banking system NPL stock (RMB bn)



Source: CBIRC

Gross NPL held by top banks (RMB bn)



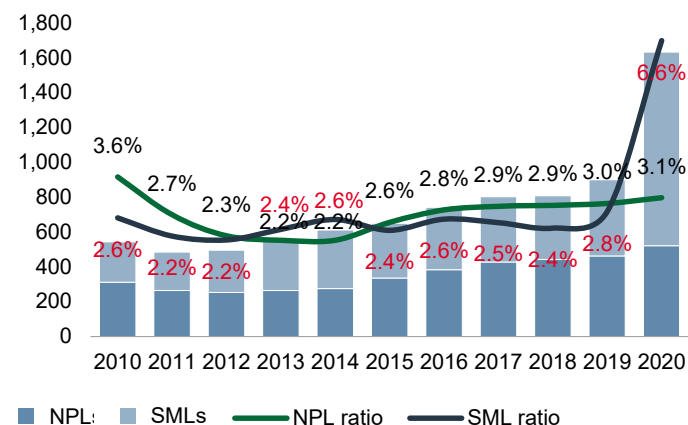
Source: most recent published financial accounts as of December 2020

Key Markets - Thailand

An increasing trend towards SME portfolio is expected with further competition from both domestic players and foreign investors in a relatively mature market

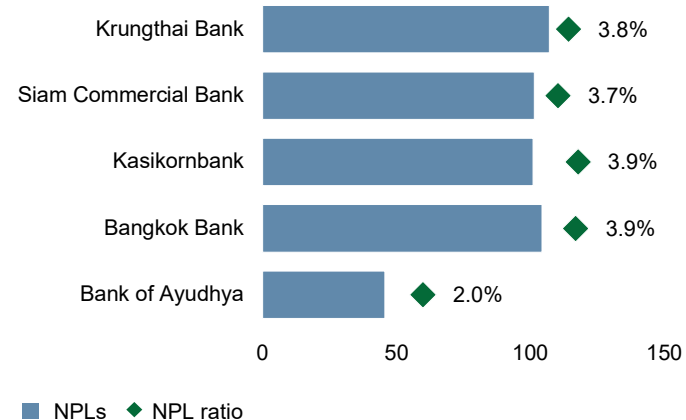
NPL Market Characteristics	
Key figures	<ul style="list-style-type: none"> NPL Stock: USD \$16bn NPL Ratio: 3.1%
Market size	<ul style="list-style-type: none"> NPL growing fast potentially – The volume of NPLs grew, reaching 3.1% of total loans in 2020, compared to 3.0% at the end of 2019. Although NPL figures may seem lower than expected in view of the economic situation, this was due mainly to the BOT's flexible loan classification rules allowing loans restructured under financial aid programmes to be classified as normal, reducing the need to make provisions. Surging Special Mention Loans (SMLs) – SMLs amounted to THB 1.2tr (\$36.4bn), representing a 163.9% increase from 2019 year-end balance.
Recent Activity	<ul style="list-style-type: none"> Extension on repayment help scheme – As the blanket moratorium scheme ended in October 2020, BOT ordered banks to provide targeted assistance to SMEs which are still under financial difficulty until June 2021. The moratorium poses a potential downside risk of deferring recognition of bad loans. When the schemes unwind next year, a significant part of loans might turn non-performing. AMC warehousing solution – BOT studied a warehousing concept later in 2020. It provides an opportunity for commercial banks to sell commercial loans that have been frozen in funds of assets management companies at prices acceptable. As the risk of rising NPLs is currently mitigated by the targeted moratorium scheme, BOT concluded that the national AMC is not needed at this stage. Banks postponing loan sales – Banks, especially private ones, have been selling portfolios of loans regularly over recent years as a mechanism to de-risk their balance sheets. Some major banks in Thailand indicated that they would manage the problem loans internally at the current stage, as opposed to selling them at unfavourable prices amid the current market conditions.
Servicing	<ul style="list-style-type: none"> Relatively developed servicing market – There are certain established servicers in the market at present, which provide services to both local and foreign investors.
Legal Framework	<ul style="list-style-type: none"> Matured market with established legal frameworks – Since the onset of Asian Financial Crisis (ACF) in 1997, Thailand has established and refined its legal frameworks and relevant infrastructures to resolve NPLs.
Other Challenges	<ul style="list-style-type: none"> Restriction on buyers – There is no specific licencing requirement for buyers to purchase NPLs. However, investors who would like to manage NPLs as part of their business scope need to obtain an AMC licence, which is covered by the AMC Decree. Typically, foreign investors will partner with a trusted local partner or apply for an appropriate Foreign Business Licence. Limitation on foreign property ownership – Foreign investors are not permitted to hold land titles in Thailand. They are only allowed to hold up to 49% of the companies who own the land assets.
Outlook	<ul style="list-style-type: none"> The NPL market in Thailand is the most matured in SEA – It is expected to continue growing annually with regular sales from the largest banks. The portfolio tranche sizes are expected to increase as banks take advantage of larger capital providers who have already entered the market

Banking system NPL stock (THB bn)



Source: Bank of Thaila


Gross NPL held by top banks (THB bn)



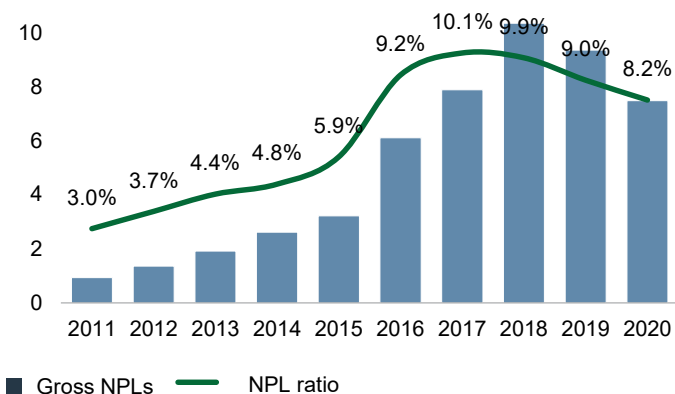
Source: published financial accounts as of December 2020

Key Markets - India

Indian NPL market continues evolving, facilitated by improved regulation and making it the market with the most potential after China

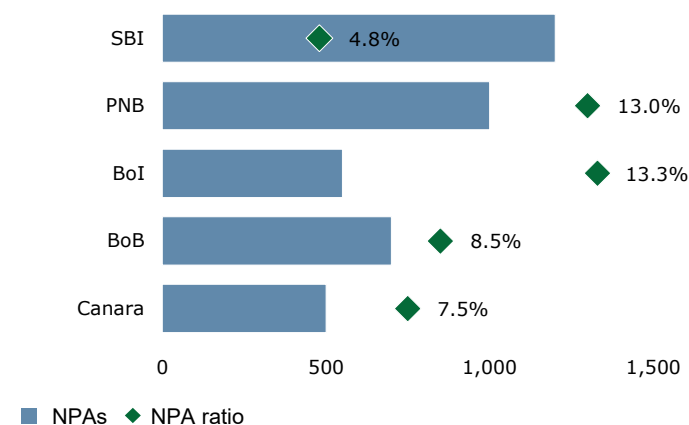
 NPL Market Characteristics	
Key figures	<ul style="list-style-type: none"> NPA Stock: USD \$121bn NPA Ratio: 8.2% Proforma without considering moratoriums, GNPA maybe 13.5%-14.8%
Market size	<ul style="list-style-type: none"> Significant growth in stock - The Indian NPL market has seen a significant increase due to rapid credit expansion between 2006 and 2011 and strict regulations implemented by Reserve Bank of India ("RBI") from 2015
Recent Activity	<ul style="list-style-type: none"> RBI's push – Regulations on NPA recognition, and the time-based provisioning regime, is increasing banks' appetite to dispose of their NPAs ARCs as major players - Transactions of NPLs are mainly made between banks and Asset Reconstruction Companies (ARCs). Since 2016, ARCs can be fully owned by overseas investors Legislation is being mooted for Alternative Investment Funds and FPIs to acquire NPLs. A National ARC to aggregate NPLs of INR 500 Crs and above has been set up.
Servicing	<ul style="list-style-type: none"> Lack of servicers - As FIs prefer in-house servicing, the independent servicing market lacks development
Legal Framework	<ul style="list-style-type: none"> Improved enforcement framework - The Corporate Insolvency Resolution Process (CIRP) was introduced, enabling either the debtor or their financial or operational creditors to initiate insolvency proceedings. The June 2019 RBI Circular outlining the Prudential Framework for Resolution of Stressed Assets. Pre-packs permitted for SMEs.
Other Challenges	<ul style="list-style-type: none"> Challenges in multi-bank lending - It is common for corporate loans in India, which would add to the difficulty in resolution of special sits NPAs Uncertainty in legal framework – Some uncertainties remain as to the amendments in law/regulation.
Outlook	<ul style="list-style-type: none"> NPL market is continuing to evolve - The market attracts increasing interest from investors as the recent enhancements to the country's regulatory frameworks force banks to be more proactive in tackling their stocks of NPAs

Banking system NPA stock (INR tn)



Source: Reserve Bank of India (

Gross NPL held by top banks (INR bn)



Source: published financial accounts as of March 2020

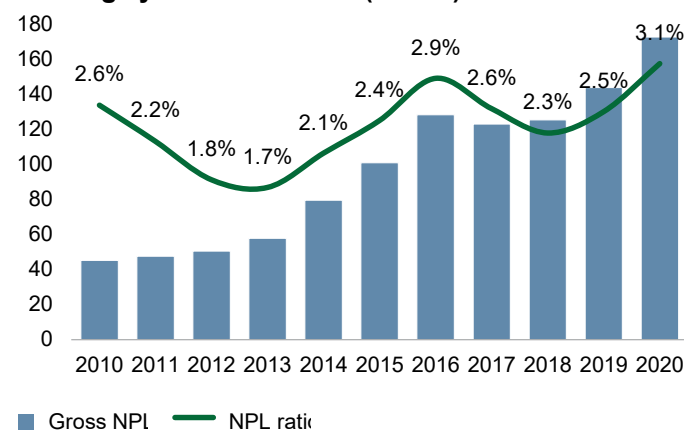
Key Markets - Indonesia

Banks are increasingly seeking for portfolio sales as an effective mechanism to reduce NPL exposures following a few successful disposal over the past years

NPL Market Characteristics

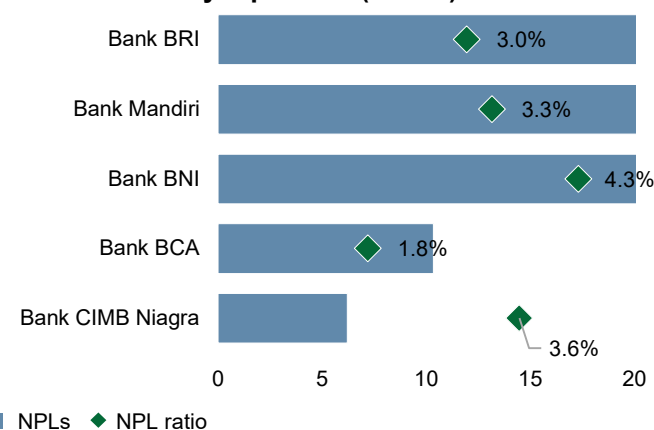
Key figures	<ul style="list-style-type: none"> • NPL Stock: USD \$12bn • NPL Ratio: 3.1%
Market size	<ul style="list-style-type: none"> • Stabilised stocks prior to COVID-19 – The growth in NPLs had been modest in recent years before 2020. However, the downturn catalysed the surge in bad debt stocks and the NPL ratio is approaching 3.1% as of Q4 2020, as reported by Bank Indonesia. The NPL levels are likely to be distorted by the COVID state support schemes and the Public AMC that has been closely cooperating with the largest state-owned banks to manage the problem assets.
Recent Activity	<ul style="list-style-type: none"> • Loan moratorium scheme – To support businesses impacted by the pandemic, in April 2020 the OJK allowed postponement of credit or leasing payments for MSMEs and informal workers, up to March 2021. Subsequently, OJK announced a one year extension of the moratorium to Mar 2022. • Successful transactions – Despite the fact that the NPL market is still at a very early stage, we have seen several deals in the market since 2018, HSBC, CIMB Niaga, Permata, Rabo, etc. • Special Purpose Vehicle (SPV) structure – A number of banks have set up SPVs to warehouse and workout their NPLs in an effort to maintain a healthy balance sheet. However, the banks continue to service these NPLs in most cases. • Potential revival of the AMC – PT Asset Management Company (Persero) (PPA) was set up to manage the assets of the former national AMC, the Indonesian Bank Restructuring Agency. In January 2021, PPA announced its readiness to become the National Asset Management Company (NAMCO), acting as a centre of excellence for the restructuring and management of state-owned assets.
Servicing	<ul style="list-style-type: none"> • Servicing – With the abundance of debt collections agencies, the loan servicing options remain limited in the market due to a lack of specific government guidelines around licensing requirements for servicing companies, making the setup of such an entity challenging.
Legal Framework	<ul style="list-style-type: none"> • No clear guidance on bank NPL deposition – Regulators provides no recommended NPL management approaches and there is some uncertainty around enforcement procedures/portfolio transaction regulations.
Other Challenges	<ul style="list-style-type: none"> • Restrictive regulations on sale of NPLs by state banks – The sale of NPLs by state-owned banks remains challenging as they need to justify that by selling or restructuring their NPLs they do not cause state loss. • Foreign ownership limitations – There are a number of restrictions around foreign entities and individuals not being able to own land plots, maximum foreign ownership set for certain industries (e.g., bamboo and rattan forestry business, fish hatchery, and fishery processing), requirements to partner with local SMEs and for minimum paid up capital when opening a new business.
Outlook	<ul style="list-style-type: none"> • NPL market is expected to be increasingly active - Banks are looking to dispose of their NPL exposures and investors have showed appetite for the market fueled by the successful transactions

Banking system NPL stock (IDR tn)



Source: Bank Indone:


Gross NPL held by top banks (IDR tn)



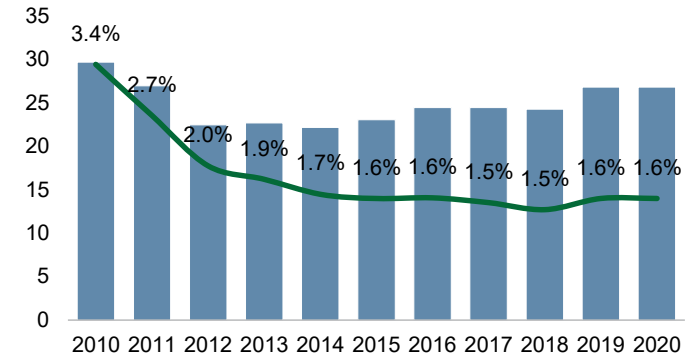
Source: published financial accounts as of December 2020

Key Markets - Malaysia

The NPL market is expected to grow as a result of the implement of IFRS9 and Basel III

 NPL Market Characteristics	
Key figures	<ul style="list-style-type: none"> NPL Stock: USD \$7.2bn NPL Ratio: 1.6%
Market size	<ul style="list-style-type: none"> NPL Stock reaching a record high – as various debt relief measures started to phase out, the impaired loans jumped to a record high of RM 28.7bn (NPL ratio of 1.6%) according to the 2020 year-end figures published by Bank Negara Malaysia (BNM).
Recent Activity	<ul style="list-style-type: none"> Extension of loan moratorium scheme – After the expiry of the six-month mandatory loan moratorium scheme in September, BNM continued to provide targeted repayment assistance throughout 2020 into 2021. As the schemes unwind, a significant part of loans might turn non-performing. Banks are reported to gradually reserve provisions as a pre-emptive measure facing the surge in NPLs. National AMC set-up – According to public sources, the regulator is considering reviving its national AMC Danaharta to bail out troubled businesses reeling from the collapse in the financial markets. Inactive loan sale market – The portfolio sale market in Malaysia has not been historically active. It had seen several small-scale unsecured loan portfolio transaction where banks disposed of their legacy unsecured stock. Few secured NPL portfolio sale were traded, except for the transaction between AmBank and Aiqon Capital in 2019.
Servicing	<ul style="list-style-type: none"> Limited servicing options – Loan servicing in Malaysia are undertaken in-house by AMCs or through DCAs. With respects to portfolios acquired by foreign investors previously, the AMCs would usually be retained to service the debts.
Legal Framework	<ul style="list-style-type: none"> Established legal frameworks – Malaysia has well-established legal and financial frameworks to support the secondary distressed debt market. Typical litigation process takes six to twelve months depending on the nature of the loans and assets.
Other Challenges	<ul style="list-style-type: none"> Restrictive regulations on deal structure – NPL transactions are required to be conducted through SPVs incorporated and tax-resident in Malaysia with foreign ownership capped at 49%. Regulatory requirements – Approval from BNM is required at every stage of the transaction, including due diligence exercise. BNM has strict vetting procedures and scrutiny which are usually undisclosed to market participants. Limitation on foreign property ownership – Foreign entities are not allowed to acquire Bumiputera land or properties, which can only be owned by Bumiputeras. Political uncertainty – State of emergency until August 2021 was announced by the King.
Outlook	<ul style="list-style-type: none"> Unsecured to secured market development – The market is developing through the sale of "low hanging fruit" unsecured NPLs. Regulation is likely to drive banks to consider secured NPLs and non-core assets.

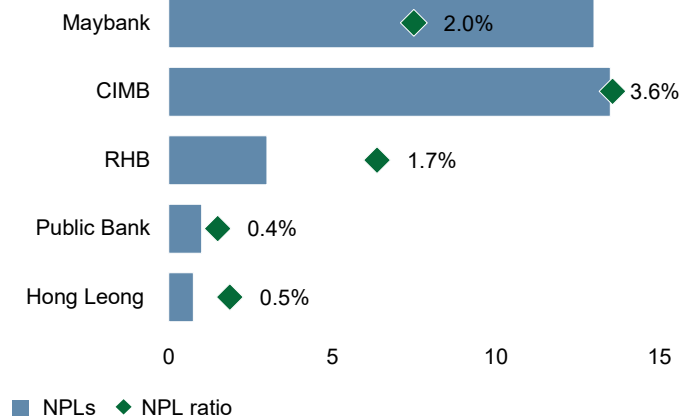
Banking system NPL stock (MYR bn)



■ Gross NPL — NPL ratio

Source: Bank Negara Malay

Gross NPL held by top banks (MYR bn)



■ NPLs ◆ NPL ratio

Source: published financial accounts as of December 2020

The logo for Pepper, featuring the word "pepper" in a white, lowercase, rounded sans-serif font. The letter 'p' is partially filled with a green-to-teal gradient.

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