Anatomy of a bond issue

THE ACT'S RECENT BREAKFAST SYMPOSIUM ON ACCESSING THE PUBLIC US DOLLAR DEBT MARKET WAS EQUALLY INTERESTING IN OFFERING DETAILS OF A FTSE 100 COMPANY'S APPROACH TO TOUGHER MARKETS, WRITES **GRAHAM BUCK**.

Despite a year that has been more volatile for financial markets than any other in recent times, pharmaceuticals giant GlaxoSmithKline has successfully wooed the investment community on several occasions.

How has GSK managed it? Sarah-Jane Chilver-Stainer, its VP and group treasurer, provided a detailed analysis of the group's attitude and approach last month at a Citi-sponsored ACT breakfast symposium on accessing the public US dollar debt market.

She began her account in July 2007, when evidence of an impending credit crunch was mounting but had yet to fully impact on financial markets. With investor confidence flagging, GSK announced that it would accelerate its share buyback programme to £12bn spread over two years, or more than double the previous level. Since then, despite the turbulence in the financial markets, the company has managed three successful debt issues in euros, sterling and dollars respectively to support its policy: €3.5bn last December, £700m in March this year and $9.5bn in May.

"There have been some horrendous graphs produced that show what has happened to spreads since the onset of the credit crunch," said Chilver-Stainer. "Ours isn't too bad by comparison."

But before summer 2007 GSK's debt profile comprised 108% fixed rate debt, with an average cost of net debt at 4.45%. The group was also an infrequent issuer, generating significant amounts of cash each year that was utilised for buybacks. Accelerating the buyback programme has meant an increase in the group's net debt. It stood at around £8.5bn in June 2008, a significantly higher figure than the average at any time over the period 2000 to 2006.

GOING FOR IT Chilver-Stainer admitted that GSK had been fortunate in its debt issuance over the past year, seizing the chance whenever a window of opportunity presented itself in the market.

The group's Eurobond issuance last December took place at a time when market conditions looked particularly grim and banks were advising against proceeding with the issue. However, GSK adopted a "fairly aggressive" stance, and when the second week of that month briefly offered improved conditions, it immediately moved in.

The sterling bond issuance in March also took place against the background of a difficult market and difficult pricing. Chilver-Stainer explained that at that point it was unclear when the subsequent dollar transaction would actually take place and meanwhile GSK was carrying out share buybacks on a regular weekly basis.

The group succeeded in issuing a 31-year bond due March 2039, before proceeding with the larger dollar issue that followed in May. That issue was preceded by a four-month preparation period: work on the documentation commenced in January, the investor presentation was prepared together with questions and answers relating to the issue. Early in March the Well-Known Season Issuer (WKSI) shelf registration was filed and in April the group issued an updated presentation for its first-quarter 2008 results (the WKSI rules having been introduced by the SEC in 2005 to make ongoing issuance easier).

Despite the credit crunch, GSK has successfully issued three bonds

On Sunday 4 May, GSK decided the go/no-go call on the issue and at 9.00am GMT the next morning the chief executive and team met in London. For the remainder of that Monday, the timetable read as follows:

- 12.00 GMT: final bank due diligence and final go/no-go call conducted;
- 12.45 GMT: announcement made of the offering;
- 13.00 GMT: online NetRoadshow got under way;
- 14.30 GMT: investor conference call and bookbuilding commenced;
- 16.00 GMT: first pricing update;
- 18.00 GMT: margins and tranches agreed;
- 22.00 GMT: pricing call; and
- 23.00 GMT: term sheet agreed.

GSK's pre-planning proved itself on the day. Chilver-Stainer said it was "quite extraordinary" how quickly investors came on board and the order book size swelled to $18bn. This posed the question of whether to add on a short-term note and upsize the deal and it was agreed that a two-year floating-rate note would be tacked on.

"It was a great maturity ladder and GSK was very happy with it coming at the end of such a momentous year," she said. "Despite the increased cost of new debt, the average cost overall was still very acceptable."

TIME WELL SPENT The outcome proved that no time spent in preparing for a bond issue is ever wasted, said Chilver-Stainer, who suggested that treasurers should approach the ratings agencies well ahead of any proposed buyback, even though doing so resulted in a downgrade for her group.

She added that GSK also follows a basic dos and don't's approach to debt investor relations.

The don't's include ruling out all investor roadshows and investor one-to-ones, on the basis that GSK makes all of the relevant information publicly accessible. Investors are instead offered a detailed presentation via conference calls, coupled with a pre-recorded Net Roadshow online presentation that is mounted on the day the issue actually takes place.

In addition to these tips, treasurers were offered the following action plan for successfully accessing the market in difficult times:

- Have a relatively loose plan ready, so that it can be adapted to meet the prevailing market conditions;
- Once you've made up your mind to approach the market, don't hang back or delay, but follow through;
- Communicate your plan effectively to both the board and the chief financial officer;
- Start your preparations early in order to retain maximum flexibility;
- Allow plenty of time for drawing up the documentation;
- Ensure there is detailed preparation for the due diligence process;
- Remember that while you may incur heavy upfront costs, they pave the way to the deepest and fastest market; and
- Ensure that you communicate effectively with the key stakeholders within the group: the CFO, corporate treasury, investor relations, corporate secretariat, corporate accounts and legal operations.

Corporates may also need to incorporate into their plan an assumption that the credit crunch will continue into next year and very possibly 2010, warned Melanie Czarra, managing director and head of cross-border capital markets at Citi.

She said that issuers coming to the market with relatively small transactions could still anticipate relatively strong demand, although larger transactions have become more difficult as investors have become more selective.

"Some companies may bring their funding plans for 2009 forward into 2008," she warned. "That's going to mean a lot of additional final demand at a time when the banks aren't looking to lend."

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In the dollar market the new issue concessions for cash have widened as investors are demanding more before they commit to any deals. At the same time the two biggest buyers of US treasuries until now, Fannie Mae and Freddie Mac, are unlikely to be buying in future following their takeover by the US government.

Yet Czarra also believes that the current market conditions can still produce "great things" if issuers are ready to take advantage of the intermittent windows of opportunity.

"If markets are moving and spreads are widening, get a cushion built into the approvals you secure from management," she said, adding that flexibility was vital. "Have lots of windows for when you can issue as there will continue to be plenty of no-go days."

She added that the big unanswered question is where investors will place their cash when the impact of the credit crunch eventually begins to ease.

"We may have wide spreads now, but when financial stock eventually hit rock-bottom and investors start to pile in they could get even wider," she said. "And corporates will then have to try that much harder."

Finally, there was general agreement among speakers at the symposium that the Eurodollar market tends to be more selective than the dollar market on the type of issue it will buy into. It benefits familiar names such as Nestlé but disadvantages a lot of others.

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