

## **BAI Newsletter IV/2021– August 2021**

*Editorial article from Frank Dornseifer*

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### **Private Debt – after the crisis, before regulation**

You know the unanimous statements of institutional investors with regard to their experience with and further investment intentions in the private debt asset class, not least in the Investment Survey 2020. On both counts, it is always “thumbs up”! Expectations have been met and a significant expansion of the allocation is planned. And it fits in perfectly that just last week the data provider PDI registered a peak in Private Debt transaction, namely in Germany!

Throughout Europe and of course throughout Germany, the so-called capital-market based fundings outside the banking sector, which, as you know, includes private debt, belongs now to the most relevant financial components on the markets. Breakthrough has been made and debt funds are playing an increasingly important role in the real economy, especially in financing the growth of small and medium-sized enterprises (SME's), i.e. precisely in areas where lending by traditional banks has declined significantly. Our partner-association ACC amounts a financing gap of around EUR 400 billion for SMEs in the EU, which the Private Debt sector attempt to close. The gap may have increased during the pandemic. It is not without reason that the European Commission - e.g. in the context of the Capital Markets Union - repeatedly emphasises how important capital-market based financing is currently.

Although 2020 was a difficult year, the ACC estimates that the private debt sector has provided around EUR 50 billion of new financial resources for the SMEs within Europe. With it, more than 1000 medium-sized enterprises received new and – in many cases – important liquidity during the pandemic. In other words: loan funds have proven themselves as reliable and long-term funding facility. Correspondingly, the willingness of SMEs to make use of precisely this form of financing has increased. In this context, it should be mentioned that there have probably been no notable failures of individual companies or of the entire sector, neither concerning borrower, investors nor the financial system as a whole. In other words: private debt has passed the litmus-test!

The cross-border lending activities as well as cross-border marketing of loan funds perform within the EU. A recently published record of PDI or Preqin speaks for itself. Nevertheless, or perhaps precisely because of this, there are made clear advances of the European Securities and Markets Authority (ESMA), the European commission and on national levels to regulate and harmonize the activities of loan funds at EU-level. Initial point shall be the upcoming review of the AIFM-directive.

The AIFM-directive – as generally known – provides the legal framework for all AIF-managers, including loan funds. And this framework works. The question is which additional structural measures are necessary that do not already exist or in which areas the authorities and policymakers see structural weaknesses. As I said, the private debt sector has so far coped well with the pandemic and investors continue to remain loyal to managers.

Together with other European associations, we have repeatedly taken a clear position at the European level that AIFMD and national loan fund regimes are – from a regulatory point of view and in respect of financial stability - exceedingly appropriate and that the private debt success story should not be torpedoed. Furthermore, we do not believe that further harmonisations of the framework for fund lending at European level are productive for now. The experience and the discussion surrounding the credit intermediary directive indicates that the intended benefits through a harmonisation to promote market growth will most likely not have an effect because most of the aspects of lending may remain subject to host Member State rules. In Germany, some appropriate regulations of granting loans by funds have been distorted through concretised provisions of supervisory authority in the form of the KaMARisk, which are which are far too closely aligned with the regulatory framework for banks, so that in fact – as a result – hardly any loan funds were launched in Germany. Thus, the German regulation is not capable of competition, namely because of the BaFin regulations. So which impact should create harmony throughout the EU? For example, shall the German regulation, which bypasses the market, be the benchmark in the end? We hope not!

With other European associations, we previously stated that – in absence of evidences for market failure or emerging risks - we are very concerned about the implementation of added European

legal provisions, which, at minimum, increase the uncertainty of institutional investors (which opt for these asset classes) and slow down rather than encourage the allocation of urgently needed capital in times of economic weakness. There's no denying that over-regulated interventions lead to a long-lasting impairment of the capability of the private-debt-sector to provide financial resources. This could result in insolvencies of establishments and a loss of growth and jobs. Caution is advised at this point!

The maturity that private debt has reached is impressive. It covers all of the financial structures as well as, meanwhile, investors are now choosing alternative ways of access like co-investments or secondaries in this area. These are very positive signals which, we hope, the German Federal Ministry of Finance and the European Commission will also take note of.

With this newsletter, we would like - once again and for a given occasion - to take a holistic look at the topic "private debt" and to present you a number of very interesting featured articles.

### **BAI Investor Survey**

Since the Investor Survey 2020 was mentioned at the beginning of this report, I would like to take this opportunity to briefly inform you that we will send the Investor Survey 2021 to our large investor network in the near future. Naturally, we want to build on the success of last year's success, but also to surpass it. Therefore, investors are now being asked to respond to the modified and expanded questions and thus provide all those involved important and new insights, which are extremely important for the direction of our association's work, as well. In order to test the results more closely, we are also launching a member survey. we are also launching an accompanying member survey and are very curious to find out where and to what extent investors and asset managers agree or not!

### **BAI InnovationsDay**

Last week you already received the program of the BAI InnovationsDay, but I would like to mention it here again and invite you to participate in this exciting new format. Because, as you know, it is not only the Sustainable Finance Initiative that is driving our industry "sustainably" or "fundamentally"; the same applies to technology topics such as the use of blockchain technology

or even the use of artificial intelligence. And this is exactly what we are addressing at the BAI InnovationsDay on Thursday, September 30, which we are organizing together with member companies and numerous tech companies and start-ups.

So, join us as we present technological developments in the asset management industry, with a primary focus on digitalization and distributed ledger technology, but also on artificial intelligence and its potential applications along the value chain. In addition to technology, it is now also the accompanying regulation at national and European level that will now change our industry significantly.

The event is divided into three blocks:

- Block DLT - Technology & Regulation, with two discussion rounds on DLT and the mapping of funds and assets in blockchain infrastructures and short presentations on, among other things, the opportunities and risks of DeFi. Furthermore, our cooperation partner Frankfurt School Blockchain Center will present the study on crypto funds.
- The Big Data Artificial Intelligence (BDAI) block, presentations on the application of artificial intelligence in asset management and the use of algorithms in decision-making processes will take place. In addition, a panel on artificial intelligence is planned.
- The third block will feature use cases from various companies, including on "Funds On Chain - Innovative Asset Management Solution according to eWpG", "ISINs for crypto assets (ITIN)" and "360X: The global secondary marketplace for digital assets".

So, take a look at the agenda: <https://www.bvai.de/en/events/bai-innovationsday-2021/agenda>.

## **BAI Trainee Program**

And speaking of innovations, the same can be reported in the area of personnel development for the AI industry. Here, too, our members have already been informed separately about an innovative BAI idea, namely the establishment of a BAI trainee program.

In the future, we would like to promote the recruitment of new qualified employees in the association itself, but also for member companies, through our own trainee program, in which we offer graduates or young professionals the opportunity to get to know different areas and fields of activity in the AI industry, both in the BAI office and at member companies, and to gain initial profound experience. The trainee program is primarily aimed at applicants with a degree in

economics, natural sciences or law (Master's degree) and is designed to last a total of 18 months, with two stations of four to five months each to be completed at member companies.

In a very short time, there has already been very positive feedback and support from the membership. Therefore, we will be launching the first job advertisement for the trainee program in the next few weeks. If you have not yet considered the trainee program, please do so promptly and contact us at the office. We are happy about every member who supports us here as well.

### **To the articles in this newsletter**

Once again, we have succeeded in winning over many member and industry companies for this newsletter, who have contributed top-class specialist articles on the subject of private debt. I would like to take this opportunity to thank them expressly, as well as the companies that have provided worth reading publications on the subject for our main topic on the homepage.

I wish you an informative and entertaining read.

Frank Dornseifer