NZX Top 50 Funding Composition

TRENDS AND INSIGHTS

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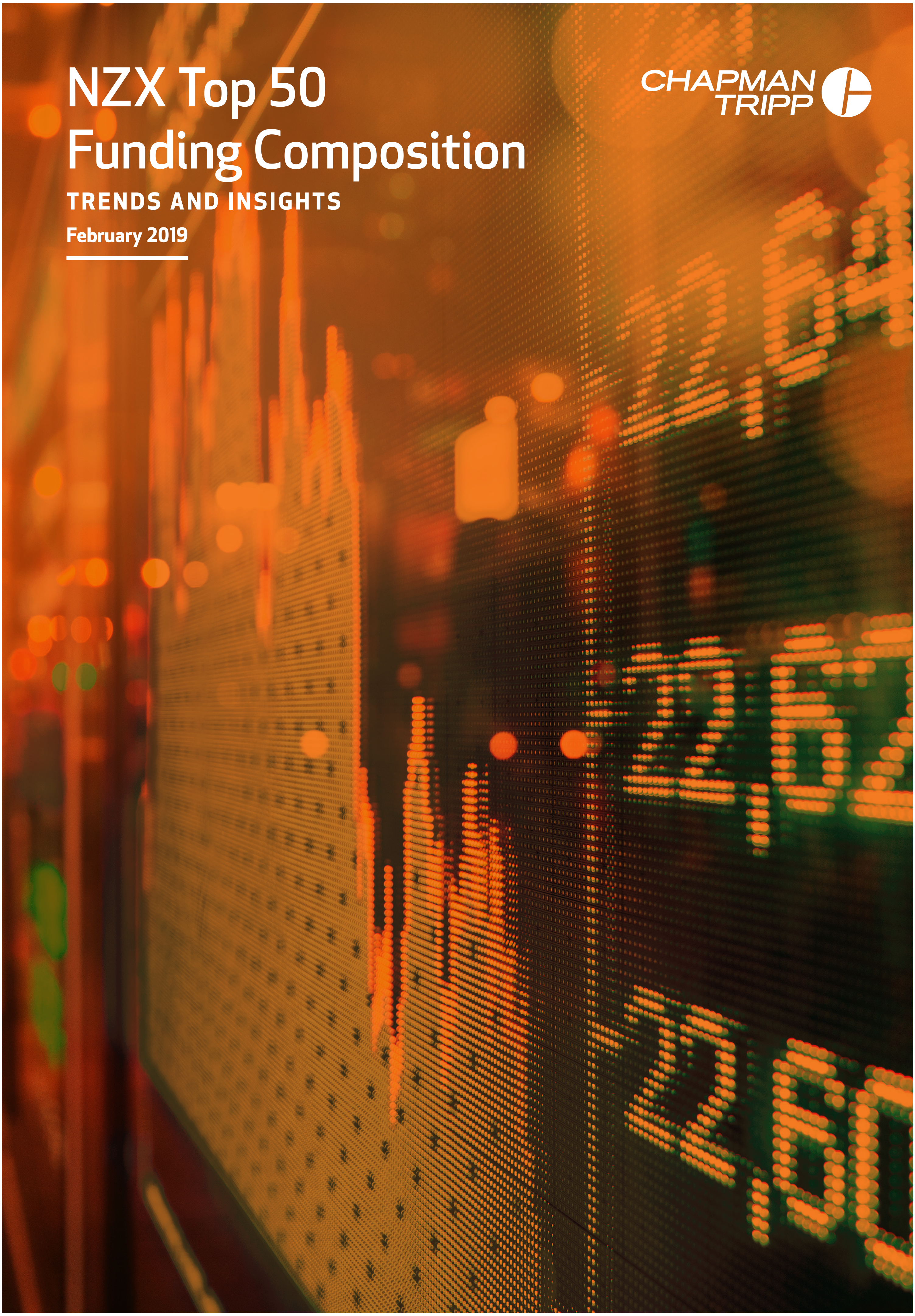
CHAPMAN TRIPP



Alternative sources of funding are here to stay for NZX Top 25 companies

Key insights

1 Most top 25 listed entities have diversified their funding, driven by a more cautious approach to capital by banks in the past few years and higher bank interest rates.

2 Greater diversity of funding sources enables greater resilience against changes in the New Zealand banking market.

3 However, most of the top 25 are likely to continue to obtain a high proportion of their debt from New Zealand banks.

Chapman Tripp reviewed the debt funding mixes of the 50 largest New Zealand entities[1] on the New Zealand Exchange Main Board (*NZX*) as reported in their latest company annual reports.

Our analysis shows good diversity of funding among the top 25 entities. Yet, the second 25 (bar a few exceptions) are entirely dependent on banks for debt funding.

Size matters

The difference between the top 25 New Zealand entities listed on the NZX and the second 25 is stark.

Most of the top 25 have a range of funding sources including New Zealand/Australian and international banks, listed bonds, US private placements and wholesale programmes. Only seven entities are entirely reliant on bank funding. This contrasts with the second 25, where seven entities have non-bank sources of funding, while the rest are entirely reliant on the banks.

A large part of the reason for this is that, while pricing from alternative sources is competitive, the cost and complexity of accessing capital markets and offshore markets can deter smaller issuers. However that is largely a first issuance problem. Subsequent issuances can be considerably cheaper and quicker.

Benefits of other funding

Capital markets and offshore funding is likely to provide a longer tenor than funding available from New Zealand banks, allowing debt maturities to be spread and helping reduce the risk of any short-term liquidity crisis.

Companies that have already accessed non-bank and offshore funding are better placed to return to those markets if bank funding tightens again in New Zealand and Australia.

A diverse mix of debt funding sources mitigates borrowers' concentration risk, and enables companies to deal with changes in New Zealand's banking market – such as margin increases as a result of bank funding costs increasing or the Reserve Bank of New Zealand (*RBNZ*) capital requirements limiting bank appetite.

[1] This analysis excludes overseas companies listed in New Zealand, Fonterra Shareholders Fund and CBL Insurance (in administration). Balance dates vary from 31 December 2017 to 30 September 2018.

Continued debt capital markets activity

The year to 31 December 2018 was busy for debt capital markets.

13 of the top 50 (mostly property and energy companies) raised approximately $2.1b collectively. Two of these entities were first time listed debt issuers – Property for Industry Limited and Investore[2].

The Financial Markets Conduct Act (*FMCA*) QFP regime has made debt capital markets more attractive to issuers as subsequent issuances are time and cost effective. Issuers can get longer tenor debt than the banks are often able to provide and pricing is currently favourable.

Funding mix

PushPay is the only listed company in this group without any debt facilities. Two other issuers – A2 Milk and Briscoes – had no debt drawn at their balance dates but have facilities available.

Top 25 entities

- 18 have listed bonds on issue
- 12 have US private placements, and
- 9 have issued wholesale notes or have commercial paper/MTN programmes.

Second 25

- 5 have issued listed bonds
- 2 have a US private placement, and
- the rest obtain all their debt funding from banks.

Overall

- Only 2 of the top 50 entities have securitisation programmes.

More limited availability of bank funding in 2017-18 and a desire for diversity have motivated a number of listed companies to look elsewhere for some of their debt funding. While bank funding continued to be available in 2018, corporates were very conscious of the need for a range of funding sources.

We predict that in 2019, another 2-3 of these entities will enter the debt capital markets for the first time. However, most entities still obtain a fairly high proportion of their debt from New Zealand banks meaning they remain reliant on banks. That will continue in the next 12 months given the flexibility of bank funding compared to the other sources and the relative ease of obtaining bank funding in New Zealand. This is unlikely to change while bank funding remains readily available.

The trend shows global large companies issuing more bonds and decreasing their dependence on banks. Global economic issues have placed higher capital requirements on banks, and resulted in smaller bank balance sheets forcing larger borrowers to diversify their funding.

At home, the RBNZ has increased capital requirements causing a material change in the availability of bank debt. The fallout from the Royal Commission in Australia may also impact the availability and cost of funding in New Zealand.

We understand almost all of these top 50 entities have more than one bank providing debt funding. This reflects the size of the facilities these companies have, generally a mix of syndicated, club and bilateral arrangements.

Some listed entities have only one bank but we would expect that to change as these businesses grow.

> “More limited availability of bank funding in 2017-18 and a desire for diversity have motivated a number of listed companies to look elsewhere for some of their debt funding.”

[2] Investore's bond was issued post its balance date so isn't included in the other statistics in this article.

Secured vs unsecured bank debt

One of the notable areas of interest is around secured vs unsecured bank debt.

Over half (27) of the top 50 New Zealand listed entities have secured bank debt and 21 have unsecured debt (with one having both secured and unsecured facilities and one having no facilities). Only three of the top 10 have given security for their debt.

Most entities with listed debt have unsecured facilities. The main exception is the listed property sector where the banks, bondholders (other than subordinated bondholders) and, in some cases, USPP investors, all share in the security pool.

Entities which have granted security to banks must decide whether bondholders will also have the benefit of the security or whether to pay a premium for bondholders to accept subordination.

Unsecured facilities are usually only available to borrowers with the highest credit worthiness. The interest rate on an unsecured facility is generally higher than on a secured facility.

NZX Top 50 New Zealand entities at a glance

ONLY **3** SECURED FACILITIES IN TOP 10

27 SECURED, **21** UNSECURED OVERALL (AND **1** WITH BOTH SECURED AND UNSECURED DEBT AND **1** WITH NO FACILITIES)

ONLY **2** HAVE NO DRAWN DEBT

23 HAVE RETAIL BONDS

14 HAVE USPP

9 HAVE WHOLESALE NOTES/CP/MTN PROGRAMMES

2 HAVE SECURITISATION

Chapman Tripp's Finance team

Chapman Tripp is the market leading firm for complex local and international funding programmes, advising major corporates and financial institutions on their most significant arrangements including debt funding arrangements for NZX listed companies.

We act for some of Australasia's most significant corporates, assisting them to finance their activities and business objectives. We are the "go-to" firm for new and complex developments and are known for our input and involvement in designing and implementing some of the most significant transactions in the banking and finance industry in New Zealand.

We regularly assist with the structuring, establishment and ongoing operation of corporate businesses in New Zealand. Our work in this area includes advising on regulatory requirements, preparing regulatory compliant documentation and advising on funding arrangements (both private and public).

Our clients also include local and international banks integral to New Zealand's economy as well as market leading issuers, investors, arrangers and trustees/custodians. This means we understand the issues faced by the majority of participants in the finance market.

This ensures our clients get the most efficient financing structure for their needs and can have confidence that they will receive the highest quality advice in all situations.

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Chapman Tripp is New Zealand's leading full-service commercial law firm, with offices in Auckland, Wellington and Christchurch. Our lawyers are recognised leaders in corporate and commercial, mergers and acquisitions, capital markets, banking and finance, restructuring and insolvency, litigation and dispute resolution, employment, government and public law, intellectual property, telecommunications, real estate and construction, energy and natural resources, and tax law.

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