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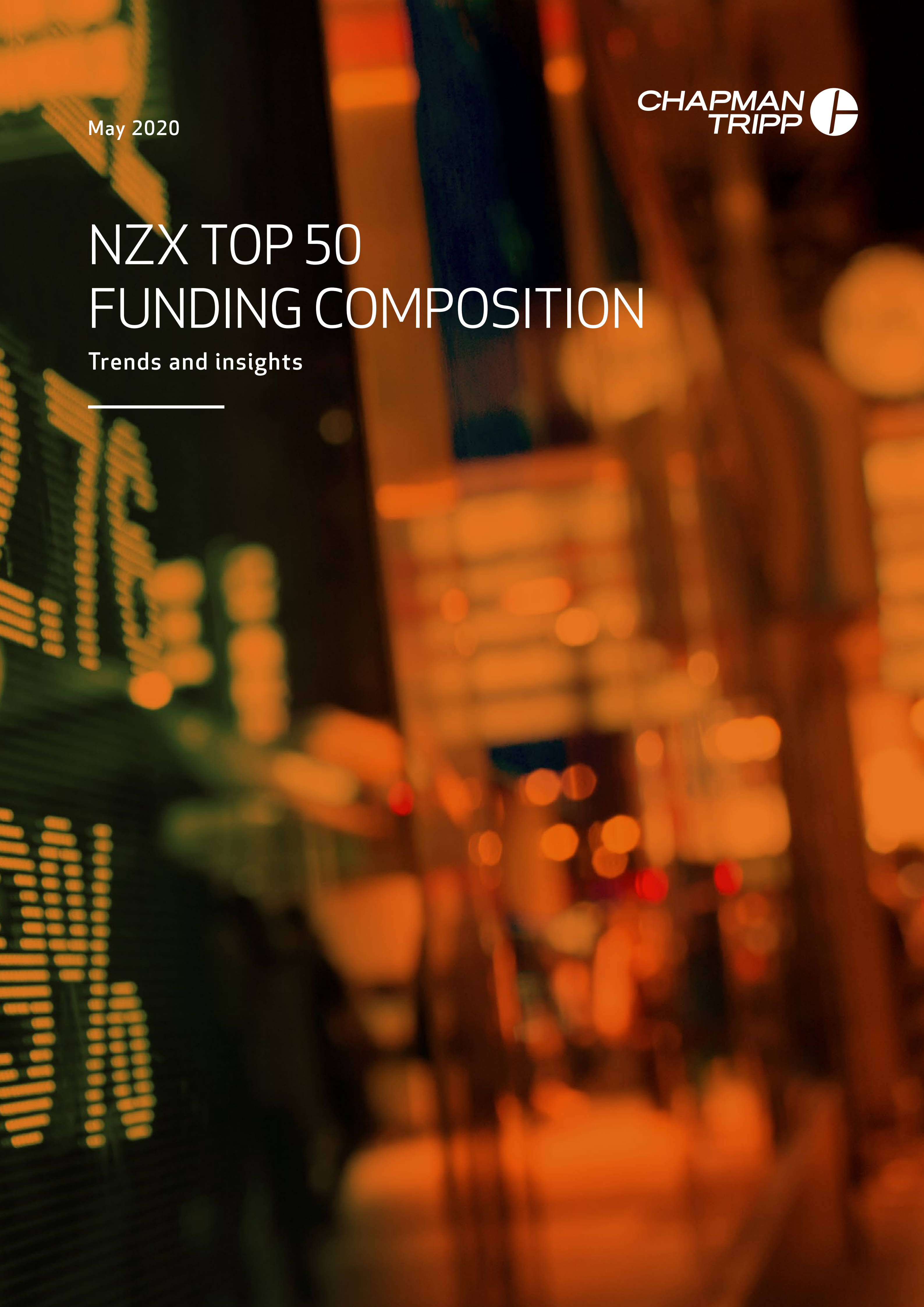

NZX TOP 50 FUNDING COMPOSITION

Trends and insights

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Key insights

This publication collates financial information from the annual reports of the New Zealand Main Board (NZX) Top 50, as at 31 December 2019. We first did this last year with the intention of doing it every year to track trends and developments in corporate financing.

Our analysis shows a large measure of continuity:

- continued diversity of funding sources among the Top 25 and continuing reliance on the banks among the second 25
- little change in the retail bond market either in volume or in the dominance of the property, infrastructure and energy sectors; and
- a slight uptick in green financing.

Beginning in January, it became apparent that the COVID-19 pandemic would bring about challenges to our economy that in many senses are without precedent, and will create corresponding challenges for the financial system. These have prompted a rapid and aggressive range of responses, from governments and central banks in New Zealand and elsewhere. As the lockdown levels begin to ease, the capital markets and broader funding implications of these measures will receive more attention.

Method of analysis

Chapman Tripp reviewed the funding sources used by the New Zealand Main Board (*NZX*) Top 50, as reported in their latest annual reports as at 31 December 2019. Balance dates vary from 25 February 2019 to 31 December 2019.

The sample comprises those entities which constituted the Top 50 as at the close of trading on 31 March 2020. We accept that COVID-19 related volatility has caused, and is causing considerable day-to-day fluctuation in market capitalisations.

Our analysis excludes overseas companies listed in New Zealand and any funds listed on the exchange.

Bank debt

Almost all, 47 of the Top 50, have bank debt available to them.

Over half (26) have offered security for their debt and 18 have unsecured facilities. Of this 18, seven are inside the Top 10.

Three entities have unsecured facilities but had not drawn this debt as at their 2019 balance date. A further three entities had no facilities in place.

Most entities have borrowings from more than one bank (whether on a syndicated, club or bilateral basis). While it isn't always evident in the annual reports which banks have provided the funding, anecdotal evidence suggests an increased use of international banks and credit funds.

Retail bonds

Activity on the New Zealand retail bond market for the 2019 financial year was steady.

Bond issuance continued to be strongest among the property, infrastructure and energy sectors and the number of Top 50 entities with bonds on issue remained at 23, although with some change in the mix.

Six entities raised $1.275b collectively in their 2019 financial year, and a further three raised $405m collectively (but these were issued post-balance date).

The number of repeat issuances indicates that the relatively simple QFP regime has encouraged entities to use listed retail bonds as a viable way to raise debt. We expect this trend to continue as entities become more familiar with the process.

The pandemic has created extreme market uncertainty and volatility both in New Zealand and globally. While recent large offers by highly rated government-sector issuers have provided some hope that the corporate bond markets will re-open in the future, there is not yet any real indication of when that will occur.

USPP market

One area of interest in our analysis is the continued utilisation of the US private placement (*USPP*) market by a number of Top 25 entities. The USPP market is a private US bond market open to both US and non US companies. It typically provides a longer tenor than funding available from New Zealand banks and New Zealand bond issuances, with maturities ranging from five to 20 years (or longer).

Twelve of the Top 25 listed entities have secured long term funding through the USPP market. Most of them are from the property, infrastructure and energy sectors.

In 2019, Precinct Properties borrowed US$110m with maturities of 10 and 12 years (two tranches) and Meridian Energy borrowed US$300m with maturities ranging from 10-15 years (three tranches).

Some of the benefits of borrowing via the USPP market include:

- providing the issuer with the ability to dictate the tenor(s) that best suit its funding requirements
- the opportunity for longer tenor allows the issuer to spread its debt maturities against instruments with shorter term tenors and manage the associated risks
- providing issuers with the ability to raise small or large amounts of capital (issue sizes may range from US$20m to US$1b)
- providing the option to delay drawdown, which allows entities to lock in desired rates and commitments, but delay receiving funds until they are needed

> "While the USPP market has been open for new issuance during the COVID-19 pandemic, widening spreads have generally discouraged New Zealand corporate issuers from participation."

Alternate short and medium term debt instruments

The commercial paper market allows entities to borrow funds from banks for a short term to meet current payment obligations and manage cashflows. Our analysis shows that throughout the 2019 financial year, five Top 25 entities met short term payment obligations through issuing commercial paper. Most of this commercial paper had maturities of three to six months.

We understand four Top 50 entities have issued wholesale bonds, two have issued Australian medium term notes, one has issued euro medium term notes (*EMTNs*) and one has issued convertible notes.

Diversity

A diverse mix of debt funding mitigates concentration risk and typically means healthy spread in respect of debt maturities.

The majority of Top 25 entities have created that diversity, helping them to deal with unprecedented changes due to COVID-19.

Although the second 25 remain dependent primarily on the banking market, recent announcements from the Reserve Bank will assist in bolstering their position.

Multiple financiers can present some challenges when waivers or amendments are required, as many corporates have experienced in the last few weeks.

Many companies have required covenant or material adverse change waivers under their funding documents or amendments to give them longer term flexibility. Generally, these are required from each funding group separately so there is additional time and cost involved in going to each group.

Offshore funders also often have more complex credit processes than the New Zealand banks and their more limited exposure to the New Zealand market means it can take a bit longer to get them to come to the table.

It is very difficult to get waivers or amendments in relation to bond documents, which has put some issuers under pressure.

Green financing

The two "Green Financing" products in the New Zealand market are green bonds and green loans.

- Argosy Property launched its first and second "green bonds" in 2019 to support building upgrades to achieve low carbon impact office, retail and industrial buildings.
- Contact Energy launched a "green bond", as part of its $1.8b Green Borrowing Programme, the proceeds of which will be used for the financing of renewable generation and other eligible assets.

Green finance is typically aligned with one or more internationally recognised standards, with the Green Bond Principles created by the International Capital Markets Association (*ICMA*) and the Climate Bonds Standard frequently used by issuers to determine what qualifies as green financing.

Chapman Tripp has discussed the guidelines, regulations and the potential of green, social and sustainable financing **here** and the options available to corporates to allow them to green their financing **here**.

Impact of COVID-19 and outlook

The impact of COVID-19 has instigated a flurry of responses from the Reserve Bank and the New Zealand Government to ensure the stability and liquidity of the financial system and to assist New Zealand corporates through unprecedented times.

The Reserve Bank:

- cut the official cash rate by 75bps to 0.25% on 16 March
- announced it would undertake a $30b Large Scale Asset Purchase Programme of New Zealand Government bonds on 23 March, and
- On 30 March, committed to holding a weekly Open Market Operation, where it will provide up to $500m for terms of approximately 3 months in exchange for corporate and asset backed securities. This is aimed at providing additional liquidity to strong corporates and to keep funding costs low.

The Reserve Bank has also delayed to July 2021 the start of the increased bank capital requirements and will decide prior to that date whether further delays are needed. It estimates that the delay will allow banks to provide approximately $47b more in loans in the next 12 months.

The Business Finance Guarantee Scheme

This was announced by the Government on 1 April 2020 and is expected to provide $6.25b in loans to the business sector.

It is targeted to businesses with annual revenues of up to $80m. They can apply for loans of up to NZ$500,000 for a maximum term of three years. Applications will be accepted by participating banks until 30 September 2020. The Government will provide a guarantee of 80% of any loss incurred by a bank following failure of the bank's normal enforcement procedures.

The Government announced changes to the scheme on Friday, 1 May 2020. Key among these was the inclusion of agriculture – which is significant given that agricultural lending accounted for 13% of total bank lending in the first quarter of 2020.

These decisions are an attempt to provide financial stability to the New Zealand economy and to maintain healthy liquidity levels in the financial system. Over the next 12 months, we expect to see the Top 50 entities continue to rely on banks for funding, as funding costs remain low and banks have the capital to lend.

To date, the New Zealand banks have been largely supportive of their existing customers, particularly those listed on the NZX. However, they are in some cases requiring additional equity to be raised to pay down debt. We have seen a number of NZX companies raise equity over the last few weeks. It remains to be seen how that support will play out over the coming months.

Funding mix

Top 25 entities

17
have
listed retail
bonds

12
have
US private
placements

12
have raised debt
through wholesale bond issuance, euro or Australian medium term notes and commercial paper.

Second 25 entities

6
have
listed retail
bonds

1
has issued
Australian medium
term notes

The rest obtain all their debt funding from banks

Further points

Only 2
of the top 50 entities have securitisation programmes

3
have
no debt
facilities

3
entities
have no drawn
debt

Chapman Tripp's finance team

Chapman Tripp is the market-leading firm for complex local and international funding programmes, advising major corporate and financial institutions on their most significant arrangements.

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 all 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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