A big deal

MYLES MCBRIDE EXPLAINS THE BACKGROUND TO GLAXOSMITHKLINE'S SUCCESSFUL ISSUANCE OF $9BN OF SEC-REGISTERED BONDS.

In July 2007, GlaxoSmithKline announced a £12bn share buyback programme, to be completed over a two-year period. This was to be financed with debt and consequently alter the capital structure of the company. At the time, Glaxo was rated Aa2/AA and was one of the few AA corporates worldwide. There are arguments, more vociferous in the last 12 months, that to guarantee debt market access, the higher the rating the better. But pragmatically speaking, anything rated A or better should be assured of good access in all but the very worst markets.

Glaxo worked closely with the rating agencies on the new capital structure. In July 2007, Moody's assigned an A1 rating, while S&P maintained its AA. Only in February 2008 did S&P lower that rating to the current A+ with a stable outlook. Indeed, even at this point the ratings were not identical, as Moody's had assigned its A1 rating a negative outlook.

Finding significant liquidity in these challenging times is far from easy. For many corporates, securing funding in connection with, say, a major acquisition is possible, but only with the express intention of a 'take-out' in the capital markets. Treasurers will no doubt testify that the pressure to reduce the time between drawing bank lines and undertaking refinancing is much higher than it was just a year ago. But bank lines were not the solution for Glaxo in this instance; there was no acquisition and, importantly, no single funding event. The repurchase programme is a rolling one, averaging around £500m a month.

Glaxo is no stranger to the capital markets. Indeed, it has enjoyed access to euro, sterling and dollar markets previously. Although it had not raised dollars since 2004, the company was fully aware of the depth of liquidity in that market, and also its relative reliability since the onset of the credit crunch. With an objective of $6bn or more in a single exercise, there was only one market to consider.

In late 2007 work began on the documentation for the dollar financing. With that process under way, Glaxo demonstrated its maturity and expertise as a borrower by issuing an opportunistic sterling bond in March 2008 of £700m, a relatively large size for this market, and executed in one of the very few strong market windows that the sterling market had seen since the onset of the credit crisis. The 31-year maturity was a neat trick, taking advantage of the long end demand in sterling (where there is flexibility to choose off-the-run maturities) while keeping the 30-year free for the dollar issue. The dollar market is much more rigid with tenors.

The documentation platform set-up was a well-known seasoned issuer (WKSI) shelf registration, which is available to the majority of corporate borrowers. This differed from the format used in 2004 which was an old-style dollar shelf. The bonds are SEC-registered securities, ensuring the broadest possible investor interest to maximise capacity and price tension.

With the documentation in place, the key decision was the timing of the issue. This is important in every transaction, especially in volatile markets, but in this case it could not have been more so with an objective of size and with a story to be told around the recent capital structure and rating changes. The week beginning 5 May was targeted, and, with a UK bank holiday on the Monday, it was decided that if conditions were conducive, the bookrunners would announce the transaction on Tuesday morning (6 May). Since the US was open that Monday, Glaxo and the bookrunners had a market update call on the Monday evening (UK time) to see how the market was faring in the US. At that stage it became apparent that, barring any overnight detrimental news, Tuesday would be the go day.

The transaction was announced swiftly after the New York open, partly to ensure other borrowers were kept on the sidelines and partly to give European accounts time to look at the deal and place orders before they left for the day. The bookrunners had given major consideration to allowing a two-day process (rare in the US), but Europe needed to know that there was always the possibility that it could complete in one day.

The announcement specified there would be maturities of five, 10 and 30 years, with $2bn per tranche. It was important to give guidance on size, given that the word 'benchmark' implies a minimum of just $250m in the US and could have been misleading.

The credit story is vital, and it was key that the messages were effectively delivered. Glaxo CFO Julian Heslop represented the company on a global investor call, giving an audio presentation attended by more than 130 investors and then taking questions from the attendees. In addition, Glaxo had prerecorded an electronic roadshow, which was made available via Bloomberg. It is Glaxo policy not to offer one-on-one calls with investors, to ensure that all investors have access to exactly the same information. The number of investors on the call, and the nature of the follow-up questions,

Executive summary

- On Tuesday 6 May 2008, A1/A+ rated GlaxoSmithKline priced a staggering total of $9bn of SEC-registered bonds in four tranches.
- The proceeds were to be used for general corporate purposes and to help finance a £12bn share buyback programme.
- The deal was the largest ever pharmaceutical debt issue, and followed AstraZeneca's $6.9bn deal in September 2007. It was also the largest corporate issue since 2002 and the largest yankee issue since BT's $10bn back in 2001.

showed the interest in the Glaxo credit. Despite the ensuing two-notch downgrade, investors were still confident that the company was committed to a strong investment-grade profile.

It became clear very quickly that the communication strategy was effective; investors bought into the story and were actively doing the credit work and submitting orders. Momentum built quickly and a number of points became clear within a few hours: the desired size could be achieved, a floating-rate note could be added at the short-end, and the trade would close in one day. Given the investor dialogue on the fixed–rate tranches, the floating-rate note discussion was straightforward and Glaxo opted to fund $1bn at two years. This was noteworthy as liquidity in the short-end had been limited, open to very few borrowers.

Price guidance was released as T+175bp across the three fixed tranches and three-month dollar Libor +65 on the floating-rate note. By the time the book went subject ahead of pricing, orders stood at a massive $17bn (from almost 400 investors). But most important was the significant volume of top-quality accounts, with sizable orders showing their commitment to the issuer and to the transaction. Given the strength of demand, Glaxo was able to tighten pricing to T+173bp and Libor +62.5bp while also upsizing the overall transaction from what had been originally envisaged, resulting in $8bn of fixed-rate debt (up from $6bn), plus the $1bn floating-rate note.

When the deal was freed to trade, the scramble for bonds (given the scale-back at allocation) pushed spreads a few basis points tighter, as was expected. The absence of any significant spread movement indicated that the bonds had been appropriately distributed, correctly priced and that the issuer had once again done an excellent job in the capital markets.

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NOT FOR THE FAINT-HEARTED

Accessing the US market is not for the faint-hearted. The up-front costs are substantial, the documentation requirements onerous, and there is always the knowledge that you are about to issue debt into the most litigious environment in the world. However, the reason for going through such an arduous up-front process is clear: access to the deepest market at an impressive speed, which has become a much more critical point over the past year.

As Glaxo already has a US registration for equity and regularly files company information with the SEC, establishing the WKSI shelf did not mean we had to start from scratch. The documentation process started back in December to ensure we would be ready to issue debt should a window of opportunity become available once the 2007 20F disclosure had been filed with the SEC.

Glaxo last visited the US market in 2004 and it was clear when we announced the £12bn share buyback programme in July 2007 that we would want to access this market again. We have watched developments throughout the credit crisis to ensure we could pick a relatively calm period in which to launch. Nearer to the issue date, we were aware of rumours of a number of large debt deals about to come to market and this meant that the pressure was on to ensure we were first in the queue.

Glaxo has a particular style of debt issuance. Due to numerous black-out periods, we will never be an opportunistic issuer, but tend to come to the market in size when all the stars are aligned. We consider that the relationship with the investor is long term and all-important and do not shave the last basis point off the price. Performance of the bonds in the market is very important and we work on the basis that a good experience for the investor in one transaction will encourage investment in the next. For years, we have tended to issue medium-term and long-term fixed-rate debt, which has provided the company with a sensible maturity profile at attractive fixed rates.

For this transaction, the investor presentation was critical. Glaxo does not hold one-to-one investor meetings or roadshows, as we like to ensure that all investors have access to exactly the same information. As the investor presentation was to be the one piece of marketing for this issue, we put a lot of effort into ensuring that it would cover all relevant points. Our CFO, Julian Heslop, made an excellent presentation and it was gratifying to see the book build so quickly after the call. We were able to price the deal later that day, neatly removing any worry from having the book open overnight in these turbulent times.

A transaction of this nature requires the full involvement of the treasury to manage the complex but necessary procedures and documentation. At Glaxo the whole team did an excellent job in ensuring we were fully prepared prior to launch and after the sale during the closing process.

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