EUROWEEK

US PRIVATE PLACEMENTS 2014

January 2014

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Source for graphs: Lloyds Bank

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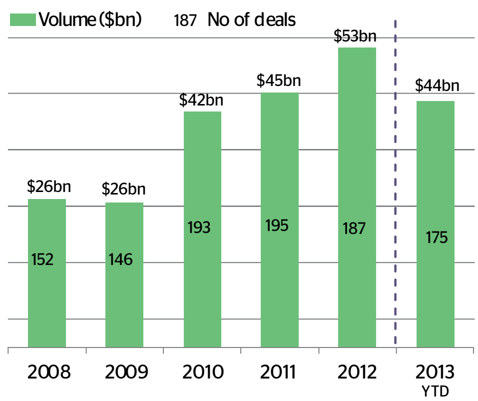

US PP issuance in 2013, to November

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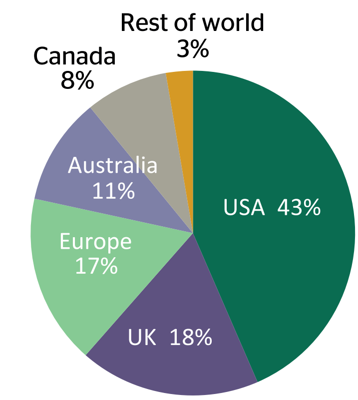

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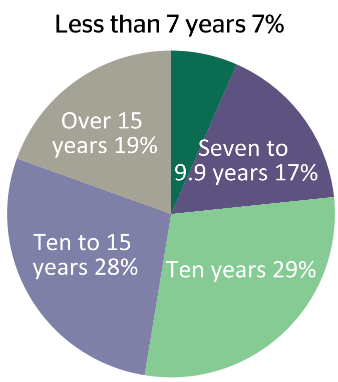

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Printed by Williams Press

BBC's unique credit wins new fans among US insurers

Everyone knows what the BBC is, but what kind of credit risk is it? That question becomes still more tricky when you are lending to BBC Commercial Holdings, an unguaranteed subsidiary that sells BBC content around the world. It was a challenge US private placement investors relished, enabling the BBC to raise its first on balance sheet bond at near record low interest rates.

The BBC's *Sherlock* drama has been sold to over 180 territories

THE BRITISH Broadcasting Corp, the UK's state-owned broadcaster, is not a typical US private placement issuer – or even a typical company.

But its unusual nature demonstrates the readiness of US PP investors to consider complex credits – and the market's attractiveness for borrowers with limited funding needs.

The BBC had issued bonds before: three securitizations totalling £1.3bn between 2003 and 2005, to finance property upgrades. These count as leases, not debt, on its balance sheet.

Its £170m private placement in June 2013 was different. It was for BBC Commercial Holdings, the division that sells programmes to broadcasters globally, mainly through its unit BBC Worldwide.

BBC CH had sales of £1.09bn in 2011-12 and made a £115m profit. Since 2003, the government has permitted it to borrow up to £380m for working capital. It has a revolving bank credit facility of the same size.

The parent Corporation, mainly financed with licence fee payments by UK television owners, has a separate borrowing limit of about £200m.

For a long time, the bank facility was perfectly sufficient for BBC CH, but over the years, Stephen Wheatcroft, the BBC's group treasurer, had been thinking more and more of supplementing it. BBC CH's debt cap is unchanged, but the PP will enable some bank drawings to be repaid.

The PP had three purposes. Despite BBC CH's small debt, there was value in reducing its reliance on banks, Wheatcroft says. "The second thing was to extend our maturity profile — we do have a core debt of around £170m that I'm happy to take a view will be there over seven years. Thirdly, we wanted to lock in what are absolutely fantastic all-in levels."

The rating agencies have assessed the BBC's credit for the purposes of its securitizations, but Wheatcroft did not want a public rating.

"US PP investors were hungry for good, strong credits, and given the BBC's brand and credit strength, I was more than happy to let investors derive their own view," he says. "The rating on the CMBS deals is not a public rating, and we didn't particularly want a subsidiary to be the subject of a rating."

The BBC's banks advised that the US PP market offered better pricing than a public bond, and two of them, Barclays and Lloyds Bank, won the mandate.

The seven year bond was priced on May 30, well before the worst of the rise in US interest rates.

It comprised £28m in sterling and $216m in dollars. The dollar tranche pays a 2.71% coupon, or 115bp over Treasuries. After swapping to fixed rate sterling, BBC CH will pay less than 2.3% interest.

To put that in context, at the end of May, the seven year sterling swap rate was about 1.53% and the March 2020 Gilt yield about 1.35%.

The bond was more than five times subscribed, and the BBC ended up with eight investors, all US-owned.

Delving into the credit

Attracting investors' attention was not difficult, but helping them to understand the credit proposition involved a lot of discussions.

BBC CH's debt is not guaranteed by the BBC as a whole. But it is intimately linked with the BBC. While this arguably creates a "halo effect", strengthening the company's credit, it is also a source of uncertainty.

Wheatcroft says that when marketing the deal, the BBC emphasised "the concept of public service broadcasting, and the tremendous public support the BBC receives and the political support that goes alongside it, together with describing in detail the business of BBC Worldwide".

Its main business is acquiring rights to BBC programmes from the BBC and other creators and maximising their value by selling rights overseas. In some cases, such as the US version of *Dancing With the Stars* (*Strictly Come Dancing* in the UK), BBC Worldwide's studios around the world actually make the programme.

BBCW also sometimes co-finances productions with the BBC, giving it free access to the rights.

BBCW pays what is considered an "arm's length" price for rights to BBC programmes, but it has a right of first refusal; something a completely separate business would not enjoy.

From 2016, the BBC will need a new settlement from the government — something that is subject to political opinion. Rival media such as Rupert Murdoch's titles have attacked the BBC, claiming it should not be allowed such commercial freedom.

These concerns were addressed with a change of control put. PP investors also have a put if the BBC's Royal Charter — due to expire in 2016 — is changed in a way that materially weakens BBC CH's credit.

Financial covenants were the same as on BBC CH's loan – that Ebitda must cover interest three times, and net debt may not exceed three times Ebitda. ▲

Mitie finds PP buyers open to bespoke M&A financing

With modest capex needs and narrow margins, outsourcing companies are ideally suited to the US private placement market. They don't need to borrow vast amounts, but can benefit from investors with deep credit skills that value stability. Mitie refinanced an acquisition with a PP in 2010 — then, when it did another takeover in 2012, the PP market was the natural place to turn.

THE OUTSOURCING industry is one that US private placement investors love, bankers say. Big UK names like Compass, Serco and Capita have all borrowed in the market.

Mitie is smaller, with £2bn of revenue in 2013, but still a visible presence across the UK, where some 70,000 staff perform facilities and property management services for clients as varied as PriceWaterhouseCoopers, Odeon Cinemas, Norwich City Council, the Royal Opera House – and Lloyds Bank.

It is also growing steadily – revenue is up 63% since 2007 and never stopped rising through the financial crisis.

Until 2010, the FTSE 250 company had only ever borrowed from banks, but acquisitions are part of its growth strategy, and in that year it turned to the US PP market to refinance takeovers.

In August 2009, Mitie agreed to buy Dalkia Technical Facilities Management, a UK technical and energy services provider, for £120m. Mitie paid in cash up front out of its bank facilities, and swiftly placed £40m of new shares. Then in November it bought a social housing management business for £37m, again drawing on its bank lines with the four main UK clearers.

"Through 2010 we were approaching the refi of our bank facility in March 2011, and everyone crystallised their thoughts around having some larger chunks of longer term debt," says Rob Jennings, head of operational treasury at Mitie in Bristol. "When the payback period of an acquisition is longer than your bank facility, it makes sense to be more broadly aligned to it."

Being unrated, and only wanting about £100m, Mitie opted for a US PP, especially as the tenor of bank loans available was shortening at that time.

With Royal Bank of Scotland as agent, Mitie visited investors in the US and came away with a $96m seven year tranche at 3.39%. Mitie was flexible about tenor, between five and 10 years, so when a sterling-based investor offered to buy a nine year note, it was quick to work that into the deal. The £40m tranche paid 4.38%.

The currency swap from dollars to sterling – partly floating rate – was the first for Mitie. With all its relationship banks keen to compete, Mitie could exercise some pricing tension on capital and credit margins, while sharing the ancillary business around.

A Mitie staff member cleans the stage at the Royal Opera House

Smooth second outing

In October 2012 came another acquisition, of Enara, the UK's fourth largest provider of care services for elderly people in their own homes. This time, Mitie knew in advance how it wanted to finance the £111m deal – to keep its revolving credit facility for working capital and maintain headroom with the banks for any future borrowing.

Before announcing the takeover, Mitie had secured a £150m bridge to PP facility from its club of banks. Lloyds Bank and RBS, the agents, were ready to launch the PP on November 1.

Cost-conscious Mitie didn't visit the US, but held a roadshow in London on November 5 and that afternoon, a two-and-a-half-hour conference call for US investors, with its finance director and investor relations team. Part of their task was to get investors comfortable with a covenant package updated to match Mitie's bank facility, refinanced in 2011 – and then to convince them to alter the covenants on the 2010 PP to match the new ones.

Eight days later, the agents delivered the 'bid book'. "In the bid process on the first deal, we'd had more of a spread of tenors and margins, because Mitie was not known to the PP market," says Jennings. "In 2012 we were looking for bids at seven, 10 and 12 years and 90% of them came in a concentrated range. They knew Mitie's story and over the past two years we'd done what we said we would."

The deal was oversubscribed, at the margin Mitie wanted, so it had room to negotiate a bit, suggesting that investors move from one tenor to another. "The following day the agents were back out talking to investors," Jennings says, and by the end of November 14, the deal was 'circle priced' and Mitie did the swaps.

There were two 10 year tranches: $153m at 3.85% and £25m at 3.87%, and a £30m 12 year at 4.04%. Mitie ended up with 15 investors including all the 2010 buyers bar one, and some new big houses it had been keen to bring in.

This time, some banks were less competitive on the swap, only willing to do them if they were also the agent, while new lenders came in aggressively. Mitie was able to get three banks to comparable pricing and share the business around, spreading its counterparty risk.

The borrower was highly satisfied. "You get all three," says Jennings. "Longer tenor, an increased amount, and the spread, taking into account maturity, is not materially greater than on a bank loan. Circa 4% for 10 or 12 year money – I don't think anyone would say that's expensive." ▲

Britvic stays a regular PP issuer before, during and after crisis

Soft drinks maker Britvic was happy with its new bank group in 2007 — but knew it wanted something else as well. Forging links with US private placement investors, and maintaining them with regular meetings and calls, stood it in good stead in 2009 and 2010, when financing conditions were harder. Britvic was able to keep raising long term debt at modest coupons, leaving its bank facilities free to use flexibly for financing acquisitions and other needs.

BRITVIC IS A household name in the UK, where it is the second biggest soft drinks producer. Brands such as Robinson's, J2O, Fruit shoot and Tango are its own – but it is also the exclusive bottler of Pepsi drinks for the UK, with revenue of £1.3bn.

In the US, Britvic is much less well known – but that has not stopped it finding a second home, financially speaking, in the US private placement market.

In that way, Britvic is typical of European issuers of US PPs. The mainly US-based investors are willing to analyse credits they don't already know, and then to stick with them, deal after deal.

Britvic's involvement with the market goes back nearly 10 years. "Before we did our IPO in 2005, we set up a £450m bank facility," says Dominic Whyley, director of treasury at Britvic in Hemel Hempstead. "At the time the bank market was very strong and supportive, but we wanted to have an alternative source of funding as well."

From the original group, Barclays, HSBC, Lloyds Bank and Royal Bank of Scotland are still with Britvic.

Britvic issued its first US PP for £229m-equivalent in 2007, the year it bought Ireland's Cantrell & Cochrane for £170m. "We wanted a tranche of core long term, fixed rate funding," says Whyley.

Rather than issuing PPs for specific acquisitions, Britvic's policy has been to use PPs to term out debt, creating headroom in its bank facility for future needs.

Its PP debt has grown through a further three issues, partly as the company has grown, and partly through a gradual conversion of its debt to fixed rate, PP form. Some of Britvic's original investors have bought all its subsequent offerings; others missed some deals and then returned.

"We have regularly evaluated our

Britvic's bottling deal with Pepsi has helped it bring its brands to the US

financing options, and typically the private market has at the time been the most appropriate," Whyley says. "We don't think it's necessary or appropriate to have a public rating at the current time. We can issue manageable deal sizes and we have a supportive group of investors that understand our credit story."

Britvic has never used any other kind of non-bank funding. Keeping Barclays and RBS as agents, it returned in November 2009 with a $250m issue in four tranches from five to 10 years – roadshowing in the US as usual.

Then in May 2010, Britvic moved into France with the €237m acquisition of Fruité, maker of Teisseire fruit syrups. The deal was financed from bank facilities and a £94m share placement, but in September 2010, Britvic raised $163m and £7m of seven to 12 year PP debt.

Consent sought for merger

Since then, Britvic's big manoeuvre has been the attempted all-share merger with AG Barr, the Scottish drinks group that makes Irn-Bru. News of the talks became public in September 2012 and Britvic headed to the US to meet PP investors, whose consent was needed for the merger.

That was obtained without difficulty, but after nearly a year, the Barr deal was abandoned in July 2013.

With its latest private placement in November 2013, Britvic needed a smaller amount, partly to refinance two PP notes that will mature in February and December 2014. The issue comprised four tranches of seven to 12 year notes totalling £35m and $44m at coupons from 3.4% to 4.24%.

Britvic held a fresh contest and chose Lloyds and RBS as agents. To maximise the efficiency of refinancing, it took advantage of one of the PP market's unusual features: funds can be drawn down at a future date, in this case February 2014.

Whyley highlights two ways the market has changed through the financial crisis. "In 2007 a number of investors were able to do the swap into sterling themselves," he says. "That fell away in 2009 and 2010, and then came back in our current deal."

Meanwhile, in the crisis years, some US investors became unwilling to invest in Europe, or in specific countries. That, too, has now largely gone.

"What we have done, since 2007, is make a concerted effort to maintain a regular dialogue with our investors," Whyley says. "We do a half yearly call on our results, and I know investors appreciate it."

Britvic will always look at other sources of financing, but for the moment, the PP market is hard to beat. "We've issued four times, been through a successful consent process when we needed to and investors have been very supportive," Whyley says. "It's still a market we'd see as leading our financing options, alongside the bank market."

And while the cost of bank debt has risen in the last few years, Whyley adds, PPs have got cheaper with interest rates, reducing if not totally eroding banks' cost advantage. ▲

Companies seek long term debt from astute relationship lenders

THE US private placement market – where the main investors are US insurance companies – has a long history of being open to high quality European corporate borrowers. For companies that do not want to borrow a full benchmark-sized amount, or do not want a public credit rating, the PP market offers an alternative to the public bond market.

Since the financial crisis, corporate treasurers' enthusiasm for diversifying their funding away from banks has redoubled, and with interest rates exceptionally low, many are attracted by the chance to raise seven to 12 year fixed rate debt.

EuroWeek and sponsor Lloyds Bank brought together a group of leading investors and corporate issuers to discuss the latest developments in the private placement market at the London offices of White & Case.

As the participants reveal, borrowers can now sometimes obtain PP funding at rates comparable with bank loans – yet for longer tenors. Investors are increasingly willing to perform swaps on an issuer's behalf. But while demand is strong from US investors, progress at broadening UK and European demand is still frustratingly slow.

Participants in the Roundtable

Back row, L to R:

James Douglas, partner and global co-head, Deloitte Debt Advisory

Calum Macphail, head of private placements, M&G Investment Management

Stephen Valvona, director, US private placements, Lloyds Bank

Rob Jennings, head of operational treasury, Mitie Group

Donald Campbell, senior vice-president, Pricoa Capital Group

Stuart Hitchcock, managing director, private placements, New York Life Investments

Front row, L to R:

Andrew Weiler, partner, White & Case

Marcus Dix, vice-president, structured asset finance, Rolls-Royce

David Cleary, co-head of US private placements, Lloyds Bank

Jane Pilcher, group treasurer, Anglian Water Group

Jon Hay, corporate finance editor, *EuroWeek* (moderator)

Stephen Wheatcroft, group treasurer, BBC

EUROWEEK: Could you start by introducing yourselves and your involvement in the US private placement market?

James Douglas, Deloitte: I'm here as an issuer and an adviser. We've raised $1.5bn in the PP market and most recently issued in October. I've also advised issuers on private placements.

Calum Macphail, M&G Investment Management: We are one of the few non-US investors in the market, active for about 15 years now.

Andrew Weiler, White & Case: I've been active in the private placement market for about 15 years, and worked on over 100 of them. I'm originally from New York, but I've been in London for that whole time, so both an English and a US lawyer.

Marcus Dix, Rolls-Royce: We've accessed the private placement market as recently as this year to finance our aero-engine leasing joint ventures.

Stephen Valvona, Lloyds Bank: I'm a director in the

Lloyds private placement team, acting as an agent on private placements. I've been doing this now for about seven years.

Stuart Hitchcock, New York Life Investments: I'm managing director of our London office, which we opened in January 2013. Before that, I spent a decade at RBS on the agent side, both in the UK and also distributing financings in the US.

David Cleary, Lloyds Bank: Based in London, I co-head the US private placement business at Lloyds. By the end of this year, we should have led 14 transactions in 2013, raising just short of $4bn for UK corporates.

David Cleary,
Lloyds Bank

Rob Jennings, Mitie Group: We entered the market for the first time in 2010 and again in 2012, when we took a mix of dollars and sterling.

Jane Pilcher, Anglian Water: We first accessed the US private placement market at the end of the '90s and then went through a complicated restructuring of our debt which involved a novation process with our debt investors. The majority of our US private placement noteholders opted to be repaid at the makewhole price. Then we had a period of absence from the market, but then since then we've issued four or five times, including in dollars and sterling.

Stephen Wheatcroft, BBC: We were a first time issuer in June-July this year, for about $256m.

Donald Campbell, Pricoa: I joined Pricoa at the end of 2006. I work in the London office as a senior vice-president, managing a team. We have three teams in London covering Ireland, the UK and the Netherlands.

EUROWEEK: The last couple of years have been busy for the PP market, for European issuers including in the UK. Was that because companies found it hard to get bank finance? And if so, what is driving deals now that bank lending appears plentiful?

Douglas, Deloitte: Recently, there's been lots of bank liquidity, but we think that's going to change, so we've taken pre-emptive action. Clearly that's an unfashionable view at the moment, but longer term, we think conditions will become more challenging, so we decided to add some core, longer term debt.

It's our view that long term rates are going to go up, so locking in 10 year money now made a lot of sense, and the pricing was very attractive. We've never issued long term debt in any other market.

Macphail, M&G: It wasn't necessarily a lack of bank liquidity that was driving transactions in the 2009-11 period. It was a concern that liquidity might not be there when companies actually came to need it. So they prefunded upcoming maturities with an element of private placement debt.

More recently a lot of the transactions have been driven by a desire to lock in long term funding when people perceive rates will increase.

Weiler, White & Case: Yes, I would agree. Even before the banks were not lending, it was still a very robust market, because it allowed investment grade corporates to diversify their lender base and get fixed rate money, much longer than the bank market. I do think the shrinking of bank lending right now is creating an opportunity in the private placement market in a lot of other, non-classic areas, like shipping, aircraft and other types of asset-backed financing that might previously have gone to the bank or bond markets.

Dix, Rolls-Royce: We've issued several times to finance our aero-engine leasing joint venture companies. They operate in US dollars, the natural currency for the US private placement market.

For our core long term debt, we analysed various financing alternatives. Private placements have a number of advantages. They allow us to diversify funding sources away from the banks and obtain longer maturities. The sweet spot for private placements is 10-12 years. In the bank market, you'd do well to get over five years. That allows us to match our debt maturity profile with the lease terms we write.

And what we've found recently is that we're able to raise 10-12 year US PP money at pricing comparable to five year bank debt, which obviously works well for us.

Valvona, Lloyds Bank: Historically, the ability to diversify away from banks has been a strong selling point. Treasurers want opportunities not to put all their eggs in one basket and to access another pool of liquidity that has no need for ancillary business.

That means when opportunistic items come up, like M&A or other strategic financing needs, there's liquidity left in the bank market that they can take very quickly and then look to bring the debt into capital markets later.

Campbell, Pricoa: Most of our business is refinancing. It's following a secular shift from mostly bank funding to a broader mix of bank debt and private placements.

We are seeing a lot of new names, happily – about 60% of our business this year has probably been new borrowers, so the shift from bank-only to shares of bank and long term debt is still going on, and the market is still growing.

Hitchcock, New York Life: I think Calum hit the nail on the head earlier. It's not necessarily a purely bank-driven dynamic. In my view the biggest change over the last 10 years is the desire for issuers to know their investors, to have the same kind of relationship with longer term debt providers that they have with the banks.

That shift was reinforced by the financial crisis. There was some recalibration of bank appetite, particularly with banks focusing on their home markets, but liquidity's extremely strong again now in the bank markets.

But the philosophical shift isn't changing. Issuers are looking for diversification by maturity and lender and to having long term debt providers with a long term relationship. That is what has driven the private placement market over the last few years and I think it will continue.

Rob Jennings,
Mitie

Cleary, Lloyds Bank: I agree. The financial crisis caused corporate boards to reassess their capital structures. We've had increased levels of enquiries from UK midmarket clients looking to diversify and access the market.

The challenge is whether the market can accommodate corporates of that scale. This year has been interesting, because the Funding for Lending scheme has meant that banks in the UK have been eager to lend. The relationship side of our organisation has been putting sizeable balance sheet commitments out there to UK PLC, so our product is competing with the bank to some extent. But issuers continue to come, and I think it's more strategic than liquidity-driven.

EUROWEEK: Do you think James is right to think banks' lending capacity is going to become constrained?

Cleary, Lloyds Bank: My colleagues in loan markets will tell you that the demand by banks for lending is phenomenal and pricing is tumbling almost on a weekly basis. Large numbers of banks are bidding and overseas banks are moving back into the UK market, so we don't see that in the short term.

I think James is right, in the long term, bank liquidity may be an issue, but in the short term, if you're in northern Europe and you're investment grade, the bank market is absolutely wide open for you.

However, although there's plenty of liquidity there from the banks, the pricing on PPs at the moment, when swapped back to floating rate sterling, is often cheaper than where companies are getting new five year bank facilities.

That arbitrage is here to stay. With increased regulation pushing up the banks' cost of capital, bank finance is unlikely to get back to the levels seen pre-financial crisis.

The cost of borrowing for banks is higher than it's been historically and long term interest rates are relatively low still, because of the impact of intervention. So you've got this dynamic where the benefit to corporates is to go longer and still receive a pricing benefit.

Jennings, Mitie: Although liquidity's returning, the tenor isn't. If you go back to 2009, bank deals were coming in from five years to three years.

You could have funded some deals with bank debt in the past, but companies got pushed to the PP markets because tenor is key. Diversification was also key for us – having a mixed investor base rather than just the four main UK funders we had at the time.

EUROWEEK: Your private placement in 2010 was the first time you'd gone out of the bank market?

Jennings, Mitie: Yes, and tenor was a major issue. At the time we weren't too sure exactly where we wanted to be, tenor-wise, but we ended up taking seven and nine year debt. We'd seen our ability to get five year bank money being pulled in to three and a half years in 2009, so tenor was absolutely key. We use debt really for acquisitions so our core debt should have a closer alignment to payback from our acquisitions.

Pilcher, Anglian Water: In the sterling capital markets, there's been a drive for larger and larger public bonds. Probably now £300m is the minimum preferred benchmark size. On occasion, we are keen to raise that amount, but the US PP market enables us to raise smaller amounts of financing as well.

What I've also found is that the sterling public markets in times of crisis are like kids in a sweet shop, they're looking for distressed assets and not so keen to invest in stable, more expensive credits.

The US investors are more about long term relationships. Even in times of market disruption, they've got a certain amount of cash they're looking to invest. What they're after is a long term, steady investment return compared to Treasuries, whereas in the public markets in sterling, investors are seeking value opportunities. It seems to us on occasions, they don't want boring, stable, steady returns.

Actually it's then meant some sterling investors have come to me and said, when are you going to come back to the sterling market? Maybe it's been quite good to give them a bit of competition.

Wheatcroft, BBC: The BBC's quite unique as it has borrowing limits determined by the Department of Culture, Media and Sport and HM Treasury.

But although our overall on-balance-sheet debt requirement is relatively modest, we have found in terms of pricing loan facilities that the modest level of ancillary income we generate has had an impact on the ability of some banks to lend to us.

Our organisation is obviously at the higher end of the credit spectrum and that does present a challenge to the banks in terms of justification for lending. So diversification was a big driver for us to come to the market.

We also wanted to lock in some fantastic rates that are likely to go only one way from here, and extend our maturity profile. The market was a perfect fit for what we were trying to achieve.

EUROWEEK: Are the long term relationships with investors that Stuart mentioned really valuable to you?

Wheatcroft, BBC: We're just embarking on this journey, but

Stephen Wheatcroft,
BBC

one of the reasons I wanted to go on the road was to start that relationship on a positive footing, because we are asking these investors to make a significant investment in the business.

Actually going and explaining the business thoroughly, looking into each other's eyes and starting to build that relationship of trust is pretty important. I see it as an active relationship that we invest in and manage through time.

From a selfish perspective, if we do get to the stage of needing any consents or approvals from investors at any stage, that's much more likely to be forthcoming if we've had a constructive dialogue through time. But it's also about just treating our investors fairly and having an open and collaborative partnership.

Dix, Rolls-Royce: We consider it vital to maintain strong relationships with our investor group, for a number of reasons. We see US private placements as an important market which we'd like to access again, so we try and build relationships as strongly with our investors as we do with our banks.

That can be challenging sometimes, because the investors are based in the US, so face-to-face contact might not happen as often, but we certainly welcome the US firms opening offices in London.

Stephen Valvona,
Lloyds Bank

Valvona, Lloyds Bank: Over the last few years, there has been a lot of repeat issuance, about 50% of the deals. If you've got strong relationships, and you've continued to feed information to your investors, it makes it easier for them to support you, whether you have M&A going on, or additional refinancing you want to do.

Hitchcock, New York Life: For repeat issues in particular there's a trend towards companies being much more selective about the investors they go to, perhaps making a small offer to existing investors. Once upon a time, they would go out to everybody in the market, but now that's not the case at all. We've certainly seen a trend towards London-based club deals to have London-based relationships.

EUROWEEK: Calum, do issuers make an effort to keep up the relationship with you?

Macphail, M&G: In any portfolio, there's always going to be a spread. If it's a PLC, they're typically going to have to come to London and talk to the equity community, so it's easy for them to then come and have a cup of coffee with us and a conversation about how things are going. And for the rest we try to be proactive and go talk to them.

When the investors are on the other side of the Atlantic, it can be more difficult. Certainly, in the '08-'09 period when issuers were coming for covenant amendments, the relationship aspect of the market was tested in a way that I'm not sure everyone was entirely happy with.

Some issuers had worked at their relationships and that paid dividends. Others hadn't, or the investors hadn't worked as hard with the company at retaining the dialogue.

EUROWEEK: Jane, when you weigh up the burden of doing investor relations for a bunch of PP deals compared with for your public bonds, which is bigger?

Pilcher, Anglian Water: About three or four weeks ago I was out on the road in the US. We were planning a new US transaction and were visiting investors in several states in a very short period. It's very gruelling, relative to going to London or Europe for a roadshow.

Usually we offer a semi-annual investor call for our US investors to run through our results, we won't typically go out and do that same trip once or twice a year for existing investors.

But one of the beauties of this market is the annual industry conference in January, which gives you an opportunity to go and visit investors in a more informal environment. Typically I'll meet 20 or 30 investors over three or four days in a nice environment, compared to seeing less than a handful over three or four days of brutal time difference.

Hitchcock, New York Life: A relationship is what you make it. The minimum level of maintenance is very low. In many respects, it's un-burdensome and that's one of the attractions of the market. But issuers really enjoy the relationships and they try and do more than an annual update conference call – this is particularly helpful should issuers require further capital or other support.

Jennings, Mitie: We don't see it being quite as embedded, maybe, as bank relationships, just because of the ancillaries that come with a bank relationship. It's all about making sure the investors are informed, so they can be supportive for the next deal, or if there are any issues on the way.

EUROWEEK: James, with $1.5bn of PPs, you probably have quite a lot of investors, or have you tried to keep them a concentrated group?

Douglas, Deloitte: It is quite concentrated, but on this relationship point, we think three things are important in the context of the banking market. Firstly, quantitative easing is going to end and when it does, there'll be less bank lending. So longer term institutional relationships are important to us.

Secondly, we have a requirement for core debt in our business and the private placement market allows us to access longer term debt.

Thirdly, Basel III is going to drive up bank lending costs, and banking is also going to become a much more asset-backed business. We don't have any fixed assets, so relationships with the private placement market are crucial for us.

EUROWEEK: Andrew, are there any legal difficulties in maintaining a relationship with PP investors at the same time as being a public company, for example? Has that issue changed over the years?

Weiler, White & Case: No, generally no. Public companies have not had a problem discussing issues with their investors. If you are a UK listed company and you're disclosing material non-public information to a non-bank investor, you don't have the same benefit of exceptions that you would otherwise and you might have to be careful about how many people you talk to. But it's a pretty rare situation that once you've done the deal you would ever need to disclose that kind of information. In terms of managing the disclosure aspects, it's quite similar to the banks.

EUROWEEK: It's been a very strong year or two in the public bond market, and public investors have become more willing to buy sub-benchmark and unrated bonds, especially in euros. So is the public market encroaching more on the typical space of the PP market?

Macphail, M&G: At M&G we have always bought those unrated, sub-benchmark public transactions, so there hasn't been a change in our approach.

Many of our peers have not. There have been more transactions, yes, but the number of investors looking at them has not increased.

While there may be advantages to doing a sub-benchmark Eurobond, it doesn't necessarily offer all the advantages a private placement can. Certainly, you don't see the same range of tenors.

Valvona, Lloyds Bank: If you do a sub-benchmark euro deal of €300m, you're still having to do all €300m in one five or seven year bullet maturity. In the private placement market that same transaction can be put into as many tranches as you like.

So the flexibility of the private placement market, things like multiple tranches and delayed draw funding, still gives it a competitive edge.

Campbell, Pricoa: I think it's actually the converse: our market is opening up new opportunities for investing, in addition to the public market. Universities and housing associations are coming to our market. Traditionally, they'd have been rated and gone to banks or the public market.

We manage quite a bit of institutional money in the US and we're getting enquiries in the UK from pension funds, insurance companies, thinking about getting into our market and talking to us about whether we can manage a portion of their assets in fixed income.

So I don't see our market being squeezed or pushed aside by the public market – there seems to be room for both.

Cleary, Lloyds Bank: If you speak to public bond bankers there tends to be a caution about bringing unrated issuers to market. They want to know the location of the listing, where is it going to price, the likely liquidity and trading volumes.

Whereas in the PP market, we're much more certain on the comparables and where an issue is likely to price. Being able to have meaningful conversations with investors helps.

So I agree with Donald. It's the other way round, this market's encroaching on to the public space in some respects. Obviously you've also got the retail bond market at the smaller end that butts up against us a little bit.

But the health of this market is demonstrated by the fact that we get much more incoming enquiries now from potential new PP investors, through our public sales desk. They want us to come and explain the product because they're not buying privates at the moment, yet they're seeing a market that's healthy, that's active, and they'd like to get involved.

Steve and I were out earlier this week talking to investors about what a note purchase agreement looks like and how it works in reality.

EUROWEEK: And these are some of the investors that banks in the market have been knocking on the doors of for the last decade and being essentially turned away?

Cleary, Lloyds Bank: Yes, to some extent. Demand is very strong for PPs in the US but we'd like to have pools of liquidity as well in the UK and the euro markets. We're not seeing those coming through yet. Though as I say, in the last six months, we've had more enquiries from large, UK-based institutions asking, how does this work? How do we get involved? What will my team structure look like, etc?

EUROWEEK: Have any of them started to buy?

Cleary, Lloyds Bank: If we have a broadly syndicated transaction, we always advise our public salesforce. They'll phone up the key houses and say, there's a roadshow on this day, do you want to come along? They have attended, but they've been very selective. It's linked to the sectors Donald alluded to, education, housing associations, regulated entities, really. I can't think of a corporate PLC deal they've bought into that we have led this year, but I'm sure it's not far off.

Douglas, Deloitte: But it's fair to say – I sat on the Breedon taskforce on non-bank lending last year – that apart from the UK Prudential [i.e. M&G] there's been little progress in developing the UK investor base. It's been like wading through treacle, hasn't it?

The Association of Corporate Treasurers did a good analysis on the issues impacting on the development of the private placement market in the UK. The ACT paper said there were numerous minor issues inhibiting market development. Individually none of them are that significant, but trying to solve them all is more effort than anybody seems to be prepared to make, amongst the large institutions.

James Douglas,
Deloitte Debt Advisory

It's credit training, it's fund allocation, it's liquidity requirements. There are a host of obstacles for large UK institutional investors.

Macphail, M&G: The opportunity is hampered to some extent by the success of the US market. There's an infrastructure and an investor base that's built up. When a UK company comes to market, where do you go to ensure ease of execution? Your bank is probably saying 'There's a ready pool of capital in the US. Let's go there and raise the money.'

Campbell, Pricoa: I think you'll see pension funds and possibly insurance companies allocating to PPs. Their advisers are increasingly looking at how they can invest through fund managers like Pricoa Capital and M&G who have the skills, infrastructure and the commitment to the market.

Macphail, M&G: That's true, but there are still a lot of misunderstandings and misconceptions about what the market actually does and what it offers.

Hitchcock, New York Life: Something that hasn't been raised is the pricing dynamics. As US investors, our ability to analyse credit or price a transaction is based on relative value, compared with other credits we can invest in, such as in the public bond market.

There is a wealth of publicly traded bonds in the States, which in certain sectors can trade more tightly. So we can be aggressive price-wise and that can create an arbitrage for issuers at certain maturities.

Pilcher, Anglian Water: There are a few investors who buy publics and privates, who would not participate in one of our private transactions if they considered the pricing was significantly tighter than the public price. In a way we see it as quite good news if they don't participate, because it means the pricing on the PP is probably quite attractive for us.

Cleary, Lloyds Bank: Jane, how do you feel the rapid book-building process in the public market works, relative to the way, in our market, we get the bids in and then show you a spreadsheet analysis of them? And it's more of a partnership where you can upsize or change the documentation.

Pilcher, Anglian Water: I've worked with different agents and they approach that in different ways. Some would, by the time they presented the spreadsheet to us, have had that dialogue with the investors to push the pricing where they can and are trying to get every last penny for us. Whereas others have perhaps gone a little bit native and seem more on the side of the investors and are saying 'this is where their price is'.

Wheatcroft, BBC: We had quite a hard night's work to achieve the right pricing outcome. Documentation was not so complex, because we just have a pretty standard form document, but on pricing, we were presented with a good book where a lot of work had been done, but there was certainly more to do at that point.

Valvona, Lloyds Bank: Coming back to what Andrew mentioned earlier, there are now more and more structured deals in the private placement market. The PP investors are very experienced with amortising structures, more complicated asset financing, and they want to do the work and understand the deal.

Public investors can have a set mindset when they look at asset-backed transactions, and if it falls between the cracks, it can lose focus.

Dix, Rolls-Royce: Our deals are structured finance. You've got a strong credit story but, in addition to that, you're giving investors security over the assets.

Marcus Dix,
Rolls-Royce

Stuart Hitchcock,
New York Life Investments

Investors always look for the strong credit story, and you need to make sure it's clear. Irrespective of whether you've got a rating as well, they'll always do the due diligence on the credit story.

But in addition, you need to explain the security you're providing. We've spent a lot of time in recent years educating investors and our relationship banks on the robust residual value characteristics of aero engines, and why they represent strong and attractive collateral.

That's worked well for us, although it's taken a lot of effort, because today we've got over 20 financial institutions that lend money to our leasing companies. And we've got 30 private placement investors as well.

EUROWEEK: Are your deals rated?

Dix, Rolls-Royce: The most recent one was, by Standard & Poor's. We wanted to take away the risk of the NAIC taking a different view on the rating. We thought it would be easier to explain the credit to S&P and get that in the bag, so we could come to market with a transaction and have it ratings-exempt with the NAIC.

Investors have welcomed that, because it's given them certainty about what the rating will be.

Hitchcock, New York Life: Marcus brings up a good point. Issuers really appreciate the fact that we spend time analysing the credit, getting to understand their story and their history.

Because we do that, a structural advantage of the private placement market is that it remains open. Whereas the public market will go through windows of opportunity, and can shut for periods, the PP market has remained open, after 9/11, through the financial crisis etc.

We are long term asset and liability matchers and we have to put money to work. Where we have good credit stories we will make investments, regardless of what's happening in the wider world. That's one of the core advantages of the market – we like to understand and analyse credit properly.

Wheatcroft, BBC: That's true. The level of analysis we faced from PP investors was more rigorous than anything we'd faced from banks over the years. Really good quality people are analysing the credit, and you get some excellent questions... I wasn't expecting a dozen pages of Q&A. I was genuinely very impressed.

That gives you confidence as you go forward. This is a transaction that's been bought into with very thorough due diligence and this plays back into that whole relationship and continuing to keep people informed as we go along.

EUROWEEK: Rob, your deals are not structured, but you used them in a specific way, for acquisitions – how did it work, getting that story across?

Jennings, Mitie: It was challenging. With the second deal, we approached the market while we were doing due diligence on the acquisition. We had a pro forma balance sheet and obviously we could point to a previous transaction where investors were comfortable with Mitie's credit.

We had to explain to the investors why it was right for Mitie to move into a different field, from facilities management into domiciliary care. Our finance director was instrumental to explaining that on our conference call in the US.

Cleary, Lloyds Bank: Mitie also chose not to go and meet the investors in the US. So there was, as Rob said, a two and a half hour conference call with them. There were a couple of questions that you passed to the investor relations team and they answered.

In fact, there were fewer questions incoming from the investors on your transaction than there were on Stephen's – and with the BBC you'd expect people to be much more comfortable with the credit. There were a lot of questions over the BBC's business model and the licence fee, which was alien to the US investors.

Wheatcroft, BBC: Yes, the US media model is very different. Understanding that the Corporation is incorporated under a Royal Charter and doesn't really have any owners in the traditional sense, it took a little bit of explaining, but we got there eventually.

It was interesting, because we marketed in the UK as well. It all came down to pricing at the end of the day. But we did end up with a transaction that was wholly funded by US investors. That was a shame, but next time round I hope we'll get some UK uptake.

Pilcher, Anglian Water: We've been raising money in dollars and turning it into sterling, so one of the dynamics that influences the pricing for us is the swap spreads. On our first transaction, in 2011, we had a benefit as a consequence of the swap spread, which meant that just the market dynamics helped us on the pricing.

Douglas, Deloitte: We swapped back into sterling when we raised 10 year money for pretty much the same pricing as we got for five year bank facilities. We got the extra five years for comparable pricing, so for us it was an attractive deal.

Cleary, Lloyds Bank: It's not just the level of the basis swap to get back to your currency, it's the availability of swap lines as well, and the cost of them.

It clearly depends – if you're the BBC the swap is a lot cheaper than if you're in real estate or construction. The availability of lines from banks will be a big driver going forward.

Weiler, White & Case: Plus you have the advantage that in the private placement market the investors will swap for you. Some corporates may not be experienced in it or have internal reasons why swapping is problematic for them. Investors will do it for you, and while there is a cost to the issuer for that, the investor will often get better terms for a swap than the issuer could.

It's been around for a while but we've seen a lot more deals recently with embedded swaps.

Campbell, Pricoa: I would echo that. There are more natural sterling borrowers coming to the market – in education and social housing, and like the BBC.

International corporates, who were the mainstay in '06, '07 are a little subdued currently, perhaps because of the lack of M&A. As the economy picks up we'll probably see more dollar issuance. But we've done a lot of sterling and euro lending this year.

The basis swap advantage has been very good, particularly in euros; it's a really significant difference. So we're getting good economics, relative to US publics. And they can still provide really attractive economics for the issuer.

We have natural dollars, we don't have a sterling business, so we hedge our currency exposure by swapping with counterparty banks.

Macphail, M&G: But the borrowers are ultimately indemnifying you for that risk?

Campbell, Pricoa: In a lot of situations, particularly on club deals or direct transactions, we will do natural sterling transactions without swap indemnity.

Jane Pilcher,
Anglian Water Group

Pilcher, Anglian Water: On the transactions we've done where the investors have done the swap, we've given protection only in the event of makewhole.

We brought a club deal last year which we specifically wanted to have issued as sterling notes. We priced it off US Treasuries but then the investors did the swap.

At the time the banks were quoting a significantly higher cost for the swaps.

Wheatcroft, BBC: We just had synthetic sterling and that was a challenge, just because of the swap breakage language. It took quite a long while to get my head round it and get comfortable with it. But we only took one tranche that was swapped with an investor. The rest of it we took in dollars because the swap credit charges that we can procure with our banks, especially after some manoeuvring, were under the price investors could provide.

EUROWEEK: Stuart, do you offer this kind of flexibility as well?

Hitchcock, New York Life: Yes, we're in exactly the same situation as somebody like Pricoa. We can provide all major tradable currencies, for the right issuers. We're selective about it but we can absolutely provide it. This year, a significant portion of our transactions in London have been in direct currency.

Dix, Rolls-Royce: We've talked about currency, but we've also recently done a transaction where we took a large proportion in floating rate dollars. I think it was the largest floating rate PP ever. That was a mixture of natural and synthetic or swapped floating rate note providers. We've seen good availability in the market for that type of transaction as well.

EUROWEEK: I want to come back to the question of UK and European demand. Anecdotally it's clear there is growing interest, several people have mentioned that. But you've also described it as like wading through treacle. Are we moving towards there being a different UK/ European private placement market, alongside the US one? Or is it more about investors in Europe joining the US PP market?

Weiler, White & Case: There are a number of issues. The investors need to have the credit analysis, but that is quite manageable. You could hire a team if you wanted to. The most challenging issue is regulatory, because it's not a liquid investment or listed on an exchange. That creates all kinds of problems and limits for insurance companies and pension funds. That is going to be the biggest hurdle because it requires governmental intervention to open up.

If it's not publicly traded they have issues in terms of how they value it. There are also valuation models that can be applied, whether internal or not, especially if it doesn't have a formal rating. Often you need 10 years or more of history to mark it to market, and they may not have the comparables to be able to do that. So they can get punished in terms of balance sheet allocation.

Andrew Weiler, White & Case

Then there are other issues, like tax gross-up. Listed securities can get exemptions from tax withholding. US investors are very comfortable that they can trade unlisted PPs if they want to get out, even though they are buy and hold investors and the secondary market is fairly small, because there's a big US market to trade them in.

But if UK and other European investors want to sell, it could be to someone overseas. And the documentation provides that you don't gross up if you're not in the original jurisdiction of the investors.

Pilcher, Anglian Water: Although we've issued our notes under US private placement regulations, they are actually listed on the London Stock Exchange. We were absent for a long time, partly because we felt the traditional US PP investors wouldn't buy our notes. But in fact they have purchased several issues. So that might be a solution other European issuers could look at.

EUROWEEK: One of the arguments why European investors have not got into PPs is that they fail to see the value of covenants the way US PP investors do. Is that changing?

Cleary, Lloyds Bank: We don't always get financial covenants on bank loans to some European corporates, so that can prohibit them coming to our market.

Valvona, Lloyds Bank: That's particularly common in the Nordic regions and Germany, where you have very strong local banking relationships. A company that would normally require financial covenants can have a bank deal that's completely free of them. So it can be challenging to explain to issuers why they need to give covenants to the private placement market.

For the investors, I think more of them are beginning to see the point of covenants. After 2008 a lot of companies suffered from stress and covenants and additional protections were more valuable, even if only as early warning signs.

On the public bond side, all you can do is hope that if things go wrong, you can sell it. And if things do start to go wrong, the market tends to become illiquid pretty quickly.

Macphail, M&G: There is definite growth in interest in PPs in Europe but it's manifesting itself in a number of ways. We still have local markets – the Schuldschein market in Germany has grown strongly in the last couple of years. The French market has gone from nothing to €6bn in 18 months, which is frankly incredible. There are people talking in the Netherlands about how they create a solution; Italy's done some reforms to try and kickstart a market.

For me, the question is whether at some point all these people start talking to each other and you get a genuine European market, or does it continue to happen on a more regional basis. The obvious exception is the UK, where, as James said, there have been a number of reports and discussion about how we do something but no tangible progress.

Douglas, Deloitte: I'm pretty gloomy actually, I think it's going to be very difficult to get the UK market to develop. Many of us around the table have been trying for a long time.

EUROWEEK: Anyone disagree? Are the big UK institutions about to embrace change?

Cleary, Lloyds Bank: We would absolutely love to have more investors in London and in Europe for our clients to go to, and we're doing our best to move it forward. But as James said earlier, it's like wading through treacle.

Campbell, Pricoa: I would agree with that.

Valvona, Lloyds Bank: I do think, though, that there are opportunities in third party money management for those investors. That possibly is more of an opportunity in the near term. There are investors looking to find partners who can invest money for them in this product.

Macphail, M&G: There are, but you're still having to sell a story that's quite long term. You're not entering this market to get a big yield pick-up. It's all about risk mitigation and protection and stability of cashflows and returns, rather than shooting the lights out in terms of yield.

And sometimes, when there are other markets offering higher returns, that can be difficult for someone to pitch to their CIO. So I'm not necessarily the most optimistic person but I don't share quite James's gloom. It's just that there is still education to be done. One of the things we have been talking to people about is the opportunity to diversify your portfolio with new corporate names.

EUROWEEK: Is there one thing you would like to change about the market?

Donald Campbell,
Pricoa Capital Group

Jennings, Mitie: Well, you still have to get your board comfortable with the uncertainty of what happens between circle price and funding… all you can say is it's always worked in the past. But by the time you've done it a couple of times they're comfortable with that.

Cleary, Lloyds Bank: That's a question we get all the time from debut issuers: 'I've priced the deal and done my swaps – how many times have you worked on a deal that's not happened after that?' For me, though, it's the leap from NAIC 2 to 3 for US-based accounts. We have an army of UK midcap businesses that would look to access the market, but they can only go to sterling investors because of this NAIC 3 risk.

Usually it's not because of their leverage, their Ebitda is just too small, so they would end up being rated as NAIC 3. It's penal for US investors to hold NAIC 3s, from a capital allocation point of view. Without that, more investors would look at these issuers and the pricing would be better.

Pilcher, Anglian Water: For me it's the holding of the investor register – bringing in a little bit more uniformity and maybe having more players involved in that. Because of the amount of work involved, we outsource it; I don't know if other issuers hold the register internally or outsource it. But there are a large number of transactions out there. Having some consistency as to the management of the register would be good.

Hitchcock, New York Life: What I'd like to see more of is businesses being introduced to investors very early on in the development of their capital structures. Even if they're not in a position where they can currently do something, developing a relationship for the long term is important. It could benefit them and us in the future. I do see an increasing amount of this happening.

Campbell, Pricoa: My change is the opposite to David's. We have appetite to go down the credit spectrum, but we don't see enough crossover credits, the triple-B minuses, double-B pluses. We would like to see more.

It's partly pricing but I think equally the banks have got so much money that prising these names away from the relationship managers is very tough.

We've tried to build partnerships with some of the high street banks. There's always willingness on the capital markets side, but as soon as you get outside that, into the regions, it seems to fall over flat.

Valvona, Lloyds Bank: I'd like to see more issuance. At the moment there is liquidity and there is a real opportunity. There are smaller corporates that are run very prudently with conservative balance sheets and one times leverage, but just suffer from being in that £40m-£75m of Ebitda category that might fall foul of the NAIC. We'd like to see more access for them.

But also, some larger corporates are looking at the market and waiting to see what is the value. The euro market's really a 10 year market, so 12s and 15s is something we can offer that's different.

Dix, Rolls-Royce: One thing we find is that we spend a lot of time crafting the offering documentation, and are then advised by the agents that it needs to be posted on to intralinks two or three business days before we go on a roadshow. I question whether that gives some investors who have lean teams sufficient time to go through the documents and facilitate the best discussion on the roadshow. On a recent roadshow we had a split between investors who quite obviously hadn't read the documents before, which didn't help a productive two way discussion, and those that had done their homework.

Weiler, White & Case: I'll pick on the NAIC again, which is moving in the right direction, but on the recognition of financial statements. They have a limited pool of accounting principles that they accept right now: IFRS, UK Gaap, US Gaap, Australia... They're trying to figure out how they can get comfortable with other ones.

In a lot of places, including northern Europe, central and eastern Europe, southern Europe, public companies may already be reporting under IFRS. But large, private companies like you see in a lot of these regions may be using local Gaap, which means the NAIC cannot give a designation to the notes.

So issuers would have to get a rating, and that could defeat part of the purpose of this market.

Calum Macphail,
M&G Investment Management

Macphail, M&G: I want to see a European or UK private placement market that gives potential borrowers a genuine alternative to going to the US.

Douglas, Deloitte: We need more flexibility from investors around the makewhole calculation for difficult situations. I appreciate it's a thorny subject but it is an impediment to issuance. As an adviser it's the one thing you always stumble over.

The company doesn't know what's going to happen over a 10 year period. Unforeseen corporate developments can happen, and the penalty for getting out of one of these transactions is so significant that many are put off it. ▲

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COMPASS GROUP $500 Million Placement Agent	British American Tobacco £650 Million Bookrunner	bp €600 Million Bookrunner	EQUINITI £440 Million Global Coordinator
BBC Commercial Holdings $260 Million Placement Agent	AA £350 Million Bookrunner	M MORRISONS €700 Million Bookrunner	Thomas Cook Group €525 Million Bookrunner
Vitol $814 Million Placement Agent	HIGH SPEED 1 £760 Million Bookrunner	BACARDI LIMITED €650 Million Bookrunner	towergate £396 Million Global Coordinator

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