AFMA

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Dear Mr Cohn-Urbach

Australian Debt Capital Markets Management and Practice

The members of the Australian Financial Markets Association (AFMA) appreciate the opportunity to discuss Australian debt capital market (DCM) activities and practices directly with ASIC staff. At a meeting in June 2019 between AFMA and ASIC, ASIC indicated that ASIC would welcome views being put in writing while ASIC is conducting its review into Australian debt capital market management and practice.

Debt capital market issuances and underwriting are complex services provided by financial market participants in their capacity as lead managers. Lead managers work to ensure debt capital market transactions are executed as smoothly and as efficiently as possible, whilst meeting the issuer's size, maturity, pricing and distribution objectives. At the same time, lead managers also need to take into account possible secondary market performance and the willingness of a professional investor base to participate in current and subsequent debt capital market transactions by the relevant issuer. These and other relevant factors need to be considered in constantly changing market dynamics, often involving subjective judgments. Market confidence in the success of new issues is critical in debt capital market transactions. Maintaining this confidence is essential to a successful and sustainable debt capital market in Australia. Australia has a long-standing and well respected debt capital market which is vital to the functioning of the economy.

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AFMA members collated these select guiding principles which generally underpin market issuance practices in Australia, which are divided into matters dealing with Allocations, Market Communication and Joint Lead Manager (JLM) Orders. These guiding principles are not exhaustive, may not be relevant for all debt capital market transactions and need to be adapted to suit the particular circumstances of each debt capital market transaction.

1. Allocations

1.1. Dealers are often required by the issuer to consider a number of variables when asked to determine allocations.

1.2. Where variation in treatment is applied, there should be a reason for the variation.

1.3. Subject to the issuer's directions, the acceptable reasons for variation in treatment relate to orders that provide leadership in a transaction, to the extent that they meaningfully assist in improving the prospects, volume and/or price of a new issue. Relevant factors that may result in a preferential allocation include, without limitation:

- the timing of the interest being reflected, including prior to the new issue being launched;
- the volume of the order;
- the price level of the order;
- the likely investment horizon of the investor and the likely impact on the aftermarket;
- whether the order is not dependent on a switch out of bonds from the same or another issuer; and
- issuer preferences around factors such as investor type, style, size and/or geographic location.

1.4. Joint Lead Managers (JLM) may have policies and/or procedures that set out their process for managing allocation recommendations for debt capital market transactions.

1.5. To manage perceived and/or actual conflicts of interest, JLMs should disclose their related party interest to the issuer as part of the allocations process.

1.6. Allocation recommendations for parties related to the JLM should be made in line with similar investor types and in line with the guiding principle mentioned above.

1.7. JLMs should have policies and/or procedures to manage any potential and/or actual conflicts of interest.

2. Market Communication

2.1. Primary market activity is an important indicator of prevailing market conditions and informs Market Participants assessment of fair value prices for securities.

2.2. Intermediaries and issuers should give due consideration to the interests of the marketplace and all its participants when managing communication on primary market activity and intentions with investors and the market more broadly.

2.3. Information relating to primary issuance activity which is to be shared with 'public side' participants, other than under a formal wall crossing, should be made 'generally available' to all market participants simultaneously and in a consistent form. To be considered 'generally available', information should be actively disseminated via a channel which can be readily accessed by investors, intermediaries and trading desks.

2.4. Market announcements should be limited to objective factual accounts.

2.5. In the event it becomes clear that a prior statement is no longer accurate or becomes misleading or deceptive, this should be clarified through a subsequent update as soon as possible.

2.6. Market announcements will by necessity include information in a summary form. Information should be sufficiently complete to be informative and to limit the risk of it being misinterpreted. Intermediaries should give careful consideration to the information provided so as to ensure that the information is not misleading or deception (by omission or otherwise).

2.7. Where information is sourced from supporting documentation, announcements should reference the source document if it is practical to do so.

2.8. Where supporting information is being made available on request to a potential investor, it should also be distributed on request to all bona fide market participants as practicable.

3. Joint Lead Manager (JLM) orders

Increasingly investors want more transparency during the syndication process. Specifically when there in an interest to know the proportion of bonds held by JLMs, as this can form part of their decision making process in participation in a transaction.

3.1. On book updates, the AUD market has started to include the text "including JLM interest", in the case where there is JLM interest in the transaction. In some other jurisdictions, JLMs additionally quantify the scale of the JLM interest as part of the overall order book (noting this has been largely driven by regulation). While the AUD market is yet to fully progress to this level of transparency, there have been some instances where JLM interest has been quantified on book updates.

3.2. The definition of a 'JLM order' may for example include orders through a trading book, relative value book, balance sheet investor. Assessment will come down to factors seeking to determine how 'arm's length' the order is. Initial questions to assess the allocation ticket would be:

- Is the investor broadly marketed to by other dealers?

- Do they have separate reporting lines to the JLM? What is the rationale for the investment.

3.3. Credible inclusions as 'JLM interest' are:

- trading books from JLM banks,
- Relative Value (RV)/ Accrual book from a JLM-bank especially if it is aligned to the DCM business.

A key question is would the RV book buy this deal if the JLM was not on the deal? Historical behaviours of the investor could also be taken into account by the syndicate.

3.4. There is broad consensus that what is excluded from 'JLM interest' are:

- liquidity book/balance sheet orders that are from the dealer's Treasury; and
- JLM associated private bank or asset management orders who are investing on behalf of or managing third-party independent funds.

3.5. It is noted that whether a transaction is underwritten or not, there should be no difference to the treatment of JLM orders as described. In either case, a trading desk order should be completely separated from the private side/syndicate orders.

- In the case of underwritten trades, the JLM group have committed to underwrite a minimum deal size and/or price. The syndicate desk may have an agreement with the issuer to either place a lead order upfront, or to take down a residual of bonds. In this case although the bonds are allocated through the primary syndicate or DCM desk and passed to the trading desk, any secondary trading order should be distinct and separate, and be included within the 'JLM interest' as previously described.
- In the case of non-underwritten trades, where the mandate is on a "best efforts" basis and there is no underwriting agreement in place, and the JLM group are not expected to make up a short fall in the event of undersubscription, an order from a JLM trading book would still need to be disclosed in book updates. This is consistent with the offshore treatment of JLM trading bids.

4. Future development

These principles are the subject of current consideration by AFMA members who are considering whether to develop AFMA industry guidelines dealing with market practices which would provide more granular information. This work would build on the existing AFMA *Handling Inside Information & Market Soundings Guidelines for Institutional Debt Capital Markets*.

However, members have agreed that before proceeding further with development work on AFMA guidelines, we should have regard to any report ASIC may publish relating to its current DCM allocations review.

AFMA and its members remain keen to maintain a dialogue on DCM market practices and we are at your disposal if you have any queries.

Please contact David Love either on 02 9776 7995 or by email dlove@afma.com.au if further clarification or elaboration is desired.

Yours sincerely

David Love
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