Debt Market Update

Q1 2018

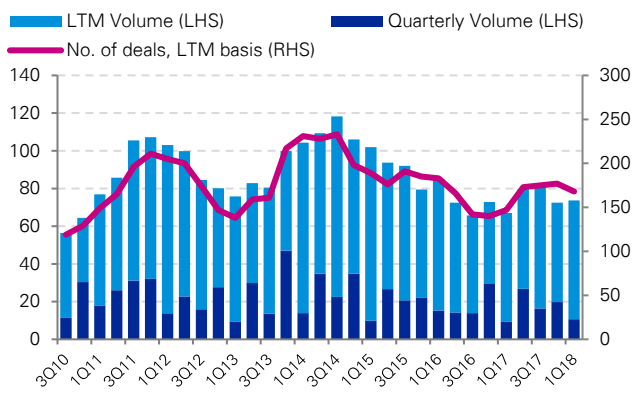
Key themes

- **Australian bank debt market** – expectedly slow start to the year, with the quarter opening with leveraged buyout transactions and more renewable energy projects
- **Australian domestic bond market** – steady opening to the market with issuers continuing to benefit from investor demand, increasingly at longer tenors
- **USPP –** the market continues to work for the domestic borrowers and complement the local markets
- **Robust pipeline** - with several large-scale infrastructure projects in the 2018 pipeline

AUSTRALIAN DOMESTIC BANK DEBT MARKET

Consistent with every opening quarter since 2001, the first calendar quarter of 2018 experienced a decline in the syndicated loan volume compared to the previous quarter as the market returned from holidays and readied itself for the year ahead. When assessed on a rolling 12 month basis, transaction volume increased by 9.9 percent to US$73.6 billion compared to US$67.1 billion in the corresponding period last year showing signs of continued market strength.

Figure 1: Australian syndicated loan volume (US$ billion)



Source: Loan Connector (data extracted April 2018) and KPMG Analysis

A number of large leveraged buyout transactions, renewable energy project financings as well as general purpose corporate (re)financing contributed to the loan volume in Q1 2018. Notable transactions for the quarter included:

- Image Bidco Pty Ltd, the borrower for private equity firm Permira Advisers Ltd launched a A$690 million 5-year year LBO loan to fund its takeover of X-ray provider I-Med Pty Ltd. The opening margins are 375bps over BBSY for amortising term loan and 400bps over BBSY for bullet term and revolver tranches;
- China Merchants became the first Chinese bank to lead the financing of a leveraged buyout in Australia, winning a sole mandate on a A$400 million loan for the acquisition of Real Pet Food Co. The interest margin is 250bps over BBSY, which appears competitively priced, demonstrating strong demand for local credit;
- Sydney Desalination Plant received A$1.6 billion in funding to refinance its existing debt. The deal contains a A$500 million 11-year Ninja loan underwritten by MUFG and syndicated to Japanese lenders. The A$ tranche pays 170bps over BBSY;
- The Murra Warra Wind Farm closed A$320 million 5-year project financing to support the development of the project's first stage (226MW capacity farm in Horsham, VIC). The project is sponsored by RES Australia and Macquarie Capital;
- Infrastructure Capital Group completed a A$124 million 12-year refinancing for the Mumbida Wind Farm acquisition debt, provided by BNP Paribas and CBA on a club basis. The term of the loans goes beyond the expiration of the project's PPA with state utility Water Corp (expiry 2028) and sets a precedence in terms of the duration;
- Bulgana Green Power Hub project (194MW wind farm combined with battery storage) secured A$235 million in project financing in Mar-18. kfW IPEX-Bank is contributing A$101 million of the financing package alongside participation from Societe Generale and the Development Bank of Korea. Project sponsor is Neoen.

(Source: IJGlobal, Inframation and LoanConnector)

Pricing for the above wind farm transactions has not been disclosed, however the market observed recent wind farm transactions pricing around 180bps over BSSY during the construction phase and 165bps over BBSY during operational phase.

Table 1: Notable syndicated loan transactions

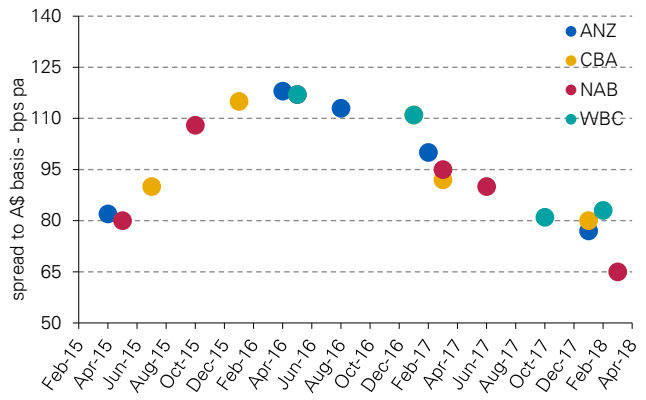
Borrower	Date	Tranche amount (A$m)	Tenor (years)	Margin (bps)
Adani Abbot Point Terminal Pty Ltd	Mar-18	500	5	160
IM Australia Group Pty Ltd	Mar-18	350	4	388
Spotless Group	Mar-18	480	4	155
		280	3	140
Defiance Resources Pty Ltd	Feb-18	85	2.5	350
Oaks Hotels & Resorts Ltd	Feb-18	171	5	164
RPFC Bidco Pty Ltd (Real Pet Food)	Feb-18	400	7	250
SDP Finco Pty Ltd (Sydney Desalination Plant)	Feb-18	680	3	90
		500	5	120
		250	11	170
Southern Cross Austereo Pty Ltd	Jan-18	425	3	180

Source: Loan Connector (data extracted April 2018) and KPMG Analysis

M&A related financing activity in the general corporate space picked up momentum in the quarter. Some of the notable transactions included acquisition loans for (i) takeover of Real Pet Food Co by a Chinese consortium (A$400 million) and (ii) Permira Advisers' takeover of I-Med Pty Ltd (A$690 million).

Loan pricing remains competitive as institutional investors and offshore banks continue to increase their share of lending in the domestic loan market. The Major Banks' domestic new 5 year MTN transactions continue to reduce after a peak period through 2016. While this forms only one cost input in their total funding structure, primary MTN issuance has historically provided a sound gauge of pricing direction in the local bank loan market.

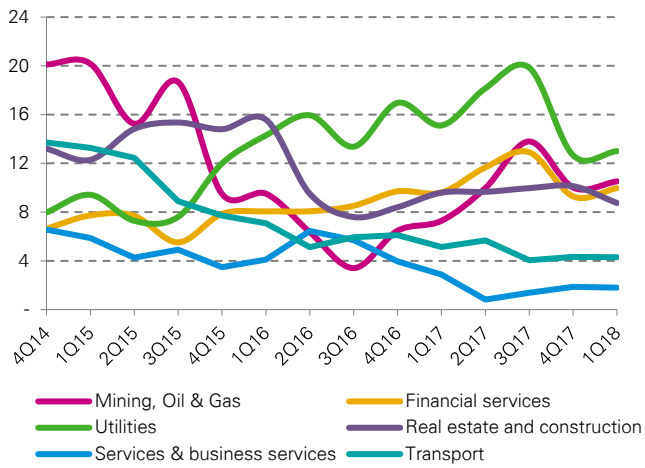
Figure 2: Domestic Major Bank 5-year MTN Primary Issue Margin



Source: Kanganews and KPMG Analysis

In regard to sector performance, the utilities sector continues to be supported by renewable energy project financings. The mining sector saw several refinancing deals including Wiggins Island Coal Export Terminal's 6-year extension of circa A$4.0 billion existing debt.

Figure 3: Australian syndicated loan volume, LTM by sector (US$ billion)

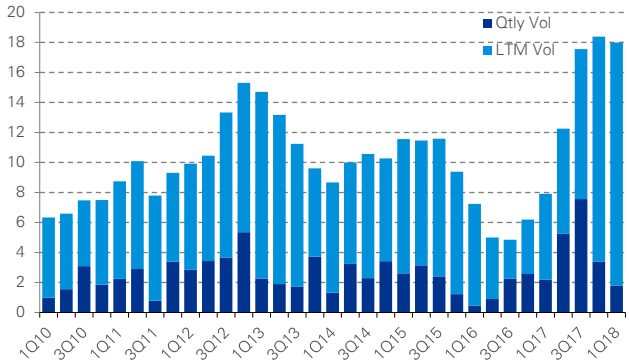


Source: Loan Connector (data extracted April 2018) and KPMG Analysis

AUSTRALIAN DOMESTIC BOND MARKET

Consistent with prior first quarters, the domestic corporate bond market opened slower as borrowers considered their forward funding requirements and focussed on reporting season. Corporate transactions priced during the quarter totalled A$1.8 billion, circa 47 percent lower than the preceding quarter. The Australian / US interest rate differential continues to widen, largely owing to the varying monetary policies of the two countries. This has somewhat caused A$ denominated coupons to appear relatively less attractive, in particular to the Asian fund managers looking for higher yield returns. However, a large number of Asian investors continue to participate in A$ transactions as they seek to diversify their portfolios.

Figure 4: A$ corporate bond market (A$ billion)



Source: Bloomberg (data extracted April 2018) and KPMG Analysis
Note: Criteria has changed, new criteria excludes Financials and Government

Continuing the trend observed in Q2 2017, the recent transactions were dominated by issuers seeking longer dated

funding (AusNet Services: 10.5-year and Victoria Power Networks: 10-year, refer Table 2 for deal size and pricing details).

This quarter saw several repeat domestic issuers open the volume build for 2018:

- AusNet Services raised A$500 million in Feb-18, to refinance its existing debt and fund continued asset base growth. According to KangaNews, AusNet's deal is the third largest 10-year tranche deal and also the mostly tightly priced 10-year corporate issuance (with a margin of 130 bps over swap) post GFC;
- GPT Wholesale Shopping Centre Fund returned to the market 6 months after its last issuance with a 10-year transaction, issuing A$200 million in Feb-18 at 160bps over swap. Books reached A$200 million upon pricing, which was upsized from the initial A$100 million, demonstrating investor demand across long tenors;
- Victoria Power Networks returned to the market with a 10-year A$225 million issue in Mar-18, at almost similar pricing as the previous issue in Aug-17. ANZ, CBA and Mizuho Securities were joint lead arrangers; and
- United Energy Distribution also returned to the market, printing A$400 million to prepay some of its bank facilities ahead of maturity. A recent upgrade in the credit rating by S&P (A- from BBB+), enabled the issuer to achieve a beneficial pricing outcome.

Table 2: Notable corporate bond transactions

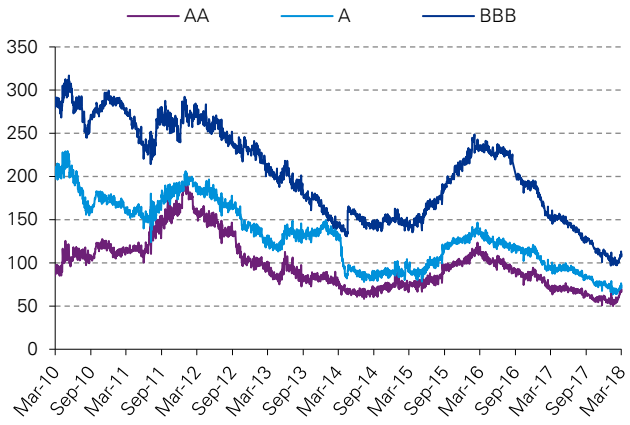
Borrower / Rating	Date	Amount (A$m)	Tenor (Years)	Margin (bps)*
Victoria Power Networks / A-	Mar-18	225	10	133
GPT Wholesale Shopping Centre Fund / A-	Feb-18	200	10	160
Seven Group Holdings / NR	Feb-18	350	7	NA
AusNet Services / A-	Feb-18	500	10.5	130
United Energy Distribution / A-	Jan-18	150	5	97
		250	6	112

The current quarter also saw several domestic issuers accessing a range of off-shore bond markets, capitalising on a number of key benefits available in those markets – including strong demand and transaction volume, longer durations and increased diversification of funding sources. Notable transactions included:

- Scentre Group (A2 / A) raised €500 million 10-year in the EUR EMTN market and
- AusNet printed €161 million 12-year and HK$610 million 15-year EMTN.

The end of the quarter saw widening of the spreads – circa 25-30bps higher than the start of the quarter. Widening of spreads has largely been driven by an increase in global risk sentiment.

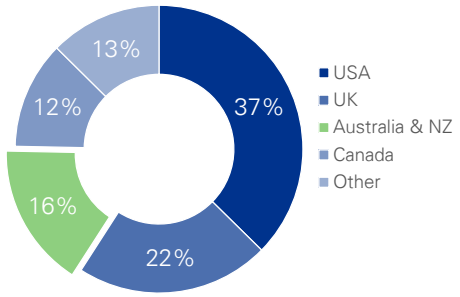
Figure 5: Australian corporate bond 5-year spread to A$ swap (bps)



Source: Bloomberg (data extracted April 2018), KPMG Analysis

US PRIVATE PLACEMENT MARKET

Figure 6: USPP 2018 YTD volume percent by country



Source: Private Placement Monitor (April 2018), KPMG analysis

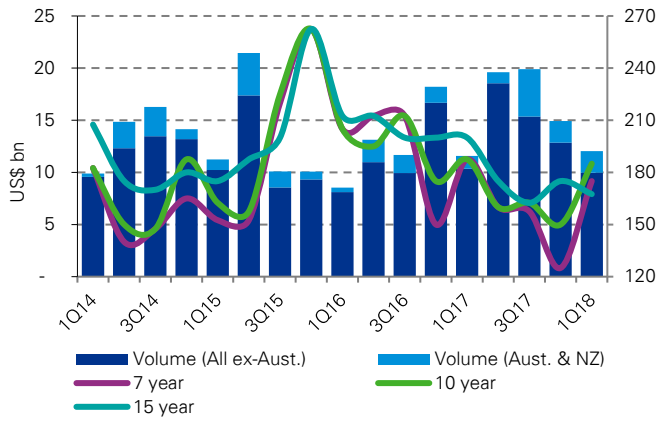
Following large Australian infrastructure privatisation deals completed in CY2017, the USPP market continues to be a preferable and viable alternative funding option for the domestic corporate borrowers. With a total of US$2.1 billion priced in Q1 2018, the USPP market experienced more transaction volume during the quarter compared to the domestic bond market as a number of significantly large transactions were successfully completed.

Notable transactions in 1Q 2018 include:

- Tabcorp's (NAIC – 2 issuer) placement of US$1.4 billion (circa A$1.8 billion), comprising four US$ and two A$ denominated tranches, with maturities ranging from 8 to 18 years. The proceeds will be used to repay the bridge facility in relation to the Tatts acquisition and existing bank debt. Pricing is indicated to be within 180-215 bps over US Treasuries (for US$ tranches) and 235-240 bps over A$ swap (for A$ tranches), respectively (*source: Private Placement Monitor*); and
- NSW Ports raised US$365 million in the longest dated (30-year) US private placement ever for an Australian

issuer in the USPP market. The 30-year A$ tranche was for A$150 million, priced at 140bps over the 30-year US Treasuries (*source: Inframation News*).

Figure 7: USPPs volumes and NAIC-2 pricing (bps (RHS) and US$ billion equivalent (LHS))



Source: Private Placement Monitor, KPMG analysis (data extracted April 2018)

OUTLOOK

We expect non-traditional lenders, including superannuation funds and other institutions, to remain active in the bank loan market. Corporate borrowers will remain supported in transaction volume and competitive terms, especially in the high quality infrastructure assets.

The results of the current Royal Banking Commission are yet to be known, however additional bank oversight and regulation could arise. In turn, this may soften the competitive position currently enjoyed by the major banks, increasing the viability of alternative lenders and markets as borrowers explore further diversification.

The local corporate bond market is expected to further develop in terms of long-dated tenors, volume and investor diversity. The market continues to meet issuer requirements and has proven its ability to provide local and reliable funding diversification at tenors up to 10 years.

While the global market volatility remains, the resilient USPP market continues to display stable and favourable conditions for the Australian corporate issuers. Expect this mainstay market to remain a preferable funding market for issuers looking to achieve tenor, diversification and volume certainty.

Our Global Debt Advisory offices

KPMG's global Debt Advisory Services of 110 professionals helps our clients achieve optimal financing outcomes across the entire spectrum of debt products.

KPMG CONTACTS

David Heathcote
Partner
Sydney
+61 2 9335 7193
dheathcote@kpmg.com.au

Scott Mesley
Partner
Melbourne
+61 3 9288 6748
smesley@kpmg.com.au

John Barry
Partner
Melbourne
+61 3 9288 6876
johnbarry@kpmg.com.au

Greg Eldridge
Director
Melbourne
+61 3 9288 5759
geldridge@kpmg.com.au

Conrad Hall
Director
Brisbane
+61 7 3434 9105
conradhall@kpmg.com.au

Matt McKenna
Director
Sydney
+61 2 9295 3878
mmckenna1@kpmg.com.au

Tony Moussa
Director
Sydney
+61 2 9455 9842
tonymoussa@kpmg.com.au

Ian O'Brien
Director
Perth
+61 8 9413 7926
lobrien2@kpmg.com.au

KPMG.com.au