



Debt Primary Market Conventions

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Preface: AFMA Code of Conduct

AFMA promotes efficiency, integrity and professionalism in Australia's financial markets. The aim of the [AFMA Code of Conduct](#) (the Code) is to establish a common understanding of the standard of behaviour expected of all AFMA Member organisations and their employees when conducting business with clients, counterparties and colleagues and when providing financial services to retail and wholesale clients.

All AFMA Financial Markets Members and Partner Members are expected to observe the Code and operate with integrity, professionalism and competence. The Code is designed to support behaviours that put the interests of clients, the firm and the wider community ahead of personal or individual interests and promotes confident participation by users in Australia's OTC markets.

Market participants are reminded that they are generally expected to observe the market conventions as set out below when engaging in any form of market dealing.

1. Description

Debt capital markets are an important part of the global financial system, providing a source of long and short term funding for public borrowers for the maintenance and growth of businesses and governments.

Debt instruments represent a financial commitment by the borrower or issuer of the security and typically pay interest at set intervals and return the face value of the instrument to the investor or holder of the security at maturity. Primary debt markets are where debt instruments are issued and traded.

Borrowers generally engage intermediaries, usually banks or investment banks, to organise, structure and distribute new issues of debt securities. Intermediaries hold inventory of debt securities for sales and trading purposes and, in certain instances, for regulatory capital purposes. Investors generally purchase new issues of debt securities through intermediaries.

These Conventions reflect current market practices in the Australian debt capital markets for intermediaries originating and distributing new issues of debt securities and are maintained by the AFMA Debt Capital Markets Committee.

2. Products

2.1. Fixed Rate Notes

A Fixed Rate note¹ is a debt instrument which pays a fixed rate of interest (coupon) at specified dates over the term of the debt, as well as repaying the principal on the maturity date. Typically, the interest is paid semi-annually.

2.2. Floating Rate Notes

A Floating Rate Note (FRN) is a debt instrument which pays a variable rate of interest (coupon) at specified dates over the term of the debt, as well as repaying the principal on the maturity date. The floating rate is usually a money market reference rate, such as BBSW, plus a fixed margin. Typically, the interest is paid quarterly.

2.3. Medium Term Notes

Medium term notes (MTN) are debt obligations of an issuer, and according to the notes issued, may rank pari-passu with other senior debt or may be subordinate to senior debt. The notes are constituted by a deed poll and take the form of entries on a register, e.g. domestic corporate bond market.

MTN are issued in a series. Each series may comprise one or more tranches issued on different dates. These subsequent series may be fungible with earlier series, but fungibility is not guaranteed. MTN may be issued depending upon documentation as a number of different instruments as allowed under its documentation or program. Typical issue characteristics are either floating or fixed, e.g. subordinated debt.

2.4. Asset Backed Securities

Asset backed securities are supported by defined assets such as credit receivables which are usually held by way of a trust arrangement. Obligations to investors are met solely by the defined assets and resultant cash flow. An example of an asset backed security is a mortgage backed security (MBS). Asset backed securities may also be backed by credit cards, car loans, commercial loans and consumer loans or a portfolio of debt obligations in the case of a CDO.

2.5. Mortgage Backed Securities

Mortgage backed securities (MBS) is a generic name for any bond or other style of security issued by a mortgage provider and supported by pools of mortgages or specified mortgages. In Australia MBS are generally structured as FRN, reflecting the rate basis and prepayment options of the underlying mortgages.

¹ The terms note and bond may be used interchangeably throughout this document.

2.6. Subordinated Debt

Subordinated debt is a debt facility that ranks behind all other forms of debt in terms of security but ranks ahead of equity. In the event of the failure of the issuer, subordinated debt holders would not receive any payment until all legally defined creditors, including unsubordinated debt holders, are repaid in full (i.e. they rank behind holders of unsecured notes). There may be various repayment rankings within the subordinated debt category (e.g. senior and junior subordinated debt).

3. Transparency

3.1. Transaction announcements

The principle of transparency to the market applies to transaction announcements. It is standard practice for all deal roadshows and transaction mandates, along with launched transactions to be announced to the market in a transparent manner. This is typically done through an announcement to financial media outlets.

3.1.1. Issuance disclosure format

Broad and consistent dissemination of debt primary market issues in a standard format assists access and ease of monitoring of upcoming market transactions. The objective is to give market participants the same access and consistent disclosure to primary market trades.

Disclosure should be made in the following manner:

1. A media release is be sent to appropriate media vendors simultaneously with the Bloomberg alert that investors receive.
2. The wording of the media release and Bloomberg alert may adopt the following standard format, which is an example only:

[Issuer name] [Rating] [Guarantee if applicable] has launched a minimum A\$ [XXX] [Tenor] new issue. The transaction is being marketed at asw+[XX]sq / ACGB MMY+ [XX] and will price on or before DD-MM-YY. [Dealer name/s] are the lead managers. [Issuer name] [Rating] [Guarantee if applicable] has launched a minimum A\$ [XXX] increase to its [Coupon] [Maturity date] line. The trade is being marketed at asw+[XX]sq / ACGB MMY+ [XX] and will price on or before DD-MM-YY. [Dealer name/s] are the lead managers.

3.2. Mandate announcement types

3.2.1. Generic roadshow mandate

Types of roadshow mandate announcements would include but are not limited to the following:

- Investor updates i.e., annual/semi-annual, non-deal roadshow

- Deal roadshow
- Transaction specific roadshow, such as capital

An example of a generic roadshow announcement is:

MANDATE: Queensland Bank Ltd, rated A1/A+ by Moody's/S&P, has mandated ABC Capital Markets and XYZ Investment Bank to arrange a series of investor meetings in Asia commencing the week of April 18th. A capital markets transaction may follow, subject to market conditions.

3.2.2. Generic transaction mandate

An example of a generic transaction mandate announcement is:

The Sweet-Cola Company (Aa3 (Stable) / AA- (Stable) / A+ (Negative)), the world's largest beverage company and producer of the world's most valuable brand Sweet-Cola, has mandated Southern Cross Banking Group Limited, Atlantic Bank, and ABC Capital Markets as joint active bookrunners for a potential Australian Dollar offering. The transaction may launch in the near future, subject to market conditions.

This announcement does not constitute an offer to sell, or a solicitation of an offer to buy, any security and shall not constitute an offer, solicitation or sale in any jurisdiction in which such offer, solicitation or sale would be unlawful.

3.2.3. Specific transaction mandate

An example of a transaction specific mandate announcement is:

TASMAN BANKING CORPORATION, rated Aa2 by Moody's and AA- by S&P has mandated APAC BANK, YAMAICHI and TASMAN INSTITUTIONAL BANK for an AUD Tier 2 Subordinated transaction []. A transaction is expected to follow, subject to market conditions. The Subordinated Notes are expected to be rated [A3]hyb by Moody's and [BBB+] by S&P. (MS)

3.3. Marketing

The marketing process is important in the context of satisfying the local public offer test and interest withholding rules under section 128F of the Income Tax Assessment Act 1936.

Transactions are marketed electronically via the use of email, Bloomberg (IB chat rooms and generic messaging), Reuters and summary term sheets.

These marketing methods do not constitute legal documents and dealers should ensure the necessary disclaimers are provided on such communications where applicable.

Marketing documentation should clearly specify:

- Issuer
- Guarantor
- Credit rating
- Documentation
- Maturity
- Pricing Benchmark (see below)
- Settlement date
- Denominations
- Legal status
- Other deal specific terms

Following is an example of a typical Bloomberg marketing announcement for public distribution:

***** NOT FOR PUBLICATION IN OR DISTRIBUTION INTO THE UNITED STATES (OR TO ANY U.S. PERSONS) OR IN ANY OTHER JURISDICTION IN WHICH SUCH PUBLICATION OR DISTRIBUTION WOULD BE PROHIBITED BY APPLICABLE LAW *****

ISSUER: Mango Inc.
EXPECTED RATINGS: Aa1/AA+ (Stable/Stable)
SECURITY DESCRIPTION: Senior Unsecured Notes
DOCUMENTATION: Issuer's A\$ MTN Program
TOTAL SIZE: AUD-Benchmark
MATURITY: 4yr FXD | Long 7yr FXD
MATURITY DATE: [10] June 2020 | [10] Jan 2024
INDICATIVE YIELD: [2.755%] area | [3.440%] area
INDICATIVE COUPON: [2.75%] area | [3.40%] area, full first coupon on 10 July 2016
PRICE GUIDANCE: S/Q ASW+85bps area | S/Q ASW+125bps area
TRANCHE SIZE: A\$[Benchmark] | A\$ [Benchmark]
REOFFER PRICE: [●] % | [●] % plus 152 days accrued
B&D: GSI | DB (Risk Manager)
BOOKRUNNERS: GSI | DB | ANZ

MINIMUM DENOMS: A\$10,000. The minimum consideration payable when issued in Australia will be A\$500,000, subject to limited exceptions

NOT REQUIRED

SETTLEMENT: T+5 (10 June 2016)

EXPECTED TIMING: Pricing expected Friday morning Sydney

Information Memorandum and Preliminary Termsheets Attached

Important Notice

This communication is confidential and is for your information only and is not intended to be used by anyone other than you. This information is subject to change and does not purport to be a complete description of these securities or the offering. Please refer to the information memorandum dated DD-MM-YYYY and the applicable pricing supplement for a complete description.

This communication does not constitute or form part of and should not be construed as an offer to sell or the solicitation of an offer to buy securities in the United States or in any other jurisdiction. The securities described herein will not be registered under the US Securities Act of 1933 and may not be offered or sold in the United States. Neither this communication nor any information thereof nor the fact of its distribution shall form the basis of, or be relied on in connection with, any contract or commitment or investment decision whatsoever.

4. Pricing

4.1. Pricing call

New issues should be priced on a taped telephone line (or other recorded medium e.g. email) with full representation from the syndicate and (if possible) the issuer. As far as practical, transactions should be priced during Australian business hours (8:30am – 4:30pm in Sydney)

One of the syndicate managers is designated to run the pricing call. A representative from the swap desk of the syndicate running the pricing call may be included on the call where a live quote for risk transfer is required. Common terms of the issuance are read out on the call. At a minimum the following terms should be covered:

- Issuer name
- Issuer programme details
- Type of issuance i.e. fixed or floating rate
- Size of the new issue and (if relevant) individual tranche sizes
- Pricing date, settlement date and maturity date
- When pricing the individual tranche, spread
- Billing and Delivery (B&D) bank
- Issue and redemption price

4.2. Pricing methodology

4.2.1. Floating Rate Note Pricing

Floating Rate Note (FRN) pricing is normally simple as the note is normally priced at par. This means that the re-offer level will be equal to the coupon.

On the call for FRN pricing, the syndicate member leading the call will call out the key terms of the tranche beyond the common terms. These terms including the

- Coupon roll dates
- Date of first coupon
- Coupon margin
- Re-offer margin
- Capital price
- The reference benchmark

Once a quorum of the syndicate agrees (incl. the issuer), the syndicate will call the FRN tranche priced.

4.2.2.Fixed Rate Note Pricing

In order to 'price' a fixed rate note, a final yield and cash price based on the trade parameters must be agreed. This requires the syndicate and issuer to conduct a pricing call which also normally includes at least one of the B&D dealer's swap desks.

The syndicate member leading the call will propose the key terms of the tranche beyond the common terms. These terms include the coupon roll dates, date of first coupon, coupon yield, reoffer margin to the semi-quarterly coupon matched asset swap and capital price.

The pricing call for a fixed rate note is to solve for the yield that equates to the reoffer margin to the semi-quarterly coupon matched asset swap or other relevant pricing benchmark. If the intention is to solve using a different metric (e.g. semi-semi, quarterly/mid-swap) then investors should be made aware of the proposed pricing convention through the marketing process and documentation.

The syndicate and (if possible) the issuer need to be in agreement on the final cash price based on the parameters agreed during the call.

On the call the following inputs are agreed by the syndicate:

- Swap EFP (mid) for the tenor. If the bond straddles two tenors, then more than one swap EFP may be utilised.
- If the tenor of the new issue is >3yrs, the 3s 6s adjustment (mid) for the tenor or next nearest.
- Bid side of the relevant bond futures contract (currently; 3yr, 5yr, 10yr or 20yr) if no swap associated with the issuance. Pricing from the Offered side is appropriate in situations where the underlying risk transfer warrants.

- If the syndicate and issuer intend to use reference bond futures contract/instrument other than the “current” contract, there needs to be agreement on the precise contract, and marketing should clearly reference the agreed instrument/contract.

A yield is derived based on these inputs solving for a Semi-quarterly coupon matched asset-swap plus (or minus) the margin. This yield and/or a ‘new issue EFP’ is agreed by all parties. The ‘new issue EFP’ is the differential between the yield of the new issue and the yield of the futures sighted.

The cash price (to three decimal places) of the new issue is agreed based on the derived yield.

Additional points

The market convention is for Fixed Rate Notes to be priced at or below par. If the coupon is rounded down, it is generally accepted to be done so in increments ranging from 5-25bp.

The discounting curve used to price bonds is that which is generally used within the Australian swap market

EXAMPLE

Pricing a 7 year bond with a spread of s/q ASW+180bps	
7 year Swap EFP (2)	1 bps
3mthx6mth adjustment (3)	12 bps
10 year Govt bond futures (SFE)	97.80
10 year Govt bond futures implied yield (4)	$100 - 97.80 = 2.20\%$
7 year S/Q swap (5)	$= (2) - (3) + (4) = 2.09\%$
Reoffer spread (1)	180 bps
Approximate yield (6)	$= (5) + (1) = 3.89\%$
Assuming coupon (7)	3.75%
Adjustments (8)	2 bps
Reoffer yield (9)	$= (6) + (8) = 3.91\%$
Cash price	99.028

Assuming pricing is for a 7 year bond at a spread of 180bps over the swap rate, the underlying swap rate must first be calculated:

- 1) The market convention for fixed rate bond pricing uses a theoretical semi-quarterly coupon matched asset swap (S/Q ASW) level plus (or minus) the margin of the deal (i.e. +180 bps). As there is no directly quoted S/Q ASW level readily available, it has to be calculated.
- 2) The Swap Desk will quote the 7-year swap EFP semi-semi using the relevant broker pages on screens such as Bloomberg or other market accepted alternatives. Assume for this example, the 7-year Swap EFP (mid) was 1bps.
- 3) Outright swaps are quoted as a yield but are also quoted as a spread to the government bond futures, the Exchange for Physical ('EFP'). Swap and hence bonds of a tenor of 5 years or less, will price against the 3 year Futures and tenors above 5 years will be against the 10 year Futures.
- 4) The Swap Desk will then quote the 3 month x 6 month ('3/6s') adjustment to convert the swap from S/S to S/Q. At the time of writing, the 7 year was 12bps (mid). This gives an adjusted Swap EFP of -11bps (1-12bps).

In Australia, the 1-3 year swap curve is set on a quarterly/quarterly basis whilst the swap curve beyond 3 years is quoted on a semi/semi basis. Hence for tenors over 3 years, the floating side would need to be adjusted to make it S/Q (i.e. 3mx6m adjustment as per below calculation).

Semi-quarterly ('s/q') means it is calculated where mid-level swap is for a fixed rate (semi-annual) would be vs. a floating side paying quarterly.

The Swap Desk will then quote the 10 year Government Bond Futures to calculate the implied yield, at the time of writing the bid side is at 97.80 = 2.20% yield. The yield is derived using 100 - the price (97.80) to equal 2.20%.

The above inputs give a 'straight line' yield as follows = (Bond futures yield) 2.200% + (7 year swap EFP) 0.01% - (6/3 adjustment) 0.12% + (margin) 1.80% = 3.89%. However, the bond yield on the pricing call will differ.

The bond yield is then solved by the swap desk using the market rates quoted above that equate to a semi-quarterly ASW plus the bond margin. Based on the rates above we get a yield of 3.91% on a bond with a 3.75% coupon and a semi-quarterly asset swap plus 180bps. This rate differs from the 'straight line' one above due to a number of adjustments.

The yield that is solved is calculated on a discounted basis to equate to a semi-quarterly coupon matched asset swap spread of +180bps. This is a non-linear calculation due to: i) the coupon being set below the yield of the bond (requiring a greater amount of discounting); ii) the semi-annual payment nature of the bond relative to the quarterly pricing convention (whilst the swap rate has been adjusted the credit spread has not and is accounted for here); iii) Australian bond valuation being on an ACT/ACT day count basis whilst swap rates are calculated on an ACT/365 basis; iv) the length of settlement, noting that Australian swaps settle t+1. It is difficult to breakdown these

individual components, but this typically equates to 1-2bps at current spread levels (higher for transactions with larger credit spreads). Calculated today these differences resulted in an approximate 2bps variance relative to an arithmetic calculation.

Syndicate will then determine the cash price based on the yield. With a 3.75% coupon and 3.91% yield, the re-offer cash price would be 99.028.

4.3. Benchmarks

4.3.1.S/Q ASW (Semi / quarterly asset swap)

New fixed rate bond is referenced as a spread against a semi/quarterly coupon matched asset swap level.

4.3.2.Bond EFP (exchange for physicals)

New fixed rate bond is referenced as a spread against the most liquid and nearest (in maturity) 3, 5, 10 or 20 year Commonwealth Treasury Bond Futures Contract.

4.3.3.ACGB (Australian Commonwealth Government Bond)

New fixed rate bond is referenced to a spread against the nearest maturity and most liquid Australian Commonwealth Government Bond.

4.3.4. BBSW (Bank Bill Swap Rate)

New floating rate note references as a spread to the agreed Bank Bill Swap Rate.

5. Hedging

Typically AUD new issues / taps receive demand from Investors in two risk categories:

- 1) Outright – no hedge to be dealt with by the syndicate.
- 2) Hedging with futures - Investors often will buy the new issue and sell to the syndicate a number of futures. This is called an Exchange for Physical or an 'EFP'. The number of futures is calculated by dividing the Hedge ratio by the AUD value of 1bp in the futures.

5.1. Hedging with futures

Example:

Three year Gov't bond futures (SFE)		
1bpv in futures	30.94	Can be obtained from futures contract and Bloomberg page 'DES'
Risk (BP/million)	431	Of the new issue
Hedge ratio	13.93	Number of futures to be traded per million, to be rounded up/down to a whole number

The hedge ratio has to be agreed by the syndicate at the time of the trade pricing.

The orders that are to be hedged via EFPs are identified prior to pricing and the number of futures to be sold by the dealers calculated.

If there is a liability swap for the issuer and one of the syndicate members wins that swap, usually that dealer is B&D on the transaction. As the dealer is the swap provider, they are expected to face investors on the new issue tickets and associated futures hedge. Other members of the syndicate can face investors by exception.

If there is no issuer swap, then who will take on the risk of the futures has to be decided prior to pricing by the issuer and/or the syndicate. The EFPs can be split up by agreement or a hedge manager can be appointed by agreement of the syndicate and/or the issuer.

5.2. Investor Switching

The current market practice with respect to any primary bond activity that requires switching, involves bilateral switching between a relevant Joint Lead Manager and an investor.

6. Breaking of syndicate / free to trade

The customary market practice in the Australian market is that an issue is free to trade immediately post pricing.

7. Settlement

7.1. Standard timing

The standard convention for settlement timing is T+5, this can however be longer or shorter depending upon an issuer's request.

7.2. Settlement agent

The paying agent should be sent (quoting the relevant ISIN and bond title):

- 1) Two business days prior to closing or (where less than two business days between launch and closing) as soon as practicable -the executed: final terms/pricing supplement for a drawdown; or global note for a standalone issue.
- 2) By the end of the business day following closing - the final offer document.

7.3. Settlement methodology

Settlement is payment against delivery with interest charged on late delivery.

The Lead Manager(s) will agree upon a billing and delivery agent that will face the issuer and investors on a transaction for settlement. There are two methods of payment:

- Delivery versus payment
- Free of payment

7.3.1. Delivery versus payment

In relation to a syndicated deal, the managers agree that one of the managers will act as settling dealer on behalf of the dealers in delivering the note proceeds to the issuer (or its issuing and paying agent) on the settlement day in exchange for the issue and delivery of the notes in the relevant clearing system (generally Austraclear). The settling dealer is not liable or responsible for the performance of other dealers' obligations in connection with their respective allocations.

7.3.2. Free of payment

Where a deal is free of payment, the methodology is the same as the above except the delivery of the net proceeds and the notes are independent, and the note proceeds is a direct payment into an issuer account.

8. Cost of issuance for the borrower

Legal costs of the issue, the cost of the issuer's professional advisers, expenses incurred for the listing, the printing and delivery of the offer document and bonds and all necessary approvals should not be charged against fees paid to the managers.

Any expenses of a lead manager which exceed the expense reimbursement by the issuer should not be charged against fees paid to the managers (though any such excess may be shared between lead managers pro rata to their underwriting commitments).

Registry services, specifically Austraclear, should not be charged against fees paid to the managers. Issuing and paying services should not be charged against fees paid to the managers.

9. Fees

Fees are to be paid on settlement. There is Australian Goods and Services Tax (GST) on fees to the extent applicable.

The Issuer will normally, as agreed in the relevant transaction documents:

- 1) pay, or reimburse the JLM for, all reasonable costs and expenses (including value added tax and any other taxes or duties and fees and disbursements of counsel to the JLM) incurred by the JLM in connection with the preparation, negotiation, printing, execution and delivery of the Program Agreements and the Notes and all documents contemplated by the Program Agreements and the Notes.
- 2) pay, or reimburse each Dealer for, all costs and expenses (including value added tax and any other taxes or duties and fees and disbursements of counsel to such Dealer) incurred by that Dealer in connection with the enforcement or protection of its rights under the Program Agreements, the Notes and all documents contemplated by the Program Agreements and the Notes.
- 3) Pay any stamp duty or other similar taxes (including any penalties and interest in respect thereof) payable in connection with the entry into, delivery and performance of any Program Agreement or any Notes and will indemnify and hold harmless each Dealer on demand, on an after tax basis, from all liabilities arising from any failure to pay or delay in paying such duty or taxes.

A Fee side letter is an acceptable market practice if the fees are not scheduled in the manner outlined above.