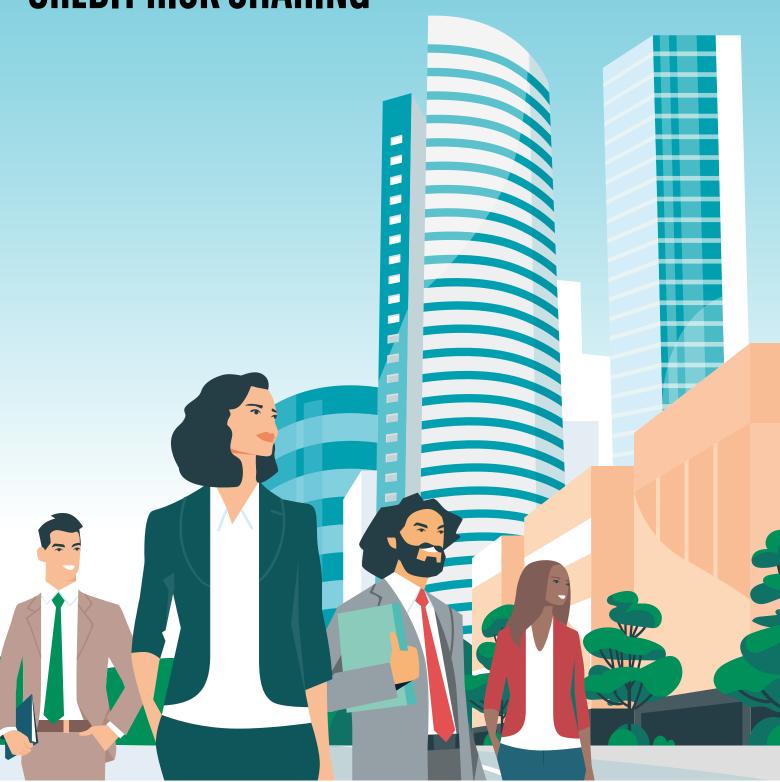
PRIVATE DEBT THROUGH CREDIT RISK SHARING





The sustainable investor for a changing world

PRIVATE DEBT THROUGH CREDIT RISK SHARING

The credit risk sharing (CRS) market opened up in the wake of the financial crisis of 2007-9. It has expanded significantly since then, spurred by changes in European regulations that increased capital requirements on bank lending activities as a means to improve financial stability.

CREDIT RISK SHARING EXPLAINED

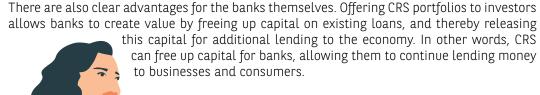
Credit risk sharing describes private transactions where an exposure to part of a bank's balance sheet is offered to institutional investors (via a synthetic securitisation). The bank balance sheet exposure can include a range of different bank lending portfolios, such as corporate and SME loans and real assets lending. In essence, banks are effectively sharing the credit risk attached to these core lending activities.

As the name implies, there is an element of 'risk sharing' to such arrangements, as CRS transactions are exposed to losses within the respective lending portfolio in unexpected and extreme market conditions.

CRS portfolios can include a wide range of private market and private debt lending, including infrastructure debt, large corporate and SME lending, commercial real-estate debt, trade finance and auto loans.

As mentioned, the CRS market opened up following the global financial crisis and has since continued to gather momentum. The more stringent regulations on capital requirements imposed as a result have effectively limited banks' lending capabilities and opened the door for other institutional investors to take on some of the lending. Subsequent regulations, in particular the implementation of Basel II & III, have further incentivised banks to issue CRS arrangements. This has encouraged the growth of CRS as a strategic lending tool across the European banking market.

From a regulatory perspective, robust and well-managed CRS arrangements help ensure efficient capital markets with strong credit risk management in place at a large portfolio level. Notably, CRS transactions are subject to scrutiny and review by bank regulators.





KEY BENEFITS FOR INVESTORS

Credit risk sharing portfolios and funds can offer a number of benefits to institutional investors, particularly in today's uncertain economic climate. They can be effective ways for investors to manage risks, boost returns and increase diversification across a range of risk profiles:

ACCESS

CRS is one of the few ways in which institutional investors can gain exposure to banks' core lending activities. Prior to 2009, this pool of lending was almost entirely serviced by the banking sector.

HIGH-OUALITY CREDIT EXPOSURE

The originating banks have to complete strict credit checks before arranging such transactions, so CRS portfolios tend to offer access to high-quality loans. Given the importance of CRS arrangements to banks, it is in their interest to maintain a regular and successful CRS issuance programme to ensure participation from investors. Moreover, the majority of loans within the bank portfolios have investment grade ratings.

ATTRACTIVE RISK/RETURN PROFILE

The combination of high-quality credit exposure and competitive yields mean that CRS portfolios can offer attractive risk/return profiles for institutional investors. While the high rates may be lead to the transactions being perceived as high risk, it is important to highlight that the rates are not reflective of the quality of the loans within the CRS portfolio, but the need for the bank to obtain capital relief. Notably, CRS investments have exposure to losses only in extreme conditions.

DIVERSIFICATION

CRS portfolios have exposure to a wide range of private market lending, which has historically had very low correlation with traditional listed equity and bond markets. A CRS portfolio can offer exposure to a number of different markets, such as infrastructure debt and SME lending. They also offer the opportunity to diversify across different sectors and geographic regions.

COMPETITIVE YIELDS

CRS investments offer relatively high returns due to the economy of capital achieved by the banks. This can make them appealing options for investors, particularly in recent years when returns on high-quality credit investments have been far lower. This compares favourably with many yields available in the private market/fixed income sector.

STABLE INCOME

Most CRS portfolios offer predictable quarterly cash flows. This can be attractive for investors looking to generate a reliable and stable income from their investments.

DURATION

CRS portfolios typically have a duration of up to six years, average being between three and four years, which is significantly shorter than many direct private market and private debt lending contracts. This can be attractive to institutional investors looking for flexibility and unwilling to tie up capital for too long.

WHY BNP PARIBAS ASSET MANAGEMENT FOR CREDIT RISK SHARING?

BNP Paribas Asset Management's (BNPP AM) CRS strategy leverages the specialist investment teams that comprise the Private Debt and Real Assets (PDRA) investment platform. In addition investors gain access to the origination capabilities of the wider BNP Paribas Group who themselves are a leading CRS issuer. BNPP AM's investment teams are able to leverage the Bank's considerable capital management expertise and intelligence network to source the best opportunities for the benefit of their investors.

Most of these teams have worked in banking, structuring and investment management. This experience enables us to analyse the different lending portfolios banks offer to investors and identify the most attractive CRS opportunities available in terms of both pricing and risk profile. BNPPAM's team of private markets specialists adopts a rigorous investment process when it comes to CRS investment. This involves:

- · Multi-channel sourcing
- Pre-screening of investments based on portfolio and structure characteristics
- In-depth due diligence, including assessment of the bank's credit risk management, lending structure and legal documentation, as well as robust 'stress-testing' to determine how the investment might perform under different economic scenarios
- Decisions overseen by an investment committee and reviewed regularly, both at the investment and portfolio level

At every stage of this process BNPPAM fully integrates Environmental, Social and Governance (ESG) considerations and criteria into our analysis and investment decisions. This applies to private markets investment processes as well as investment into listed equity and bond markets. Working closely with BNPPAM's sustainability centre, the asset manager scores each issuer in relation to stringent ESG criteria. This will relate to a number of topics, for example an originating bank's lending policies and governance.

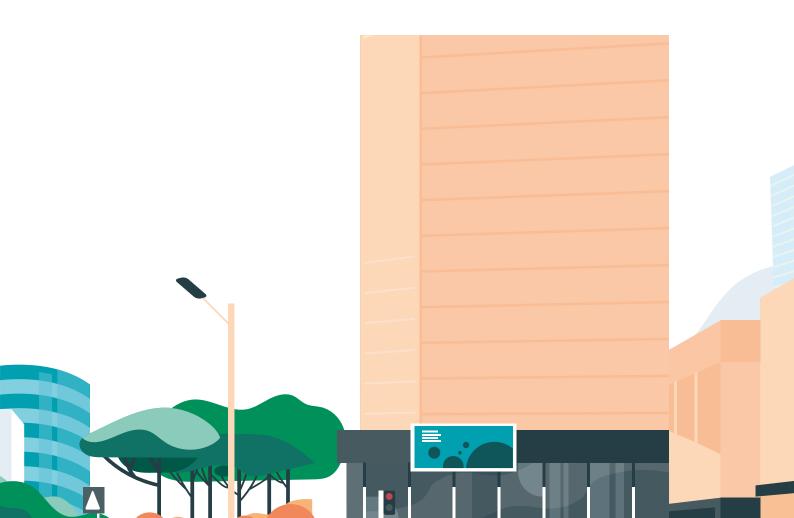


WHY INVEST IN CRS NOW?

CRS can be an attractive investment opportunity.

Many CRS lending options include floating rate notes. These can be more attractive than fixed income options in the current climate, as the income received from a floating rate investment can be linked to base rates, libor rates (or other metric) – so can increase in an environment in which interest rates are rising. Moreover, CRS offers access to high-quality credit options that have historically shown very low levels of default. As these investments are private, there is no mark to market volatility adding to the stability profile. This provides a degree of flexibility over the longer term in unstable economic times.

To conclude, these private market investments can provide stable and reliable income streams that typically require investors to lock money away for a relatively short time period. For banks they are a useful tool with which to manage their credit exposures and capital needs, and for investors they can offer an attractive investment opportunity particularly given the current high-inflationary environment and the likelihood that this will cause interest rates to rise and growth to slow down in many regions.



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