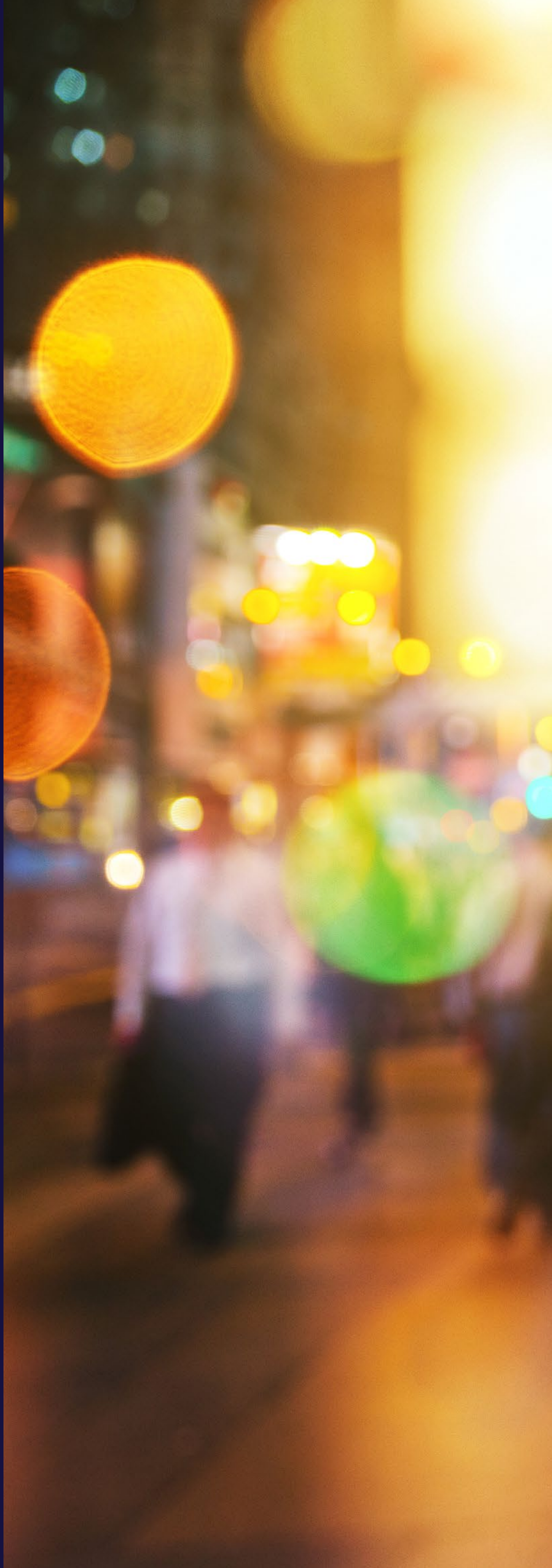
MARCH 2021

NZX Top 50 Funding Composition

Trends & Insights

chapman tripp

Contents



This is the third in Chapman Tripp's yearly NZX Top 50 funding composition series, collating financial information from the annual reports of the New Zealand Main Board (NZX) Top 50.

Our analysis also draws on NZX Main Board announcements and on our own direct experience assisting Top 50 entities with their debt funding requirements during 2020.

2020 snapshot

Banks generally moved quickly to assist their Top 50 customers to weather the Covid storm by agreeing amendments and waivers to their financing arrangements where this was sought.

Top 50 entities that breached financial covenants under non-bank debt arrangements often had more difficulty negotiating waivers and amendments.

Many in the Top 50 opted to increase (or extend) their banking arrangements and/or to raise equity in order to reduce debt levels.

The New Zealand retail bond market remained slow.

In addition, we have tracked year on year trends in regard to:

Top 50 bank facility structures.

The volume and value of New Zealand retail bond and USPP bond issuances.

The diversity of funding arrangements among Top 50 entities.

Method of analysis

Chapman Tripp reviewed the funding sources used by the New Zealand Main Board Top 50, as reported in their annual reports at 31 December 2020. Balance dates vary from 31 March 2020 to 31 December 2020.

The sample comprises the Top 50 at the close of trading on 5 February 2021. Overseas companies listed in New Zealand and any funds listed on the exchange are not included.

Every effort has been made to ensure the accuracy of this publication but the information is necessarily generalised and readers are urged to seek specific advice rather than relying solely on the text.

Banking arrangements

From March to July 2020 – the period incorporating the Covid nationwide lockdown – a large number among the Top 50 engaged their banks seeking a range of amendments, including tenor extensions, facility limit increases and financial covenant relief and amendments.

Some were in breach of their covenants so needed to act quickly. Others were looking to cushion themselves against potential future breaches or other negative effects by requesting covenant flexibility (such as increased headroom or permitting asset sales). Some did not need to draw on the accommodations or increased facilities granted.

Where the majority creditors (typically measured in commitment dollar value) were solely banks, the amendment and waiver process tended to be straightforward as the banks generally sought to support their customers as much as possible – although entities in the hardest hit sectors, such as tourism and retail, where the risks were greater, could face some fairly tough questioning and additional information reporting requirements.

Banks also required some customers to raise equity to bolster their balance sheets. Between March and July, 14 companies raised capital in excess of $5m, of which nine were in the Top 50.

Entities with a range of creditors had a more difficult experience as getting a majority to agree to the same terms was often arduous, time consuming and costly.

- USPP Noteholders were generally supportive of their issuers and worked to find solutions, but their processes typically took longer than the New Zealand banks.
- Trustees for bondholders were sympathetic to the need for waivers but they weren't always able to provide the same level of flexibility as the banks. As far as we know no issuers went to bondholders for consent.

Security structures

47

of the Top 50 have bank debt available to them.

29

have offered security for their debt.

16

(8 of them within the Top 10) have unsecured facilities.

This is consistent with the pattern in 2019 when the equivalent figures were 26 secured and 18 unsecured.

3

entities have no facilities in place.

1 +

has both secured and unsecured facilities. And in two cases, it is not clear from the annual report what the position is.

There is a clear contrast in the security position between the Top 25 of the Top 50 and the second 25, reflecting the superior credit ratings the largest companies have.

14

of the Top 25 have unsecured facilities against just...

2

...in the second 25.

10

in the Top 25 have provided security against 20 in the second 25.

1

in the Top 25 has no debt available.

2

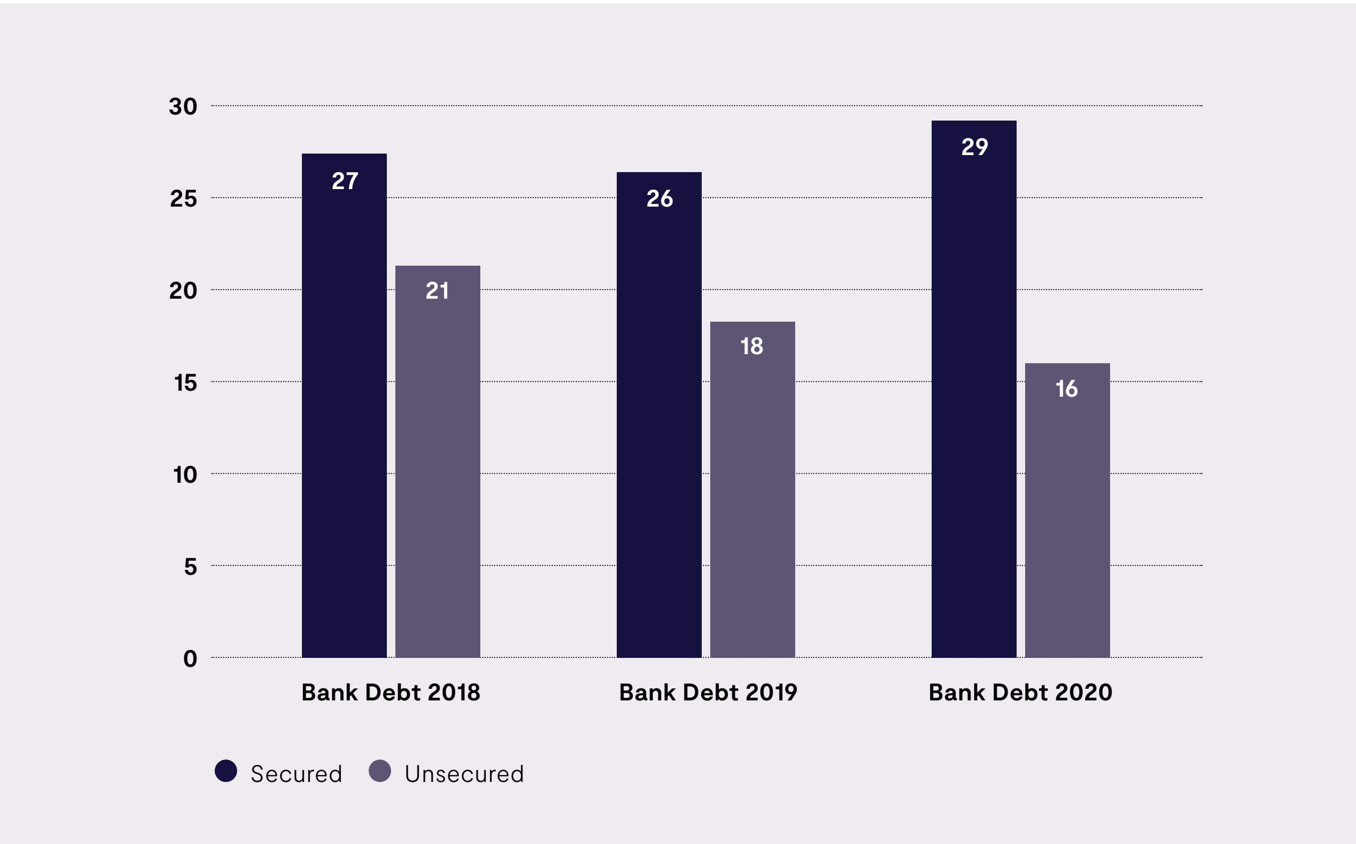
in the second 25 have no debt available to them.

Most of the Top 50 remain heavily reliant on banks as their primary source of debt. But those that have borrowed significant amounts of debt, particularly inside the Top 10 to Top 15 range, tend to have diversity of funding rather than relying solely on banks.

The majority of the Top 50 continue to source bank debt from multiple lenders. Those entities borrowing under unsecured facilities, and as part of club and bilateral arrangements, typically extend to their banks the benefit of a negative pledge and group guarantee deed.

Where there are alternative debt sources available in addition to unsecured facilities, both sets of documents need to be reviewed together to ensure all finance providers have similar terms and protections and so that the borrower does not have multiple reporting or covenant compliance obligations.

Facilities available to the Top 50 over the last three years.



Retail bonds

No New Zealand retail bonds were issued by Top 50 entities in the first half of 2020. Instead the preference was strongly for equity issues, as these are a lower risk and more flexible option in a volatile market.

Breaching financial covenants in bond documentation gives rise to complex consent-based issues. Unlike where a breach occurs under banking documents, the sheer number of bondholders makes it logistically extremely difficult to organise the necessary consents for waivers and amendments.

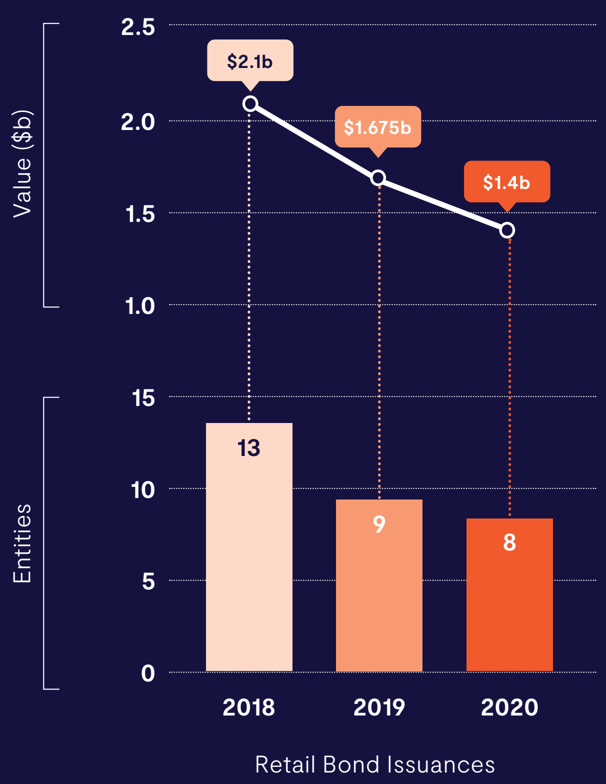
As Covid became the new normal and the financial position of the Top 50 became more stable, investor appetite returned and eight entities (five inside the Top 20) raised a total of $1.4b in retail bond issuance between August and December.

They came from the residential care, infrastructure and energy sectors – each of which was relatively stable through the impact of Covid, either because it was providing an essential service or because it was important to the Government's economic recovery strategy, or both.

Two green bonds were issued by the Top 50 in 2020 – Mercury in September and Argosy Property in October. It was Argosy Property's third green bond issue and Mercury's first. Although they did not issue new retail bonds, Meridian and Precinct retrospectively greened their existing bonds in 2020.

Overall, bond issuance was slightly down in volume and dollar value from 2019, when nine issuers raised a total of $1.675bn (a few of these were post-balance date). We expect to see a slight uptick in 2021, and some Top 50 entities issuing bonds for the first time.

Retail bond activity by the Top 50 over the past three years



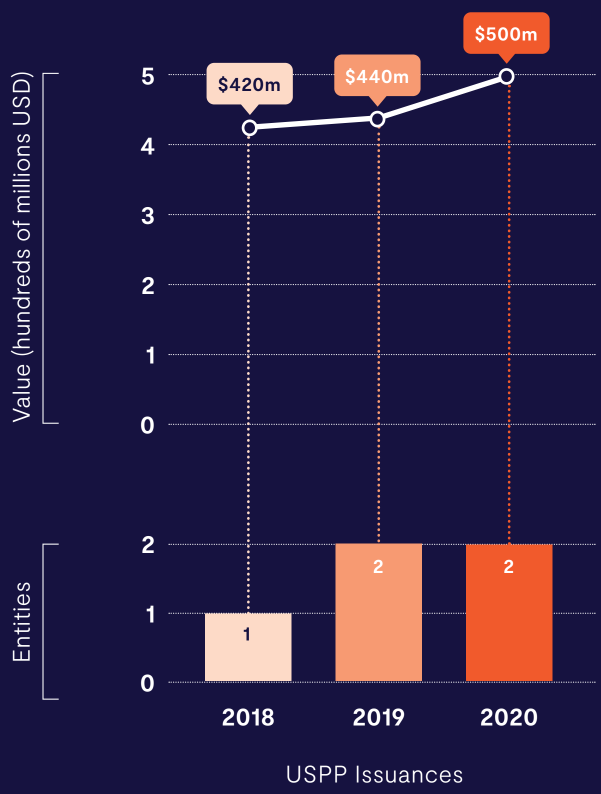
US Private Placement

Top 50 activity in the US Private Placement (USPP) market was very subdued in 2020 – a pattern which was consistent across other countries and across other private placement markets.

The two notable events for Top 50 USPP issuers in New Zealand in 2020 were:

- Vector's US$500m issuance for a tenor between 12-15 years (one of the largest placements by a New Zealand entity for some time), and
- Fletcher Building making an early repayment of their private placement borrowings (maturity was to have occurred in 2022 and 2024).

New Zealand Top 50 entity new-issuance activity in the USPP market since 2018.



Short term and alternative debt instruments

There was limited commentary in the annual reports we reviewed on other alternative debt instruments used but we were able to ascertain that 12 Top 50 entities had issued (at the end of their 2020 financial year) wholesale bonds, Australian medium term notes, European medium term notes or convertible notes.

As reported in our 2020 publication, two Top 50 entities have securitisation programmes.

Six Top 50 entities have borrowed through commercial paper to meet current payment obligations and manage cashflows. All of these entities are from the Top 25.

So what's ahead?

We still expect some uncertainty and challenges this year with borders remaining closed, intermittent lockdowns and a lack of clarity on when vaccines will be widely available. On the other hand, large sectors of the economy are tracking very well and interest rates continue to be low.

Most of the waivers obtained during the initial lockdown last year have now expired so companies will need either to be compliant with their original covenants or to have negotiated new ones. Companies are considering whether their funding mix is appropriate based on their experiences last year. For some that will mean sticking with bank debt and existing accommodative relationships, others will want more options in the face of an economic downturn.

We anticipate that there will be a greater appetite for New Zealand retail bonds to lock in longer term debt. We also expect green and socially responsible financing to continue on its upward trajectory.

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