

Stock Market Review

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Investors flock to the corporate bond market

The recent corporate bond offerings have yet again attracted a very strong response from investors. Both FIM-Bank plc and Gasan Finance Company plc announced that their respective bond issues were oversubscribed. This follows the strong take-up of the Midi plc bond issue which took place at the start of the year when the company attracted over €40 million in subscriptions. The response by the investing public to the FimBank and Gasan bond issues is a clear indication of the large amounts of money in search of more attractive rates of return.

The two large banks in Malta, Bank of Valletta and HSBC, reported at the end of their respective financial years that they have over €8,600 million in customers' deposits, so the few tens of millions being channeled into the new corporate bonds represent a tiny fraction of the amount moving away from bank deposits into bonds.

FimBank announced that the total number of applications exceeded a value of €38 million and hence the Bank exercised its over-allotment option to increase its overall bond issue to the equivalent of €30 million. Likewise, the Gasan Finance bond was increased to the maximum amount of €20 million after a large majority of the holders of the existing 6.4 per cent Gasan bonds being redeemed on May 31 opted for a roll-over while various new retail and institutional investors placed new money with the Gasan Group.

This strong response indicates that local investors are placing increased trust in the various bond issuers. On their part, the issuing companies must do their utmost to repay this loyalty by publishing their financial statements frequently and keeping bondholders regularly updated on developments and future strategy. An increased level of transparency and dialogue with all bondholders and market participants is necessary to ensure that the corporate bond market continues to attract investors. However, as investors are increasing their exposure to the corporate bond market, the liquidity aspect in the market when such corporate bonds are listed on the Malta Stock Exchange needs to be improved. All stakeholders including the recent issuers should ensure that a more liquid trading platform is established to enable investors to sell or purchase meaningful amounts of bonds on a daily basis.

This is a feature which could be fundamental to the continued suc-

cess in attracting more investors to the corporate bond market. It is inevitable that during the lifetime of a bond, some investors would need to dispose of their holdings due to a variety of reasons, while others would wish to acquire some stock. These investors must have their needs satisfied if we are to claim that an efficient securities market exists in Malta. Therefore an increased effort by all concerned to establish a market making function is necessary.

The increased issuance of corporate bonds is an occurrence which is also being experienced in many European markets as investors place increased amounts of their investible funds into fixed-interest rate securities as opposed to equities and other financial products which have gone out of fashion in recent months. It has been reported that during the first three months of the year, approximately \$331 billion was raised in the corporate bond markets across the US, Europe and the UK, a significant rise compared to the \$127 billion issued in the same period last year. A few days ago, it was also reported that the French public utility company Electricité de France is planning a big bond issue after Siemens (the German engineering group) attracted €16 billion in demand from investors. This was four times the size of the original issue! Moreover in the UK many of the larger companies including Vodafone, Tesco, Cadbury and National Grid have also tapped the market on various occasions in recent months.

At the height of the international financial crisis in the aftermath of the collapse of Lehman Brothers, many of the banks stopped lending to businesses and companies had to resort to the bond market, offering high rates of interest due to the negative market sentiment at the time. In fact, many of these issuers offered rates which were much higher than the norm with the result that some of these issues now trade at a premium as sentiment in the stockmarkets has somewhat improved over recent weeks. The strong response in the primary market as evidenced by the Siemens take-up as well as the reassuring corporate news among some international conglomerates also helped their bond prices trade above the 100 per cent issue price.

Although the local banks did not generally adopt the same strategy and continued to offer assistance to companies who required help albeit possibly at higher rates of interest in



some instances, many companies are starting to prefer to diversify their funding requirements (and reducing funding risk in the process) by opting for a mix of bank finance together with capital market finance.

As the European Central Bank lowered official interest rates in recent months, many depositors have found that their maturing fixed deposits can only be renewed at a fraction of the previous rate. This is possibly one of the main sources of the substantial demand for corporate bonds. This is also happening in overseas market and the international press recently reported that the huge demand for fixed-interest investments worldwide is due to the attractive returns being offered by corporate bond issuers when compared to those of government bonds and bank deposits.

In view of the increased participation in the bond market, one must ensure that apart from improving the liquidity nature of the Malta Stock Exchange trading mechanism, a continuous educational and awareness campaign is undertaken to explain the various characteristics of bond investing. Many investors (old and new) remain obsessed at the "security" aspect of the bond and always depart from this feature before taking an investment decision. While the secured nature or

otherwise of a bond is an important aspect, the financial strength of the issuer and its parent company should be the point of departure. Investors should first analyse the financial performance of the company including the interest cover and gearing or leverage as well as its future prospects before taking a decision rather than looking only at the security status of the bond.

The security attached to a bond is normally represented by property hypothecated in favour of bondholders. While many of the recent bond issues were unsecured, this does not imply that they are more risky than some of the secured bonds currently listed on the local Borza. Moreover, investors should also consider the allocation of one's portfolio towards a particular company and group of companies. This element of diversification is a very important consideration and the various new bond issues coming to the market provides an excellent opportunity for investors to ensure a widespread portfolio of bond holdings.

With official bank interest rates expected to remain low for an extended period of time, demand for corporate bonds should remain buoyant and this augurs well for other companies who are seeking to tap the bond market in the near future.

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