

NEW ZEALAND DEBT CAPITAL MARKETS GUIDELINES

2022



DEFINITIONS

In this paper:

Wholesale transactions are defined as offers to, or other transactions with, persons each of whom is a “wholesale investor” within the meaning of clauses 3(2)(a), (c) or (d) or 3(3)(b) of Schedule 1 to the Financial Markets Conduct Act 2013 (**FMCA**).¹

Retail transactions are defined as all transactions which are not Wholesale transactions.

Any organisation arranging the debt capital markets issue is referred to as **DCM originators** or a Joint Lead Manager (**JLM**), acknowledging that there are instances (such as private placements) in which only a single dealer/manager will be appointed. Where there are multiple JLMs, they are appointed by the DCM issuers to jointly and cooperatively work together to achieve the DCM issuer’s objective.

¹ Because of the focus of these guidelines, this definition derives from the customary ‘institutional investor’ categories of persons which are investment businesses, ‘large’, or government agencies, and/or a minimum subscription of \$750,000 applies. Other Schedule 1 exceptions may be used in particular instances.

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1.0

INTRODUCTION AND PURPOSE



The New Zealand Financial Markets Association (**NZFMA**) promotes and supports the efficient operation of New Zealand's over-the-counter wholesale financial markets. As part of our role, the NZFMA is committed to supporting New Zealand's Debt Capital Markets (**DCM**) participants to enhance the quality and reputation of New Zealand's Debt Capital Markets. Accordingly, we have facilitated the development of these DCM Guidelines which aim to outline best practice in the operation of New Zealand's Debt Capital Markets.

The DCM Guidelines are intended to provide **DCM participants**, including originators, issuers, investors and intermediaries, with guidance on market best practice in primary market issuance of DCM instruments to retail and institutional investors. They are designed to prompt DCM participants to consider the best interests of the wider market when undertaking market activities or making decisions.

These guidelines have been compiled by the Debt Capital Markets Working Group (**Working Group**) of the NZFMA. The purpose of the Working Group is to develop best practice guidance to support improvement in the operation of New Zealand's Debt Capital Markets. The Working Group comprises representatives from NZFMA member banks, NZX participant firms, investors, DCM issuers, NZX and a law firm. It was formed to review existing market conventions, protocols, rules and policies relating to primary issuance and secondary market trading of DCM products in New Zealand, and to make recommendations of any changes required to

achieve market best practice. The Working Group also reviews and makes recommendations on operational aspects of DCM, for example: settlement protocols.

These guidelines are not intended to be a wide-ranging primer on all aspects of debt market issuance. Instead, these guidelines take a high-level approach to issues on which the Working Group viewed it would be useful to provide guidance. In most instances many of the processes outlined are already standard market practice.

These guidelines are not binding and market participants remain free to adopt alternative practices to achieve the best result on any given transaction, subject to applicable law. Where legal requirements are described below this is expressly noted. These guidelines are not legal advice. DCM participants should seek their own advice where applicable.

2.0

DCM PARTICIPANTS TO CONSIDER THE BEST INTERESTS OF THE MARKET



DCM participants should consider the best interests of the wider market when undertaking market activities or making decisions. All DCM participants have an interest in promoting the integrity and functioning of the market and achieving the most fair and efficient execution of deals. This relates to all market participants and these guidelines can assist with the fulfilment of this objective for the collective benefit of both the market and its participants and stakeholders. While DCM issuers ultimately have discretion as to their approach to market, decision making relating to both pre-transaction

and transaction activities should consider fairness to DCM issuers, intermediaries and target investors alike. These guidelines are not intended to reflect or create any fiduciary or other duty.

DCM participants should also take into account the potential for the debt capital markets to contribute to market and product developments that foster positive environmental, social and governance (ESG) outcomes.



3.0

PRE-TRANSACTION ACTIVITY



Prior to a transaction occurring, it is important that confidentiality of information is maintained. Where there is pre-transaction activity (such as: relevant discussions and other communications with potential investors before launch of a transaction), the following should be considered.

3.1

PRE-ANNOUNCEMENT MARKET SOUNDINGS

JLMs may decide that it is reasonably necessary to use market soundings to help determine the appropriate structural features, term, volume, and pricing of the proposed transaction. **Market soundings** are discussions with potential investors and sales or trading staff prior to the announcement of a possible DCM transaction. While final terms of a transaction are set by the market, in the first instance, market soundings can assist JLMs and DCM issuers to understand market conditions and likely demand.

There are several considerations in the decision-making process regarding market soundings:

- Agreement by the DCM issuer to the market soundings and which organisations are being sounded out for feedback, the timing and content of market soundings and the purpose of the market soundings.
- Is the market sounding likely to disclose any inside information or other confidential information? ²
- Disclosure of confidential information should be restricted as far as practicable, and is generally expected to be limited to the DCM issuer's name/sector and general proposed offer terms.
- Disclosure of inside information in relation to listed DCM issuers is generally restricted under the FMCA and NZX Listing Rules. It should only be considered where suitable arrangements are in place to maintain confidentiality, and otherwise in accordance with the JLM's policies and procedures, NZX Listing Rules and other relevant regulatory requirements.
- Detailed records should be kept which outline:
 - the reason for undertaking the market sounding
 - the organisations and individuals involved in the process and;
 - the information provided and responses received.

² The terms "confidential information" and "inside information" are discussed further below.

Market soundings should be limited to as few parties as reasonably necessary and be undertaken as close as practicably possible to the proposed date of issue of the DCM instrument. JLMs and DCM issuers should keep in mind the obligations imposed on investors throughout the issuance process and consider how to limit and manage compliance obligations placed on investors regarding issues of confidentiality and insider trading.

When an organisation is approached to be part of market soundings, that organisation needs to be approached initially on a no-names basis to gauge their willingness to be sounded and to receive information that may be confidential and, possibly, inside information.

Any organisation who agrees to be part of market soundings and is provided with inside information, is described as having been 'wall crossed'.

Investors may have different approaches and policies in relation to market soundings. Their activities, once they have been approached regarding inside information, and any known investor preferences, should be a consideration by JLMs before they are approached.

For example, some investors may make it known to JLMs that they do not want to be wall crossed.

Any organisation involved in market soundings should be aware of all the laws and regulations applicable to inside information and agree to comply with relevant confidentiality requirements as referred to above. These confirmations should be recorded or documented.

All parties should be informed immediately when the DCM transaction and any relevant inside information has been disclosed to the market. This also applies if a decision is made by the DCM issuer not to proceed with the transaction.

DCM originators also undertake market soundings with other internal parts of their organisation and must ensure that robust policies and procedures are in place and followed, including for wall crossing where relevant.

Any proposed market sounding should not proceed if the organisation does not agree to be involved. In particular, inside information must not be disclosed to an organisation unless they have agreed to be wall crossed and met the above requirements.

3.2 INSIDE INFORMATION, CONFIDENTIAL INFORMATION AND COMPETITIVELY SENSITIVE INFORMATION

It is important to understand the difference between inside information and confidential information:

- **Inside information** is triggered by statutory definitions (in particular s 234 of the FMCA), and gives rise to specific statutory obligations, as it relates to information that a reasonable person would expect to have a material effect on the price of quoted financial products if it were generally available to the market (i.e., the information is "price sensitive").

- By contrast, **confidential information** has its ordinary meaning and may trigger conduct, common law, and professional obligations.

Confidential information may or may not be price sensitive to any quoted financial products (i.e., it may or may not be inside information). However, all inside information will generally be confidential information. If any inside information ceases to be confidential, the NZX Listing Rules require the DCM issuer to make that information generally available to the market. Advice

on this distinction should underlie the compliance procedures of DCM originators.

Confidential information may also be **competitively sensitive information**, which is the type of information that a company would not want to share with its competitors. It includes confidential information that a company considers crucial to competing in

its relevant markets. In accordance with relevant competition laws, DCM participants that compete with one another (for example: two JLMs or two DCM issuers) must not (either directly or indirectly through a third party) exchange competitively sensitive information.

3.3

MARKET SOUNDINGS COMPARED TO GENERAL DISCUSSIONS

JLMs and their related investor sales desks are likely to have general discussions with potential investors in the normal course of business. These discussions could relate to general market conditions and developments or could be regarding individual DCM issuers or securities.

They may include routine discussions to gauge the level of interest in securities of a DCM issuer in the absence of any knowledge of a potential DCM transaction.

Such general discussions are not market soundings.

3.4

MARKET SOUNDINGS COMPARED TO INVESTOR MEETINGS

DCM issuers (or potential DCM issuers) often undertake regular (or sometimes ad hoc) meetings with existing or potential investors. Information provided at these meetings must be information which does not amount to inside information. No details of any actual or proposed DCM transaction that amounts to inside information should be included in the meeting materials or discussions before those details have been announced to the market generally.

DCM issuers should be aware that in some circumstances the scheduling of investor meetings and/or marketing may have a material effect on the issue price of a DCM instrument or its other securities.

In these situations, DCM issuers should consider informing as many investors as possible of the proposed investor meetings and making available any material provided at those meetings.

There can be times where a DCM issuer will engage directly with investors without the assistance of a JLM regarding a general market update or a potential transaction. It is acknowledged that the DCM issuer (rather than any JLM) is responsible for any such meeting and the DCM issuer should follow the practices described above.

3.5

REVERSE ENQUIRY

A reverse enquiry is when an investor or DCM originator approaches a DCM issuer directly or through a DCM syndicate to propose issuing securities directly to them, rather than the DCM issuer undertaking an offer to a wider range of investors.

Care needs to be taken by the DCM participant to ensure that any information provided to the investor is consistent with information given to other investors by the DCM issuer or disclosed to the market generally, in accordance with 'fair dealing' and other relevant laws.

3.6

MANAGING CONFLICTS OF INTEREST

A conflict of interest is defined by the Financial Markets Authority as follows: "A **conflict of interest** can occur when an adviser's interests are different from yours."

Managing conflicts of interest is very similar to managing inside and confidential information.

DCM participants should be aware of the need for good policies and procedures to handle conflicts of interest and are expected to have and to follow robust internal practices.



4.0

TRANSACTION ACTIVITY



4.1

INFORMATION FLOW THROUGHOUT THE TRANSACTION

DCM transactions can be structured in wholesale or retail format and can be undertaken via tender, syndication, or private placement. Regardless of the structure or issuance mechanism the following should be considered when distributing information.

When market announcements occur, they need to be objective, factual, not misleading, and timely.

Any applicable announcement process must be transparent with any information released in a manner to be available to as many DCM participants as possible at the same time. Information should be disseminated through a channel which can be readily accessed by DCM participants interested in the transaction. Announcements must also comply with applicable FMCA and NZX Listing Rule requirements.

These announcements can cover:

- Information relating to deal and non-deal roadshows
- Copies of investor presentations
- Awarding of transaction mandates
- Issuance intentions including tenor, volume and initial price guidance
- Opening and closing notices for a transaction

- Updates throughout the transaction including volume and pricing updates
- Final terms of the transaction
- Transaction statistics

Where information is sourced from supporting documentation, announcements should reference the source document. Information that is summarised by JLMs should be clearly acknowledged as such.

Any errors or omissions that are subsequently discovered should be corrected and published immediately.

Announcements should be customised according to the specifics of a transaction or process. There are differences between the type and style of information required for transactions targeted to retail investors compared to transactions targeted to wholesale investors e.g., market updates.

Decision making and approvals by the DCM issuer, such as: term sheet approvals, final terms of transaction, deal pricing, issue size or advising allocations, are often time critical. The DCM issuer's internal approval process should be understood by all parties and within the constraints of the DCM issuer's governance processes, focussed on delivery of information to the market in a timely manner.

4.2

INVESTOR SPLIT LISTS

DCM transactions which involve the appointment of multiple JLMs, may require a split list.

A **split list** is where communication with certain investors is allocated to specific JLMs over the course of a transaction. This is typically done for the purposes of improving operational efficiency - such as ensuring efficient communication during a bookbuild. Under a split list approach, each JLM will communicate with their allocated investor throughout the transaction, rather than the investor receiving the same information from all other JLMs involved in the transaction.

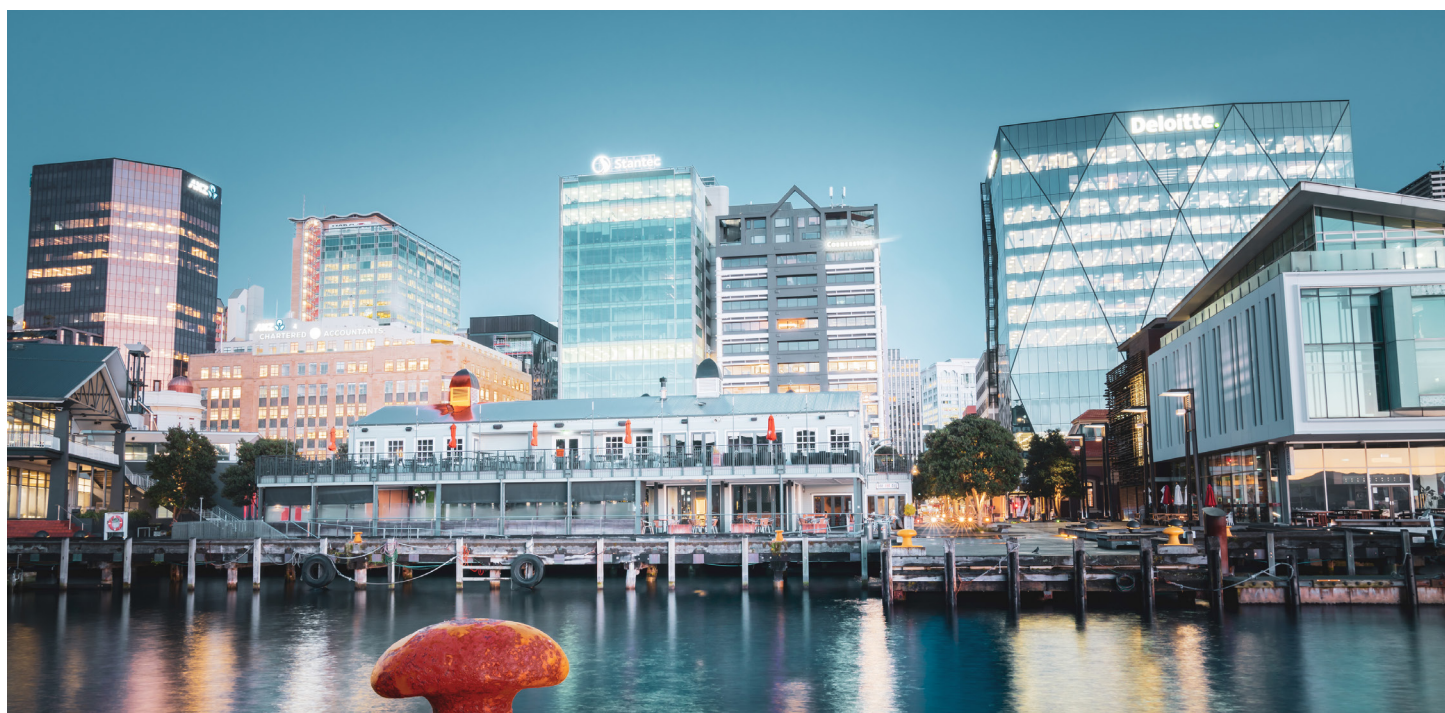
A split list can streamline the communication process, make it more efficient, and enhance DCM issuer confidence that all investors have been covered.

It is good practice for JLMs to share the proposed split list with the DCM issuer and reach agreement on it prior to the transaction launch.

Split lists may not be reasonably necessary for every DCM transaction. The following should be considered when deciding to have a split list and the allocation of investors amongst the JLMs:

- Split lists should be used for the benefit of investors and DCM issuers
- Ideally a DCM issuer should agree to the use of a split list
- Where a split list is used it must be made clear that the split list is non-exclusive meaning that:
 - A split list is not binding on an investor and the investor is free to engage with other JLMs if they wish; and
 - JLMs are free to assist investors that are not allocated to them on the split list.
- The split list only applies to the specific transaction being considered.

A split list does not cover any corresponding switches of other existing DCM instruments or any hedging activity by the investor to facilitate participation in the DCM transaction.



4.3

ORDERS

Communication of interest

Interested investors can place an order in a DCM transaction through any of the JLMs on a conditional or at market / clearing basis. A DCM issuer is not obliged to accept a conditional order. If the DCM issuer does not intend to accept conditional orders, that should be clearly communicated to the market.

Investors may choose to place their order with all JLMs (known as a 'pot' order) or a subset of those participants (a sole or discrete order).

Order inflation

Investors should, and generally do, make their investment decisions based on the fundamental merits of the DCM transaction (such as the proposed terms, the creditworthiness of the DCM issuer, and the investor's portfolio needs) rather than based on the anticipated demand for the transaction.

Orders made in contemplation of potential scaling should be discouraged by clear and consistent communication by the JLMs to investors participating in the transaction.

If the DCM issuer or a JLM has a reasonable belief or an indication that the investor's demand level differs from the true extent of its interest, or observes behaviours which are not consistent with the objectives and expectations of the DCM issuer, it is reasonable to take this into consideration during the allocation process.

Non-investor orders

It is accepted as best practice for the disclosure to the market of bids by the trading desks of the JLMs to ensure investors and DCM issuers are aware of this source of non-investor demand in a transaction. To meet this need, any bookbuild updates of volumes announced to the market during the offer period should include the text "excluding/including JLM trading interest" to make clear the volume (if any) of interest from JLM trading desks in the transaction. Information disclosed relating to the bids by the trading desks of JLMs should be limited to the minimum amount of information that is reasonably necessary to ensure investors and DCM issuers are properly informed.



4.4

PRICE GUIDANCE

Generally, JLMs will open the bookbuild of a DCM transaction by announcing deal terms, this includes the initial price guidance. The initial price guidance is an indication by the DCM issuer and JLMs of where the transaction could be priced but (unless otherwise stated) is non-binding and subject to change. The issue price will ultimately be the product of market and competitive conditions, including DCM Investor appetite.

Even with prior feedback from a pre-sounding process, it may be appropriate for the guidance to be amended to reflect market conditions and the demand response. One or more iterative price revisions of indicative pricing guidance may be appropriate to reflect the pricing point at which the market is anticipated to clear, including by reference to the DCM issuer's desired position as to quantum, tenor and other terms. For further information see the section on "Transaction Pricing" below.

4.5

INTRA-TRANSACTION UPDATES

JLMs should collectively agree, in relation to the circumstances of the particular transaction, what degree of disclosure is appropriate to be made before publicly disseminating intra-transaction updates. This is to ensure any disclosure is clear, fair, and representative of the demand received at the time, in addition to the normal requirement to comply with Part 2 of the FMCA and other applicable laws. This may result in no information relating to the order book being disclosed before the order book closes.

Intra-transaction updates need to be timely, however this may differ between wholesale and retail transactions. The use of intra-transaction updates will vary amongst retail transactions but if the DCM issuer and JLMs determine that it is beneficial to update the market, then it is important for the update to be timely and comply with the FMCA and any NZX Listing Rule requirements.



4.6

ALLOCATIONS

Once an order book is closed, the order book should be allocated in a timely manner. In the allocation process the DCM issuer finalises the overall volume of securities to be issued (where applicable), to which investors the securities are issued and in what amounts.

The allocation process may differ between DCM issuers and between types of DCM transactions but in all situations, allocations should be at the discretion of the DCM issuer. JLMs can provide advice and recommendations, but the DCM issuer should always make the final decision.

It is important to avoid or manage potential conflicts of interest throughout the allocation process. Ideally a DCM issuer should:

- have a set of procedures established in advance of the transaction that sets out their process for managing allocations to ensure a fair and equitable outcome for investors who have supported the DCM transaction
- maintain records of the allocation recommendations and decisions.

There are several factors that can influence the final allocation with the preferences and objectives of the DCM issuer being the primary considerations. Other potential factors which may be taken into consideration when allocating an order book include:

- Applicable target market for the securities
- Total oversubscription of the order book versus the size of the deal to be allocated
- Selling restrictions in the jurisdiction(s) applicable to the investor

- Avoidance of allocations in inconvenient or uneconomic amounts
- Investor characteristics:
 - Specific investor preference of the DCM issuer
- Investor type:
 - Geographical preference of the DCM issuer
 - Mix of investors to aid secondary market liquidity
- Investor behaviour:
 - Pro-active expressions of interest in terms of price or quantity in the marketing and pre-marketing process i.e., price and volume leadership
 - Size of investor interest (may be absolute and/or relative to the investor's portfolio or assets under management)
 - Participation in liability management exercise
 - Track record in investing in the DCM issuer's past debt securities
 - Track record in investing in sector/issue type
 - Timing of the investor's interest in the deal process
 - Price or spread limits given by the investor
 - Length of the investor's expected holding period for the securities
 - Geographical location of the investor
 - Level and timing of engagement in transaction process

4.7

TRANSACTION PRICING

Clean and efficient execution of the pricing/rate setting of a new DCM transaction is recognised by all DCM participants as important for the success of transactions, and participants' ongoing confidence in the market.

Key elements to achieve best practice in the pricing/rate setting process:

- Identification of the most suitable pricing mechanism during the deal design and structuring process for the type of transaction, including whether pricing should be determined as a margin to a reference or benchmark rate, or set as a yield.
- Typically, in a wholesale transaction, final investor allocations are provided to investors as quickly as possible once determined, and ideally prior to the pricing of the transaction to enable investors to manage their risk as required. This should also be considered as best practice with retail transactions, in compliance with applicable laws and Listing Rules and DCM participants' compliance policies with respect to them.
- Pricing is typically conducted on a conference call between the DCM issuer and JLMs, where the market parameters are observed and recorded, and the transaction variables are agreed and calculated. Details typically covered include:
 - Transaction details;
 - Reference rates and curves, such as government bond yields, swap rates, etc;
 - Any pricing adjustments specified for the transaction are determined (e.g., forward start adjustments, quarterly adjustments to reference rates);
 - Calculation of the interest rate, yield and issue price; and
 - A record of the time of pricing.
- Once the transaction is priced, the information needs to be recorded in the formats relevant to the particular transaction (e.g., final terms sheet, pricing supplement, market announcement), and released to the market as soon as possible. DCM issuer and NZX disclosure requirements may dictate the process for release, and whether it must be via NZX in the first instance. Minimising the time these steps take is recognised as important to all market participants.

4.8

POST DEAL ANNOUNCEMENTS AND STATISTICS

It is commonly agreed that providing statistics relating to the proportion of each type of investor or trading desk involved in a DCM transaction helps build transparency in the marketplace.

While post deal statistics are preferred, they will vary from transaction to transaction and should be at the DCM issuer's discretion. If deal statistics are to be disclosed, where possible, the DCM issuer or the JLMs should seek to distribute these within 48 hours of pricing.

DCM issuers and JLMs should also consider where investors and other interested parties can access information relating to the transaction following the closure of the transaction e.g., NZFMA, NZX (for listed deals) and JLMs. This information should cover both the primary transaction and ongoing secondary market trading.

4.9

HEDGING OF RISK FROM TRANSACTIONS

Hedging can be an important part of a DCM transaction. An investor could invest in the newly issued DCM instrument on an outright basis or could sell an existing DCM instrument in their portfolio to finance the purchase, rebalancing duration, or managing total limits. Investors may also want to hedge any interest rate exposure that could arise, through an interest rate swap transaction. The DCM issuer may also want to hedge any interest rate exposure of the transaction through an interest rate swap.

At all times, hedging may be undertaken with organisations other than the JLMs.

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