Para Bellum Advisors

PRIVATE CREDIT · SPECIAL SITUATIONS / DISTRESSED NPLS

Distressed NPL FX Lifecycle Risk – Special Situations Fund

SCENARIO TYPE	Private Credit – Special Situations / Distressed NPLs
ASSET CLASS	Distressed Credit – Multi-jurisdiction NPL Portfolios (SEA / North Asia)
RISK FOCUS	FX drift, delayed conversion loss, repatriation governance, repeatable leakage across vintages
PRIMARY OFFER	Structuring-as-a-Service™
RELEVANT SERVICES	Deal-stage FX structuring · Recovery-schedule hedge alignment · Conversion decision rights · Exception handling · Monitoring and trigger frameworks

THE SITUATION

A Singapore-based special situations credit fund with a decade-long track record acquiring and restructuring non-performing loans across Southeast Asia and North Asia. Their edge was operational – local workout teams, legal navigation across bankruptcy regimes, and creative restructurings that improved recoveries over time.

By 2023, the fund had a problem that did not look like a credit problem. Across Fund III, local currency recoveries were broadly in line with underwriting. The workout machine worked. Yet realised USD returns compressed – not because recoveries failed, but because currencies moved against them while capital sat in local currency forms for longer than underwriting implicitly assumed.

The issue was not FX volatility. It was FX ownership – or more accurately, the absence of it.

HOW THE RISK MANIFESTS

A typical NPL investment looks closed long before it is economically complete. A portfolio can be reported as operationally finished while the fund still holds meaningful local currency exposure in the last mile: delayed conversions, reinvestment holds, quarterly distribution batching, or residual equity stakes awaiting exit.

The fund underwrote a two-year workout and treated FX as a footnote. The investment's FX exposure often stretched three years or more – from LOI pricing through to final repatriation and distribution. USD outcomes were being set by a macro regime shift occurring late in the lifecycle, after the operational value had already been created.

At that stage, FX is no longer a market variable. It becomes a governance variable – who decides, when, and under what policy and the absence of a policy becomes an embedded drag on portfolio returns.

WHAT TYPICALLY BREAKS

FX treated as a single exposure rather than a sequence Funds default to a binary mindset – hedge or don't hedge. In distressed NPLs that framing fails. FX risk changes character as assets move from pricing to workout to exit. Treating it as static guarantees blind spots at every transition.	**Decision rights are mis-specified** Conversion timing often sits with finance or operations while FX risk is assumed to be an investment issue. The result is predictable: batching to save fees, holding balances until quarter-end, and delaying action because no one is explicitly accountable.
Exposure windows become long, uneven, and unpriced Recoveries arrive in lumps. Cash and REO sit idle. Equity stakes wait for exit. FX risk accumulates quietly – not because anyone chose it, but because process delays defaulted into ownership.	**LP challenge risk follows** Once local currency recoveries look strong but USD returns disappoint, LPs ask whether the fund is running a special situations strategy or an unintentional EM FX carry book. That question is very difficult to answer without a documented ownership framework.

THE STRUCTURAL INSIGHT

The fund did not have FX exposures. It had FX exposure windows that changed as deals progressed and no mechanism to manage them consistently across a portfolio.

The response built a repeatable lifecycle framework applicable deal-by-deal. Three windows were formalised with explicit owners: LOI to close (short-dated forward within five days of LOI for deals above a threshold, initiated by the deal team); workout recoveries (hedge design tied to expected recovery schedule, revised as recoveries evolve); and sale to distribution (conversion within 48 business hours, with narrowly defined exceptions requiring named IC delegate approval).

Currencies were then tiered by what was hedgeable – liquid forward markets, partial tenor markets, and illiquid or prohibitive markets – each with distinct default actions rather than a single policy applied uniformly.

A monthly FX lifecycle review was embedded alongside the portfolio workout meeting, with triggers for when hedge schedules must be revised and a simple exception log. This converted FX management from an occasional market view conversation into a controlled lifecycle process embedded in how deals were run.

INTENDED OUTCOMES

- USD returns preserved without changing the workout engine – operational alpha stopped being given back through an unmanaged FX tail.
- Recycling capacity restored – less capital sitting in local currency forms for non-investment reasons, improving ability to act on new opportunities without waiting for currency to cooperate.
- Distribution confidence improved – FX regret ceased to be a recurring internal argument at distribution time.
- LP challenge risk reduced – once FX exposures were explicitly mapped, owned, monitored, and controlled, governance conversations returned to normal portfolio performance discussions.
- Repeatable system for Fund IV – episodic FX pain converted into institutional operating discipline embedded at the process level.

WHERE THIS APPLIES

Most relevant for special situations platforms that acquire assets in local currency but report and distribute in USD; hold mixed recovery forms (cash, REO, equity) with variable exit timing; batch conversions for operational convenience; and have strong workout teams but no dedicated FX ownership model.

Generally less relevant where recoveries are rapid and monetised cleanly inside three to six months; the fund's base currency matches the investment currency; or the platform has a mature FX overlay function with clear conversion authority and policies.

TYPICAL ENGAGEMENT PATH

Structuring-as-a-Service™ – FX Lifecycle Risk and Repatriation Governance. An ongoing structuring function alongside the deal and workout cadence, designing and maintaining FX lifecycle controls across LOI pricing, workout recoveries, and repatriation timing. Secondary: Targeted execution packages – recovery-schedule hedge strips, selective front-end hedging, monitoring integration.