

NAB: INNOVATION PAYS DEAL DIVIDENDS

Innovation, especially the ability to devise and deliver innovative funding and capital solutions for clients, is a driving force at **National Australia Bank (NAB)**. Together with key members of her team, **Connie Sokaris**, general manager, investment-grade originations at NAB in Sydney, discusses how innovation is paying dividends for the bank and its clients – through the lens of a range of key transactions.

■ **NAB topped the *KangaNews* intermediary league table for Australian corporate deals again in Q1 2015, having finished 2014 in pole position. It is often said that getting to the top is one challenge but staying there is quite another. Is there more to it than just continuing what you have been doing?**

SOKARIS Absolutely. Standing still is not an option for our clients in the way they operate their businesses, which means it's also not an option for us.

We have embedded a model which is based around the client. This means our specialists and economists, as well as our market insights, all revolve around the client rather than sitting in their own silos. We're also continuing to find innovative ways to bring issuers and investors together. Being a local bank with a global focus means this includes bringing Australian issuers together with global investors.

■ **We talked last year for a profile published in the September issue of *KangaNews* about how the innovative way NAB has structured its debt capital markets business is helping the bank be a market leader in delivering funding and capital solutions to clients. This strategy has now been in place for two years. How has it been refined in response to real-world experiences?**

SOKARIS The important thing we have learned is what our core strengths are across the business, and how we can leverage off these strengths for each client engagement.

DEAL CAPABILITY: **AUSTRALIAN DOLLAR CORPORATE BONDS**

WHO? BHP Billiton Finance

WHAT? Five-year Australian dollar fixed-rate MTN

WHEN? March 2015

HOW MUCH? A\$1 billion

NAB ROLE: Joint bookrunner and joint lead manager

KEY INNOVATION: Equalling the largest deal size in the Australian corporate market despite the backdrop of a commodity downturn.

Australia's corporate bond market has taken significant forward steps since the financial crisis. But there is still a long way to go before the broad swathe of local corporate treasurers consider it to be a reliable, consistent and sizeable source of long-term debt funding.

In this context, the decision of issuers like BHP Billiton Finance (BHP Billiton) – not just a keystone name in Australia but a true global giant – to use the Australian dollar option is a big win for the local market.

National Australia Bank (NAB) was able to help BHP Billiton price A\$1 billion (US\$767.8 million) of five-year bonds in March 2015, matching the issuer's own record for the largest-ever Australian dollar corporate deal.

Brad Scott, head of corporate bond origination, Australia at NAB, is quick to point out that the issuer's premier global status helped it overcome a challenging environment for the resources sector as a whole to achieve the transaction's result. "We were highly confident BHP Billiton would

receive a superior response from debt investors in any market conditions," Scott comments. "The reason for this confidence is the company's substantial portfolio diversification and long-life and low-cost assets, matched by BHP Billiton's strong financial flexibility. It really is in a class of its own."

Although Scott says BHP Billiton's jumbo deal size is likely still an outlier – he suggests A\$500 million as a more achievable goal for regular transaction outcomes – he also points out that NAB has been successful in broadening the appeal of the corporate bond market to attract a wider range of investors by ticket size and geography.

"We are seeing a broader array of investors coming into deals, from Asia and elsewhere – such as non-institutional accounts. This has enhanced deal sizes and, at times, sharpened final pricing outcomes," Scott reveals. "Order books can often include up to 50-60 investors nowadays, and this means we're less reliant on a smaller number of big investors to drive large deals than in days past."

This isn't about refining the business model, but how the business responds to how the world is changing. We believe

we see the market better because of our strong deal capabilities and the way we collaborate as a team. To maintain this,

DEAL CAPABILITY: **INNOVATIVE LOAN ARRANGEMENTS**

WHO? Tasman Aviation Enterprises

WHAT? Dual-tranche loan financing for management buyout

WHEN? April 2015

HOW MUCH? A\$31.5 million as part of a A\$35 million buyout

NAB ROLE: Senior lender and arranger of subordinated debt

KEY INNOVATION: New means of funding buyouts without ceding control of company.

The management of Tasman Aviation Enterprises (TAE) was facing a difficult situation: it wanted to complete a buyout from the existing owner, Air New Zealand, but did not have sufficient access to sub-senior capital to do so. A solution would be to seek private-equity support, but doing so would likely involve losing control.

National Australia Bank (NAB) was willing to act as the senior lender to the bought-out company – and did so to the tune of A\$18.0 million (US\$13.8 million). But holding subordinated debt or equity on balance sheet was not appropriate for the bank.

NAB's capital finance team was able to locate a fund in Asia which was willing to lend to the buyout group on a subordinated basis. The A\$13.5 million provided in this format allowed TAE's management to retain control with its A\$3.5 million equity stake.

Tom Mazzaferro, general manager, specialised finance at NAB, says: "There is no way this buyout would

have been achieved without the debt capital markets piece. The injection of sub debt was critical to allowing management to complete the transaction without losing control."

The fact the new investor is Asian-based ties in with NAB's goal of introducing Australian companies to new, global sources of capital. Mazzaferro tells *KangaNews* that achieving investor comfort with a relatively small borrower like TAE was a key challenge.

He also believes this type of deal is likely to be repeated, and not just by management buyout candidates. He points out that it could also help family-owned companies be passed from generation to generation without ceding control to outside investors, for instance.

Sourcing a sub-debt bid is the key. "There are plenty of investors out there who want to find higher yield. I think those which are able and willing to look at innovative structures like this one can be rewarded for doing so," Mazzaferro affirms.

we also need to refine what we do as the world changes. This is a continuous process of change and adaption to suit the market and client needs.

For example, in the financial institution (FI) space we have a client set which at all times is being challenged by the ongoing regulatory process –

such as how much capital they need to hold. While we need to be able to understand what is going on in the market and what investors are thinking, we are also going through this ourselves as a bank. So we need to look at how we take what we are learning in our day-to-day business and apply that for the benefit of our customers.

Another example is about how clients issue to fund their future growth. A lot of our clients in the FI and corporate spaces only used to look at senior debt, but now we are helping them explore opportunities down the capital structure as well as tapping new investor pools.

■ **How do you manage the balance of your team's resources between innovative deals – which are high prestige but may also be more labour intensive – and the more vanilla transactions which of course support factors like league-table position?**

SOKARIS We treat innovation as a business. NAB's structure includes a team of very senior, experienced professionals – all of whom have been in debt markets for a number of years – who solely work on innovation. This team supports our broader originations team in delivering our customers cutting-edge funding solutions.

Day-to-day contact comes from the team which talks to clients in order to solve problems, provide the right type of insight and give value beyond advising which market they should go to.

The next step is to bring in our innovation team, which then comes

up with ways to innovate in order to help solve complex problems for clients. It is this team's job to actually execute on new products and ideas, or at least variations of those ideas.

■ **In what areas do you anticipate**



"We believe we see the market better because of our strong deal capabilities and the way we collaborate as a team. To maintain this, though, we also need to refine what we do as the world changes."

CONNIE SOKARIS

DEAL CAPABILITY: **REGULATORY CAPITAL TRANSACTIONS**

WHO? QBE Insurance
WHAT? US dollar tier-two
WHEN? November 2014
HOW MUCH? US\$700 million
NAB ROLE: Joint lead manager
KEY INNOVATION: First Basel III-compliant tier-two issued offshore by an Australian insurer.

WHO? AMP
WHAT? Australian dollar wholesale tier-one
WHEN? March 2015
HOW MUCH? A\$275 million
NAB ROLE: Joint lead manager
KEY INNOVATION: Australia's first domestic tier-one deal issued under wholesale documentation.

WHO? National Australia Bank
WHAT? Australian dollar listed tier-one
WHEN? March 2015
HOW MUCH? A\$1.34 billion
NAB ROLE: Sole arranger and joint lead manager
KEY INNOVATION: Helping to reset the retail tier-one market after a period of uncertainty and volatility.

The capability and flexibility National Australia Bank (NAB) offers its clients in the regulatory capital arena are perfectly illustrated by this trio of transactions. NAB is the only intermediary to have executed Basel III tier-one deals in the domestic wholesale and retail arenas as well as taking an Australian issuer offshore for non-Australian dollar tier-two capital.

Capital has become an even more important part of NAB's debt markets business in recent times, as the regulatory focus on capital – and the amount of capital banks and issuers are required to hold – has increased and become more complex. The structure of the NAB business, specifically the focus on clients rather than products, scores heavily in this environment.

Connie Sokaris, NAB's general manager, investment-grade originations, explains: "The model NAB now has in place really resonates across all the products. It is further proof that companies looking for different sources of both funding and capital are able to rely on us. The growing importance of capital gives

more support for our structure, and also means our teams become even more embedded with each other."

Nick Chaplin, head of hybrids and structured capital origination, is NAB's capital-notes guru. He says the breadth of options available for tier-one and tier-two capital issuers is starting to open up significantly.

For instance, AMP's March 2015 tier-one transaction was the first-ever domestic hybrid deal from an Australian financial issuer to be completed under wholesale documentation. The local retail market has traditionally been the biggest supporter of a product which offers these buyers specific tax efficiencies. But Chaplin says NAB's experiences in lead managing wholesale tier-two transactions for smaller Australian banks suggested there might be appetite for the hybrid product, too.

"The wholesale tier-two deals priced by Bendigo and Adelaide Bank and ME Bank in 2014 were significantly supported by institutional and other wholesale, sophisticated investors in Australia, and

also by accounts from Asia," Chaplin reveals. "We had a feeling at the time those deals were done that there would be support from sophisticated wholesale investors for a tier-one trade."

Domestic wholesale capacity remains moderate – Chaplin says he thinks major banks may in time be able to issue A\$300-400 million (US\$230.3-307.1 million) in unlisted tier-one deals. As a result, it was critical for the retail hybrid market to get back on track in 2015 after experiencing capacity issues and price widening at the back end of the previous year.

NAB was an early mover as an issuer, and was rewarded with a A\$1.34 billion outcome on its Q1 listed hybrid – an excellent result for a deal with no direct refinancing component. "There had been a lot of softness in the market through the back end of 2014 so to be able to come out with a sizeable tier-one trade in the early part of the year was impressive," Chaplin comments. "There were risks involved with doing this, but we received good reliance from NAB's treasury in terms of our read on the capacity of the market."

The US dollar denominated, Reg S transaction placed by QBE Insurance (QBE) in late 2014 shows another string to NAB's capital bow. This tier-two deal was sold into Asia and Europe, but achieved the right currency outcome for the issuer. "QBE has businesses which suit US dollars so it was a natural choice for it to look at this market – the company hasn't generally looked to Australian dollars for capital," Chaplin confirms.

The deal was the first of its type in the Reg S market, Sokaris says, and as such the investor education process was challenging. But NAB's experience with the product – including tier-two issuance into a variety of markets – helped build client confidence.

"We had that confidence from the start, because the fact we had done a European deal for NAB and also a number of domestic-issuer deals meant we had the expertise to appropriately explain the product to investors," Sokaris reveals.

your team will be focused in the coming months, in terms of delivering innovative funding and capital solutions to clients?

SOKARIS One of the most important things on which we are currently focusing our forward thinking is developing innovative ways to assist

federal, state and local governments with their funding plans.

In terms of the issues we think will be in the Australian economy in the

DEAL CAPABILITY: **POOLED FUNDING**

WHO? Local Government Funding Vehicle

WHAT? Debut bond transaction

WHEN? November 2014

HOW MUCH? A\$240.1 million

NAB ROLE: Joint arranger and lead manager

KEY INNOVATION: The first-ever transaction by a pooled funding vehicle for local councils in Australia.

The Local Government Funding Vehicle (LGFV) allows councils in the state of Victoria, for the first time, to broaden their debt funding base beyond bank loans and into the capital markets. The vehicle is not guaranteed by state or federal government and while the loans cross-collateralise each other no one council guarantees another's debt.

James Waddell, director, capital markets origination at National Australia Bank (NAB), says the LGFV's debut deal achieved much for its underlying council clients.

With new competition for council lending, banks tightened the margins they offered borrowers in this sector in Victoria as soon as the LGFV was announced, according to Waddell. He adds that they did so again when the new entity's debut deal priced inside the major-bank curve.

NAB has been part of the drive to bring individual councils up to speed with capital-markets realities, having relied on bank funding in the past. As Basel III continues to challenge bank lenders, this type of innovation will only become more important, Waddell believes.

"We will continue to educate councils in Victoria around the capital markets," he says. "We have already been active in doing so once this year, and this opportunity will be open to all councils with an interest in participating in future transactions."

Waddell continues: "The economies of scale a pooled borrowing vehicle brings to a sector like local authorities are very attractive, especially when borrowers have to deal with high administration costs elsewhere. I can see applicability across the three south-eastern states of Australia. And I would encourage politicians in Queensland and Western Australia to consider a more liberal approach to how public-sector bodies fund themselves, too."

Connie Sokaris, NAB's general manager, investment-grade originations, agrees. She comments: "As we look at medium-term themes around government and how we replace public-sector money with private capital, the likes of the LGFV will become increasingly important. It is an issue of scale, about being able to reach a type of market which borrowers are not able to access independently."

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medium to long term, the questions are around how we help bring private investment into the public sector. There are a number of ways this could be achieved – including through

securitisation, privatisation or forming entities like the Local Government Funding Vehicle.

Also important is how to develop innovative ways of assisting government

efficiencies, whether through the privatisation agenda, social impact, affordable housing or aged care.

There are a number of challenges which governments will face in the future, and we are very keen to see how we can provide support. The exciting challenge is creating attractive options for our broader investor base to be involved. We are also asking how we can be a global enabler for investors, to make sure the right capital flows are coming into Australia.

■ Is there anything you consider to be NAB's role in terms of continuing to assist with Australian dollar market development?

SOKARIS There is a lot of talk about the domestic market losing some of its steam, but I don't think this is the case. Very good corporate issuers have come to this market and found strong demand.

Given NAB is very supportive of a sustainable market, it is important for the business to ensure there is a market for these issuers to access. We can do this in two ways: by making sure we have great relationships with existing investors, and by continuing to broaden the investor base. NAB has played, and will continue to play, a leading role in growing the number of investors who are using this market.

Looking back two years, non-institutional investors only comprised 1-2 per cent of a typical corporate deal. By comparison, in late 2014 and early 2015 the figure has increased to 10-12 per cent participation in corporate issuance.

This has been assisted not only by our access to this type of investor, but through education and also accessibility via the NAB Access Bond service. This is a major shift in both the type of investors and money coming in for corporate deals. •

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It provides us with an unmatched vantage point to see unimagined opportunities, as well as hidden risks.

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