Azalea

ASTREA'S PORTFOLIO CONSTRUCTION PRINCIPLES AND KEY PRODUCT FEATURES

26 Nov 2022 - We read with interest the article by Kaye Wiggins ("Collateralised fund obligations: How private equity securitised itself", Financial Times, 25 Nov 2022), which discussed the features of collateralised fund obligation ("CFO"). We thank Kaye for highlighting the various credit strengths of the Astrea Private Equity ("PE") bonds.

Azalea's mandate is to make PE more accessible to a broader investor group. Azalea has successfully launched five Astrea PE Bonds that allow investors exposure to private equity cash flows without taking on equity risk. Starting with Astrea III in 2016 and most recently, Astrea 7 in 2022, the PE Bonds were distributed to institutions and retail investors.

Each Astrea transaction is designed with bond investors' interests at heart, and investor education has always been a core focus. As such, we believe it would be helpful to reiterate the portfolio construction principles and key product features of Astrea PE Bonds.

Well-diversified Portfolio

The Astrea PE Bonds in each transaction are backed by cash flows from a large, diversified pool of more than 30 seasoned PE funds underpinned by ~600 to 1,000 companies at launch. With this, Astrea bondholders can take comfort from the high level of diversification in the portfolio, instead of focusing on the performance of individual underlying companies that can lead one to lose sight of the strength of a portfolio approach. The high level of diversification ensures that even if some companies underperform, bondholders remain well protected.

Structural Safeguards

Azalea has also designed the Astrea PE Bonds in a CFO structure as it provides better protection to bondholders as the assets are ringfenced and the cash flows are paid out in a pre-determined order. This provides assurance to bondholders as they have priority over the portfolio and its cash flows ahead of the sponsor.

The Astrea PE Bonds were issued at conservative Loan-to-Value ("LTV") ratios to mitigate downside risks of the underlying portfolio. As the sole equity owner, Azalea (instead of bondholders) would bear any first loss arising from the portfolio. Bondholders' risks are further mitigated with other structural safeguards including the regular reserving of bond principal, credit facility to fund interest expense in event of cash flow shortfalls and maximum LTV ratio to ensure debt repayment if breached.

Validation by Internationally Recognised Agencies

The robust structural design and strong cash flows arising from the Astrea portfolios have also been consistently validated by Fitch and S&P, which have rated all of the Astrea PE Bonds investment grade over the years. Post-issuance, the bonds have also received multiple rating upgrades, which is a recognition of the strength and ability of the Astrea portfolios to continue performing across the term of the bonds.

Performance of the Astrea PE Bonds

The Astrea portfolios have performed well with all bond obligations fulfilled to date. All outstanding bonds in Astrea III are fully redeemed. The Class A bonds of Astrea IV are fully reserved, while the Class A bonds of Astrea V are almost fully reserved ahead of schedule.

This is testament to the quality of the portfolios and robust structural safeguards.