

# SHINING A LIGHT ON SCHULDSSCHEIN

**WHY IS THIS PRIVATE AND FLEXIBLE GERMAN FINANCING SOLUTION ATTRACTING INCREASING INTEREST FROM PROSPECTIVE ISSUERS AND INVESTORS ACROSS EUROPE? PAUL WILKINSON FROM REGUS, AND PENELOPE SMITH FROM COMMERZBANK, EXPLAIN**



IKON IMAGE/IMAGE SOURCE

Schuldschein loans are not a new way for corporates to borrow money. In Germany and Austria, they have been a regular mainstream product and the preferred finance tool of many domestic companies for years. Now Schuldschein, which is the German equivalent of a private placement, is beginning to attract considerable attention from a broad group of international corporates and it is easy to see why the issuer base has been growing.

Schuldschein can offer companies access to an investor

base that may otherwise be difficult to approach. With a typical maturity of between three and 10 years, and volumes that generally range between €50 and €500m, their profile as the preserve of small- and medium-sized German enterprises is changing as they become the considered choice of international corporates as well.

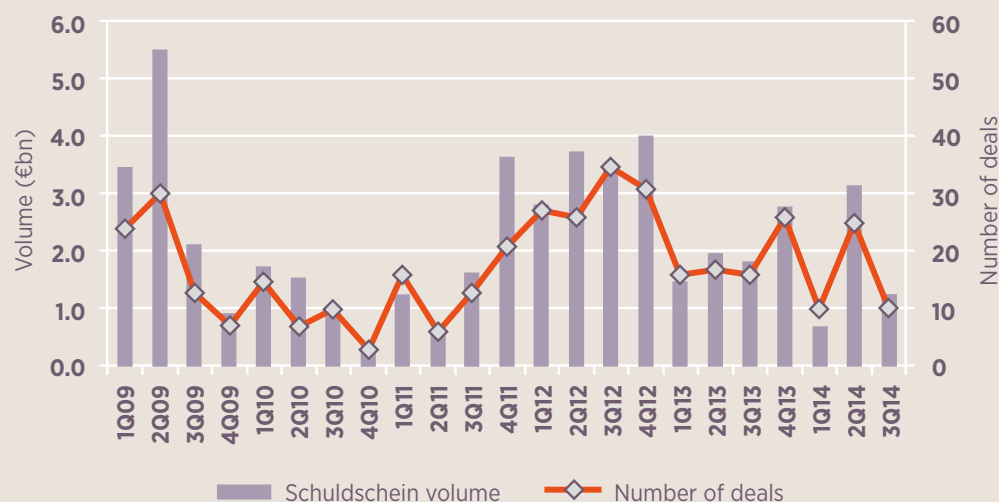
Part of the appeal of Schuldschein is that they are not a standard debt instrument and have elements of both loans and bonds in their DNA. Schuldschein tend to be less

expensive than bonds and do not need to be listed or registered at a stock exchange (meaning there is no need for a lengthy prospectus), but they are marketed like bonds. From an investor perspective, they are tradeable, but they are non-mark-to-market instruments. The documentation is shorter and simpler than loan documentation, although many of the same kind of terms are mirrored. A range of maturities, interest structures, currencies and lending amounts can all be tailored as required to deliver a bespoke product

to each borrower. As a form of private placement, borrowers can ensure such a transaction remains confidential – with minimal or no publicity if desired.

Although the number of Schuldschein issued by UK companies is still relatively low in comparison with more traditional borrowing instruments, this could be about to change. Many investors no longer require the borrower to have a German presence and are looking for strong credits in which to invest, so they work equally as well for international

## QUARTERLY SCHULDSCHEIN LOAN VOLUME



SOURCE: THOMSON REUTERS LPC

borrowers. This was certainly the case for Regus, which undertook a Schuldschein issuance earlier this year.

### Case study: why Regus chose Schuldschein

Regus, listed in the UK, is the world's largest provider of flexible workplaces. The company has more than a million customers and a presence in over 100 countries. In the first half of 2014, Regus chose to borrow via a Schuldschein issue.

Here, Paul Wilkinson, head of corporate finance and treasury at Regus, and Penelope Smith, a director at Commerzbank, talk about Regus's recent Schuldschein issue.

### Why would a UK FTSE 250 company borrow via Schuldschein?

◆ *Paul Wilkinson:* At Regus, our investment in growth is currently funded through a combination of internally generated cash flow and external debt. We do have a strong and well-balanced group of relationship banks, but we were also keen to consider how we could diversify our sources of funding.

We track various potential sources of funding, including

straight bonds, private placements and convertibles, and each of these has their advantages and disadvantages. Our CFO and I have both lived and worked in Germany in the past, so we have some knowledge of the Schuldschein market for domestic German issuers. Consequently, when Commerzbank joined our relationship banking group last year, it was logical to develop a dialogue on the potential for Regus – as a UK-listed company – to tap the Schuldschein market.

One of the funding challenges we face at Regus is how to make sure lenders understand our business model and how we manage downside risk in our property lease portfolio. The nature of good banking relationships is that you can have an

active dialogue and ensure a balanced understanding throughout the bank. This is always a consideration for us when evaluating other funding sources. If the investor base is remote, it could lead to an inappropriate risk assessment by a potential investor.

The Schuldschein market was interesting to us because issuers need to be strong credits, but not necessarily with a formal credit rating. Investors make their own analysis and we had the opportunity to present our business to them at the beginning of the book-building process. Although the number of UK issuers using the Schuldschein framework is relatively small, it was clear there were a number of features to this market that would fit well with our funding strategy.

◆ *Penelope Smith:* There are a number of reasons why a UK FTSE 250 company may be interested in borrowing via a Schuldschein because it is such a strong and flexible product. It offers a company a viable, low-cost structure to achieve attractive, confidential funding and to open up a new investor base away from relationship banks. A range of maturities can be set up within one issue, together with fixed and/or floating rates of interest and even different currency tranches – all with the same underlying terms and conditions as part of that issue.

We thought the product would work well for Regus, given the company's credit profile and desire to diversify some of its medium-term funding. Regus could seek a range of maturities and particularly liked the fact that any floating tranche would have an inherent prepayment option at par. The confidentiality aspect was also a key constituent and, >

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although the transaction closed in the first half of 2014, there was no mention in the public domain until the Regus interim results in August.

#### Was the process cost-effective?

◆ *Paul Wilkinson:* The opportunity to benefit from attractive issue costs and expenses was certainly a factor. Our needs were for medium-term funding and pricing that was aligned with the banking market, as well as an asset-driven deal (rather than dependent on ancillary cross-sell). So issuing a Schuldschein seemed to fit our needs because we were also keen to benefit from the diversification of our funding sources. In addition, we knew that if we issued floating-rate Schuldschein debt, it could be prepaid at no cost.

Nevertheless, before we agreed this approach, we satisfied ourselves that there would be an appetite for a UK-listed issuer and that investors would understand our business model so that we could achieve appropriate pricing.

◆ *Penelope Smith:* The process is cost-effective for issuers given that there is no need for rating, listing or registration. There are only minimal documentation costs given the short-form documentation that we produce in-house together with our agency costs. Pricing on the issue itself was in line with competitive levels at the time.

#### Was the issuance straightforward?

◆ *Paul Wilkinson:* Yes. As issuers in the Schuldschein market are generally unrated, investors rely on their own credit analysis. Our investor group proved to be very international. The geographic spread of investors was across three continents,

## UK COMPANIES AND SCHULDSCHHEIN LOANS

Many UK companies across a wide range of sectors could consider borrowing via a Schuldschein. It is not necessary to be listed, but it is important to have a solid credit story. Companies that would expect to fall within the BBB+ to BB+ range (whether actually rated or not) appear to be among those most attractive to investors right now.

with only one German investor. We explained our business model to potential investors in a single, London-based investor presentation that was supported by some follow-up calls.

Having decided to proceed with the issue, the first thing we needed to do was work with Commerzbank to prepare an information pack. This took the form of a term sheet and a PowerPoint presentation. As a starting point, we used existing investor relations material, which was adapted for debt investors to include specific information about our business model.

The key Schuldschein document was only around 30 pages. To put this into perspective, our bank facility document is more than 140 pages.

◆ *Penelope Smith:* Issuing a Schuldschein is a very straightforward process. The documentation was in English (given the expected international investor base), albeit subject to German law. International investors are now used to the standard Schuldschein document and fully understand the structure and how it all works. Regus itself used external counsel – just as it would on an English law transaction. We also produced in-house credit research on Regus for investors to help them understand the Regus story, and arranged a roadshow in our London offices, with a good number

of investors attending in person or via dial-in arrangements. Sometimes we just hold an investor call, but, in the case of Regus, we thought it would help investors to familiarise themselves with the company and its business model if we had a physical meeting as well – and this proved to be the case.

In general, there was very little difference in how we structured and marketed the Regus Schuldschein compared with one of our more traditional German transactions (although the investor base was far more international than we would see on a German deal). Following the roadshow, our sales team followed up with all investors to ensure that any further questions were answered, and a few weeks later the orders started to come in. This enabled us to build a strong book across the maturity range.

#### What was the Schuldschein experience like?

◆ *Paul Wilkinson:* We were very happy with it. The Schuldschein was sold on a book-build basis over a couple of weeks. The term sheet gave investors the opportunity to choose between fixed and floating rate, and three or five years. We set a conservative target for the amount we wanted to raise, since it was our first offering, but, in the end, we were significantly oversubscribed.

The lack of complexity and concise documentation allowed the process to run smoothly.

As we have established the framework now, it would be simple for us to issue more Schuldschein debt, so it is likely that we will consider this market again.

◆ *Penelope Smith:* Our feedback from clients has been that raising funds via Schuldschein is a good experience and meets their funding requirements with ease. It can compete with, but also be compatible with, other forms of more public issuance, such as eurobonds or syndicated loans given the investor base. Other, more established private placement markets, such as the US private placement market, offer different characteristics that have traditionally been attractive to UK companies, but the Schuldschein market is beginning to offer a credible European alternative.

As a financing instrument, Schuldschein offers flexibility within a simple structure away from the public eye, which can prove to be attractive for issuers and investors alike. At this time, the Schuldschein can be said to be the only pan-European alternative financing instrument for non-rated issuers and one that is becoming increasingly international, both from an investor and from an issuer perspective. ♡



**Paul Wilkinson (pictured left) is head of corporate finance and treasury at Regus; and Penelope Smith (pictured right) is a director in international loan origination at Commerzbank. For more information, email: [SSD-DCML@commerzbank.com](mailto:SSD-DCML@commerzbank.com)**

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