LOCAL ISSUERS, INTERNATIONAL FORMAT

At the same time as more international issuers appear to be looking at international programme formats for their Australian dollar issuance (see p26), so Australian borrowers are contemplating the use of EMTN programmes even for their domestic-currency issuance. Two **Allens Linklaters partners** – **James Darcy**, from Allens in Melbourne, and **Jonathan Horan**, from Linklaters in Hong Kong – discuss the considerations, relative ease and likely future direction of programme selection.

Do you think Australian corporates establishing EMTN programmes is becoming a trend?

DARCY Yes, we've seen a recent uptick in interest from Australian corporates looking to access capital in Asia and Europe through an EMTN programme.

The interest has come from various sectors and there has been a good spread of issuers. We have worked with quite a few property-sector names in both establishing EMTN programmes and issuing – for instance the likes of Vicinity Centres and Lendlease. We've also seen a number of infrastructure companies – especially airports, roads and rail networks – establish and use EMTN programmes. Recently, we've also seen interest from the regulated power and utilities sector.

A key to diversification of course is to be as ready as you can to access the various markets of interest, and recent history tells us that opportunities to access markets can come and go quickly. Increasingly, we are seeing a focus at senior-management and board level on ensuring that issuance opportunities can be taken when presented. This has manifested itself in increased activity in the establishment of EMTN programmes over the past year.

Not all the borrowers that have established programmes have issued as yet – they have built the programmes to be as best prepared as they can. But we have also seen an increase in deal activity in recent times.

> "Increasingly, we are seeing focus on ensuring that issuance opportunities can be taken when presented. This has manifested itself in issuers building flexible programmes capable of being used to access capital from different markets and in different currencies."
>
> JAMES DARCY

What do you believe are the key areas that attract issuers to establishing an EMTN programme?

HORAN As James has mentioned, flexibility is key. Issuers are attracted by the flexibility of being able to use an EMTN programme to access different pools of capital and different currencies.

Some issuers and market participants still consider the EMTN market as a European focused, predominantly euro- and sterling-denominated market. However, we regularly see EMTN trades being marketed and sold in Asia with limited European investor involvement. Indeed, many Asian-origin issuers use their EMTN programmes for Asian-focused trades on a Reg S basis – issuing in US dollars or local Asian currencies such as Singapore dollars, Hong Kong dollars and renminbi. The depth and liquidity of the Asian Reg S market has grown significantly in recent years.

EMTN programmes provide great optionality. Most are set up for multiple currencies, including renminbi, and offer various structures – for instance fixed, floating and index-linked notes. Multiple clearing systems can also be included in addition to the usual Euroclear and Clearstream – including local options in Hong Kong and Singapore.

As an interesting side development, we are also seeing issuers use their existing EMTN programmes for the issue of green bonds. This is what Stockland did in 2014 while, more recently, Bank of China and Link REIT – a Hong Kong-based property company – have followed suit.

Do Australian issuers have to choose to issue EMTNs or domestic bonds, or to maintain two programmes?

DARCY Actually, we are seeing an increasing trend towards building the capability to issue AMTNs off an EMTN programme as an alternative to running both a domestic and an offshore programme. This is particularly so for issuers establishing new programmes, when it's most efficient from a time and cost perspective to create this capability – essentially, future-proofing the programme by making it as flexible as possible. You can of course retrofit AMTN capability into an EMTN programme, but it is best to do it upfront if it suits the issuer's strategic needs.

There are several reasons for taking this approach. A key reason put forward by some arrangers is that global investors are increasingly looking for consistency of disclosure across the markets in which they invest. For an issuer issuing domestically and into the Reg S market, this outcome can most clearly be achieved through using the same programme and disclosure materials.

Some corporates also value the benefit of running just one set of programme documents, from an internal process and administration perspective. There can be cost efficiencies at the time of establishment relative to setting up two programmes.

This is not an approach that suits all issuers – particularly those with existing AMTN programmes. Also, for listed issuers, the disclosure in an AMTN programme will be less extensive and will be drafted in more of an 'evergreen' manner, so should not require much ongoing maintenance if properly established.

Issuers also need to consider that there are certain higher standards in terms of dealer protections in an EMTN programme. There is the potential for these more stringent positions to be transferred into an AMTN deal if a single programme is used.

Let's talk more about the differences that issuers need to be aware of. Exactly what are the higher standards they will find in an EMTN programme?

HORAN The three key areas I'd point out are the disclosure standards, the package of representations and the need for auditor comfort letters.

For listed Australian corporates subject to continuous disclosure, we notice AMTN programmes have a much lighter level of disclosure in the offering document, often drafted in an evergreen manner that usually does not require revisiting from deal to deal.

The expectations in the EMTN market are for the offering document to include a more detailed company profile and a set of risk factors, covering general market risk factors but also company-specific ones. Such disclosure is often derived from other publicly available disclosures for consistency and to reduce the effort for management. General market practice is for EMTN disclosure to be updated annually or at least prior to a drawdown of notes.

Driven by the more substantive disclosure in the offering document for an EMTN programme, arrangers tend to have a more extensive set of business-related representations on the issue date than one might find in an AMTN. This is usually not problematic, though, as the coverage can often be crafted to be consistent with similar domestic bank provisions.

Similarly, issuers should expect a more formal set of due-diligence questions form the arranger group, supporting the consideration of the disclosure and risk factors in the offering document.

Finally, arrangers will expect to receive a comfort letter from the issuer's auditor, confirming the financials contained in the offering document and post-balance movements in key line items. The accounting standard for comfort letters changed a few years ago, causing some disruption in the process of agreeing comfort letters. We have now worked with each of the major accounting firms on Australian EMTN establishments and drawdowns since these changes were made, and market positions have largely been set. The process is now much smoother as a result.

Are there any particular listing venues that Australian corporates are gravitating towards?

DARCY Historically, Australian issuers may have looked towards London or Luxembourg for a listing. Listings in Europe remain popular for Australian financial institutions (FIs) and other issuers with a dual listing.

But a European listing is not a must for investors. Overwhelmingly, the Singapore Exchange (SGX) is the most popular listing sought by Australian non-FI corporates in recent times. Most of the programme establishments we've advised on in recent times have been listed on the SGX. The SGX disclosure regime needs to be understood by the issuer and its board, but our experience is that it does not tend to cause any concern for an Australian Securities Exchange (ASX)-listed entity subject to continuous disclosure.

There are a few exceptions to this trend, though. We've seen one ASX-listed issuer list its EMTN programme on the ASX wholesale debt market, and successfully issue off this programme. There's some attraction to this for an issuer with an ASX listing – a familiar disclosure regime being the key one. Of course, the listing venue needs to be considered in light of the investor base being targeted.

Given the historic links to European and London listing, should we expect any impact on EMTNs from Brexit?

HORAN We have so far seen very little fallout in Asia from the Brexit vote. Clearly there is uncertainty around the timing and the final form of the exit agreement. However, the EMTN Reg S markets in Asia have remained very active over the last few months.

There is no immediate need for substantial amendments to legal documentation as a result of the Brexit vote. Most of the EMTN programmes we are involved in are governed by

English law, and this should remain the case irrespective of Brexit. For issuers with operations in the UK or Europe, adding specific Brexit risk factors in the offering circular needs to be considered. However, we haven't found this to be a particular concern for most Asia-Pacific issuers.

Given the uncertainty, we may see issuers decide to list their programmes in venues other than London. However, as James has mentioned, the more common listing venues for Asian programmes are already Singapore, Hong Kong and – looking forward – potentially the ASX for Australian issuers. Investors are already comfortable with these venues for debt listings.

Another option for issuers is a 144A global programme. What distinction would you make between the two?

HORAN EMTN programmes are typically set up on a Reg S only basis, which means that notes are not marketed into the US. When comparing EMTN standards to a 144A global programme, the key differences are the level of disclosure and the resulting increase in potential liability.

There is a higher level of disclosure required for 144A deals, including a detailed description of financial performance, the "management's discussion and analysis of financial performance" and a more fulsome risk-factors section. Given 144A notes are targeting US investors, there is also additional US liability to issuers and advisers and, as a result, a higher level of due diligence required.

To further the point on EMTN flexibility, programmes can include the legal requirements for a 144A offering – ie clearing through the Depository Trust Company – without the additional levels of disclosure. This has the benefit of having a programme which can be '144A ready' to be used to access the US market with the additional US-style disclosure added only at the time of a particular drawdown.

Having said this, upgrading the disclosure to 144A-standard, and the related increased due diligence, can be time-consuming depending on the issuer and the business. It should certainly be taken into account when planning for a 144A upgrade.

The growing depth of the Reg S market means large drawdowns, of US$1 billion plus, are available for the right issuers. However, for very large deals access to the significant pool of US liquidity through a global offering remains vital. The decision on market access ultimately depends on the individual issuer's fundraising goals.

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What are the structural issues that issuers need to contemplate when considering an EMTN programme?

DARCY A major benefit for issuers in the EMTN market is the relatively covenant-light nature of the securities. Leaving aside certain segments such as infrastructure, the market standard is for notes to be unsecured and to contain only a limited negative pledge restricting secured capital-markets debt.

There are often no other financial covenants required although, for issuers lower down the credit curve, investors will sometimes require additional covenants that may match the domestic banking position.

As a result, EMTN usually offers a significantly lighter package than what issuers will have agreed with their banking syndicates or in the US private-placement (USPP) market. This can provide flexibility – particularly for issuers looking to grow or diversify.

For issuers with a guarantor group structure, the key is to structure the EMTN guarantee in a manner that suits the ongoing profile of the issuer. We have seen several approaches taken to ensure appropriate consistency across markets, limit management effort and to provide flexibility for future acquisitions or divestments.

For secured deals, issuers need to ensure that their security structure is sufficiently flexible to accommodate bonds and bondholder requirements. There are a number of settings in security documents that suit bank debt but are less favourable for bonds – whether issued into the public or USPP markets – for example, mandatory prepayment regimes. It's a whole topic of itself, but one we're talking about to infrastructure clients in particular.

In the current environment, market disruptions and volatility can quickly eliminate alternative fundraising options. As a result, flexibility of funding sources is becoming ever more important. We see a long-term trend of Australian issuers accessing the EMTN markets in Asia and Europe.

Further, as debt-capital-markets standards across Asia converge and investors increasingly expect consistent standards and treatment across the region, the option of combining EMTN programmes with AMTN flexibility seems likely to continue. •