Hedging your debts

Building organisational resilience with debt management

New Zealand Debt Management Survey

September 2017

pwc

Contents

Welcome to our 2017 PwC New Zealand debt management survey

In a turbulent world, having access to funding that is accessible, flexible and well-priced has never been more important. What we've seen in this year's PwC Debt Survey is that those organisations that are proactively and strategically managing their debt aren't just financially better off, they're building resilience that can support their entire organisation.

The survey, which was completed in June, is the fourth treasury survey compiled by PwC and our third survey that is debt specific. Our purpose is to examine how domestic organisations make decisions about their debt and liquidity management. We hope the survey helps to shed some light on the level of importance organisations place on debt management; a discipline that is vitally important, yet is often neglected until new/additional funding is required or a refinancing issue suddenly emerges.

We believe the survey results provide valuable insights into what organisations are doing to manage their funding risk, and provides new ideas for entities that are looking to manage their debt. It's my hope that readers will find some gems that add value to their business.

The survey covered New Zealand based organisations of varying sizes, from borrowers with less than $10 million of debt and turnover (revenue) less than $25 million, to organisations with debt levels greater than $500 million and turnover in excess of $1 billion. In addition, with this being our third survey to consider debt funding in some capacity, we can now uncover trends over time. However, such analysis must be interpreted cautiously given the different composition of respondent populations across the three surveys. (For example, this survey contains a significantly higher percentage of smaller private companies than previous surveys.)

This year's results indicate there are a number of funding challenges for borrowers, particularly in the bank lending market. This has been driven by increased banking regulation which has had a significant impact on bank cost of funds. With credit margins on bonds at pre-Global Financial Crisis levels, this has created an interesting divergence between bank funding and debt capital markets.

From a macroeconomic perspective, global conditions have strengthened since our last treasury survey in 2015, supported by accommodative monetary policies and less contractionary fiscal policies. However, core inflation remains stubbornly weak in most major economies. Central banks have now kept monetary policy settings loose for a considerable period of time, resulting in over-inflated asset prices. We've also seen populist movements causing considerable disruption in the global financial markets. Firstly, the UK's decision to leave the European Union, followed by the election of Donald Trump. Looking ahead, escalating geopolitical tensions and increased global trade protectionism could derail the ongoing recovery in the global economy.

Against this backdrop, it's important to have appropriate funding and liquidity policies in place to help mitigate against any effects these risks could have on global and domestic debt markets.

We've broken down our survey results into five key sections:

- General funding issues
- Bank funding
- Debt capital markets
- Treasury policies relating to funding and liquidity risk
- Net working capital

Where relevant, the presentation of the results has been separated by survey participant type, size and various other comparable breakdowns. We have also tried wherever possible to provide the reader with the ability to benchmark against peers.

Lastly, thank you to all those respondents who kindly gave up their valuable time to participate in the survey. It was your openness and willingness to share your information and thoughts with us that has made this publication possible.

Stuart Henderson
Partner

Key findings

The following were the key findings in relation to the debt raising activities of organisations with approximately $10 million to $500 million plus of outstanding debt.

1. All domestic organisations have ***a strong reliance on bank debt for funding***. In terms of composition, smaller borrowers were 91% reliant on bank funding, medium sized borrowers were 73% reliant on banks and larger borrowers on average received 53% of their funding from banks.

2. Borrowers with access to the debt capital markets were ***better placed to lengthen their debt profile***. The increased pricing for bank lending greater than three years is causing borrowers to shorten the tenors of bank facility arrangements. By contrast, pricing for debt capital markets transactions remains low as investors hunt for diversification and yield.

3. ***A credit rating***, and the access it can provide to a broader range of funding markets, ***appears to have a significant impact on a borrower's confidence*** in their ability to refinance their debt funding. It is likely that the greater array of funding options available to rated borrowers greatly reduces concern relating to impact of a specific credit event.

4. ***Bank debt pricing remains the most important banking attribute for borrowers*** with 86% of respondents ranking it as one of their top five most important considerations. Relationships with banks were also highly regarded, indicating that bank selections are unlikely to be based solely on pricing.

5. Bank lenders continue to have a ***strong grasp of their clients' needs*** with 89% of respondents noting their contact with their banks was 'about right'. Only 10% of respondents felt they did not have enough contact with their bank lenders.

6. For ***debt capital market activity***, the selection of lead arrangers is ***heavily weighted to issuance pricing*** that is supported by relationship, evidence of track record and of distribution. Respondents clearly want to believe that the arrangers can deliver.

7. ***Smaller borrowers do not appear to place high importance on liquidity headroom***, with only 26% having a formalised liquidity headroom policy. However, they may be more susceptible to liquidity constraints from a downturn in revenue rendering a liquidity headroom requirement an essential aspect of any robust treasury policy.

8. Only 44% of borrowers have a policy in place that ***requires the spreading of debt maturities***. However, there is a strong link between the debt maturity requirement and debt size with 78% of participants with debt over $100 million reporting a formal debt maturity spreading policy.

9. ***Net working capital fluctuations were not cited as a significant risk*** for most survey participants with 58% of borrowers signalling that working capital was positive in each quarter of the year. Furthermore, only 18% of companies experienced difficulty in forecasting their net working capital balances.

Breakdown of respondents

Entity size

To enable us to provide further analysis in terms of size, selected results have been divided into small, medium and large organisations. Two distinct size measurements, namely annual sales revenue and average total debt over the last 12 months, have been used where appropriate.

Organisations are split into size categories as follows:

Turnover size	
Small	Turnover <= $100 million
Medium	$100 million < Turnover <= $500 million
Large	Turnover > $500 million

What is your current annual revenue?

	%	2015 Survey %
Small	60	63
Medium	29	25
Large	11	12

We have also classified respondents based on their average total debt level over the last 12 months as follows:

Debt size	
Low	Debt <= $50 million
Medium	$50 million < Debt <= $250 million
Large	Debt > $250 million

Over the last 12 months what was your average total debt level?

	%	2015 Survey %
Small	61	69
Medium	27	19
Large	12	12

Further information relating to the composition of our respondent base is provided at the back of this report.

General funding issues

1 Introduction

This section explores the following general debt funding topics:

- *Credit ratings*
- *Debt funding composition*
- *The change in the average tenor of debt funding over the past two years*
- *Securing debt funding*

Some of our key findings in relation to this section are highlighted below:

65% of borrowers with a credit rating have confidence in their ability to refinance, yet only 24% of unrated borrowers had this same confidence.

Bank debt facilities were the most commonly utilised funding instrument by participants, on average comprising over 50% of each borrower's funding mix.

78% of active large borrowers lengthened their debt profile, with a similar proportion (73%) of active medium sized borrowers reporting to have taken the same action. However, only 48% of active smaller borrowers lengthened their debt profile.

82% of those active in the debt capital markets reported that there had been no change or that it was easier to obtain debt funding compared to two years ago.

Use of a credit rating

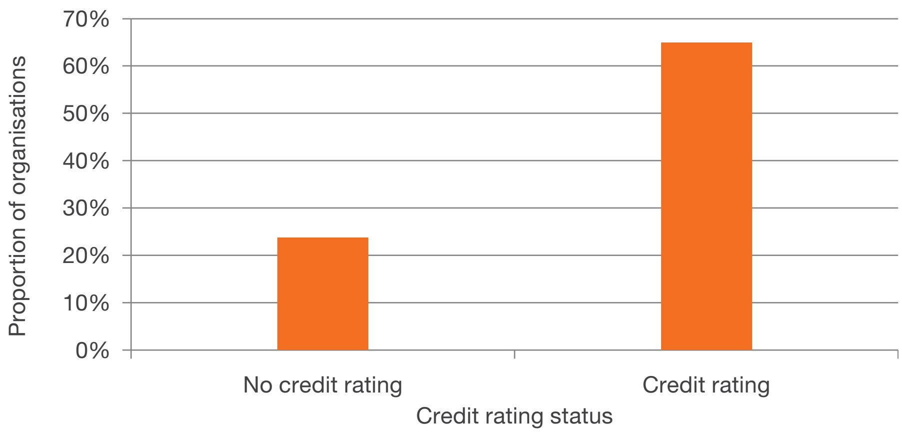
Credit ratings were the first item the survey addressed, with questions based on whether the respondent indicated they held a credit rating or not.

Only 13% of participants held a formal credit rating, which is broadly aligned with our 2013 survey findings when 20% had a rating. These consistently low proportions suggest there are a variety of characteristics an entity must exhibit before a rating becomes viable both financially and operationally.

One of the most pertinent characteristics is scale, with 59% of rated organisations falling within our larger borrower segment (those with debt levels greater than $250 million) and the remaining 41% within the medium sized borrower segment (those with debt levels between $50 million and $250 million). Scale is important as it means that the price savings procured from accessing certain funding markets would mean a rating provides a net benefit. Conversely, those with smaller debt requirements are unlikely to attract the same benefit, lacking the economies of scale to make a credit rating economically viable. For example, the pricing benefit on a five year rated debt capital markets transaction is typically between 20 to 25 basis points p.a., which would likely make a rating cost neutral for a $100 million issuance. However, on a larger issuance of $200 million, this pricing advantage would outweigh any financial costs associated with a rating.

Interestingly, our analysis found that 65% of respondent borrowers with a credit rating have confidence in their ability to refinance, yet only 24% of unrated borrowers had this same confidence. A likely reason for this is due to the wider range of funding markets, such as the commercial paper, wholesale bond markets that rated borrowers have access to. By gaining access to these funding markets, rated borrowers may be better placed to reduce refinancing risk by having access to a wider range of investors. As each investor group will have different funding constraints, borrowers are less likely to face a situation where they are unable to attract capital in any market. It also makes it less likely that a regional or sector banking credit contraction will have a significant impact on a rated organisation, which may inspire greater confidence in the ability to refinance.

Proportion of organisations with confidence in their ability to refinance



General funding issues continued

Of our rated respondents, Standard and Poors (S&P) had the greatest market coverage in New Zealand, providing a ratings opinion on 94% of respondents. Only three organisations reported using more than one rating agency. Typically, those using multiple ratings do so in order to issue in to certain international debt capital markets that require dual ratings.

For unrated respondents, the most frequent reason for remaining unrated was that the debt pricing savings procured were not viewed as sufficient enough to justify the additional rating cost and effort (50% of respondents), followed by the materiality of debt (38%). As these two answers are strongly correlated, it is unsurprising that they both scored so highly and further speaks to the role scale plays in assessing the viability of a credit rating.

However, despite such reasoning, 17% of unrated respondents noted an interest in receiving an estimate of their credit rating. Our market experience has found such 'shadow' ratings work well for organisations with debt levels between $20 million and $200 million. It allows them to better understand their credit profile without being subjected to the administrative requirements associated with establishing and maintaining a rating. As the majority of New Zealand borrowers fall within this debt range, it may be something for more borrowers to consider in the coming years.

What value does a credit rating provide?

Advantages	Disadvantages
• Greater financial transparency which may mean that organisations are able to transact with counterparties on more favourable terms. • Access to funding markets that may otherwise be closed to debt issuers such as the domestic wholesale bond market and commerical paper market. • Instill greater discipline and awareness of an organisation's risk appetite. • Better pricing and terms outcomes for debt funding and derivative transactions.	• Significant financial costs to establish and maintain a rating. • A negative outlook or ratings downgrade may affect your ability to raise capital. • Strict adherence to key credit drivers and rating agency credit assessments can lead to management and boards becoming too risk averse as they seek to maintain their credit rating. • Increased scrutiny of an organisation. • Changes to ratings assessments can lead to short term volatility (strength or weakness) in equity and bond prices. • Time costs on internal personnel given the need for semi/annual analyst updates and requirement to keep them abreast of any potentially sensitive information.

What services does a rating agency charge for?

- Issuer rating fees – Charged to cover the initial rating exercise with fees typically ranging between $100,000 and $130,000.
- Analytical surveillance fees – This is charged annually and covers costs associated with maintaining a credit rating. Fees for this service typically start at $70,000.
- Debt issue fees – These are charged for rating long-term bonds, term loans, preferred stock and private placements. Depending on the size of the issuance, fees can range between 4.5 and 6.5 basis points (bps).
- Commercial paper, certificate of deposit and medium term note programmes - Annual fee payable on the anniversary of the initial programme rating. For an initial programme, fees are typically $70,000 with additional programs attracting further fees.
- Bank loan fees – These are charged if it is determined that the credit rating was used in evaluating the loan (i.e. pricing). Fees for this service range between 2.5 and 5 bps though are not typically assessed on bank loans in the domestic market.
- Other – Bespoke assessments by a ratings agency in relation to items such as project finance, complex issuances and assessing the impact of a corporate action on a credit rating.

Debt funding composition

Respondents were asked to identify the types of debt funding they had and to provide an approximate breakdown of the mix.

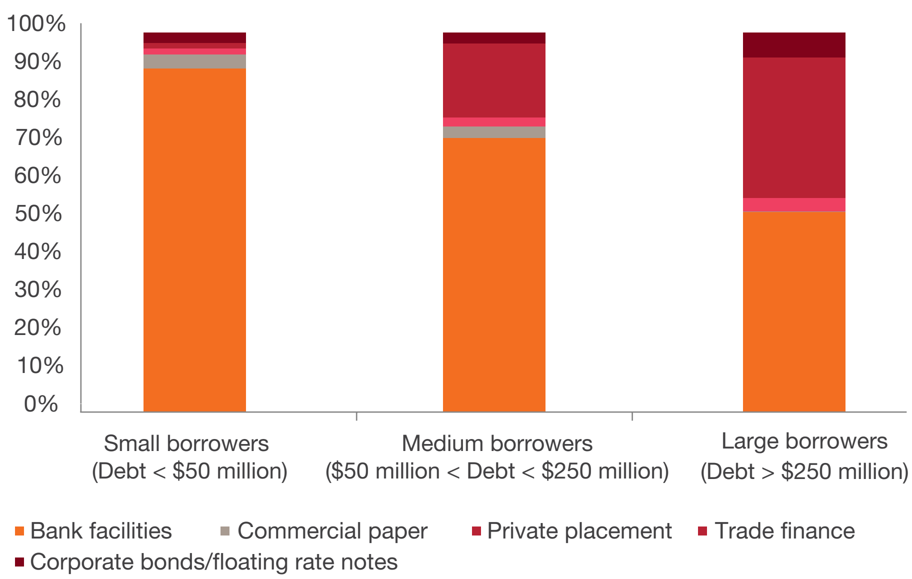
The funding types respondents were able to select from were:

- Bank facilities – core debt
- Bank facilities – working capital
- Commercial paper (CP)
- Corporate bonds/floating rate notes (FRN)
- Private placement
- Trade finance facilities
- Other bank credit facilities

Our observations in relation to this question are shown below:

- Bank debt facilities were the most commonly utilised funding instrument by participants, on average comprising over 50% of each segments funding mix. Reliance upon it does however appear to diminish as borrowing requirements increase. The greater variety of funding instruments available, as financing requirements increase, or through access to a credit rating, is a likely reason behind this.
- CP comprised on average less than 5% of all borrower segments funding mix with such a low allocation suggesting that little reliance is placed on this market. Similar findings were developed in our 2015 survey where approximately 2% of borrowers surveyed relied on the CP market for funding. As this market typically provides the most competitive short term debt pricing, the reluctance to use it may suggest some carry over from the 2008/09 Global Financial Crisis when the market was significantly disrupted, leaving borrowers unable to refinance their CP. This market is also only available to borrowers with a minimum short term credit rating of A-2 which helps explain its low usage by smaller borrowers.
- Corporate bonds become a more important funding instrument as participants funding requirements increase, on average comprising 20% of medium borrower's debt composition and 37% of larger borrowers. Likely reasons for this finding are:
  1. Size is likely to imply greater brand name recognition, making it more likely that investors are willing to purchase an issue.
  2. Such organisations may have outgrown the banking market, which increases the requirement to source funding from other markets.
  3. Larger organisations are also likely better placed to financially justify maintaining a credit rating that would encourage more issuance activity.
- Larger borrowers were also the most likely to utilise the private placement market with this funding approach comprising on average 7% of the large borrower segment total funding. Private placements are attractive for those seeking long dated funding, although a borrower must be of a sufficient scale to access the market.

Debt funding composition by borrower segment



How has the average tenor of your debt funding (from all sources) changed in the last two years?

Respondents were asked how the average tenor of debt funding had changed over the past two years. The intention of this question was to understand how borrowers are managing their debt maturity profile and refinancing risk.

The various participant interpretations to this question are described in the following table:

Debt tenor has shortened via actively shortening the duration of the debt profile	• Respondents have actively shortened the maturity of their debt profiles.
Debt tenor has shortened by the passing of time	• Respondents' debt profiles have become shorter via attrition.
No change	• Respondents have not changed their debt profile, in which case, the maturity has naturally shortened via attrition. • Respondents have increased the maturity of their debt profile in order to offset the natural attrition factor.
Debt tenor has become longer	• Respondents have increased the maturity of their debt profile in order to offset the natural attrition factor. • Respondents have increased the maturity of their debt profile.

47% of respondents have not changed their debt profile over the past two years, which is 7% lower than our 2015 survey and may indicate that borrowers have become more active in the management of their debt profile over this period.

32% highlight their tenor has become shorter either by the passing of time or through active management of the debt profile.

21% reported having lengthened their debt tenor.

Though there are noted ambiguities with how this question may have be interpreted by participants, we have defined participants that either lengthened their debt tenor or actively shortened it as being 'active' in managing their debt profile. Based on this, we have identified some interesting findings:

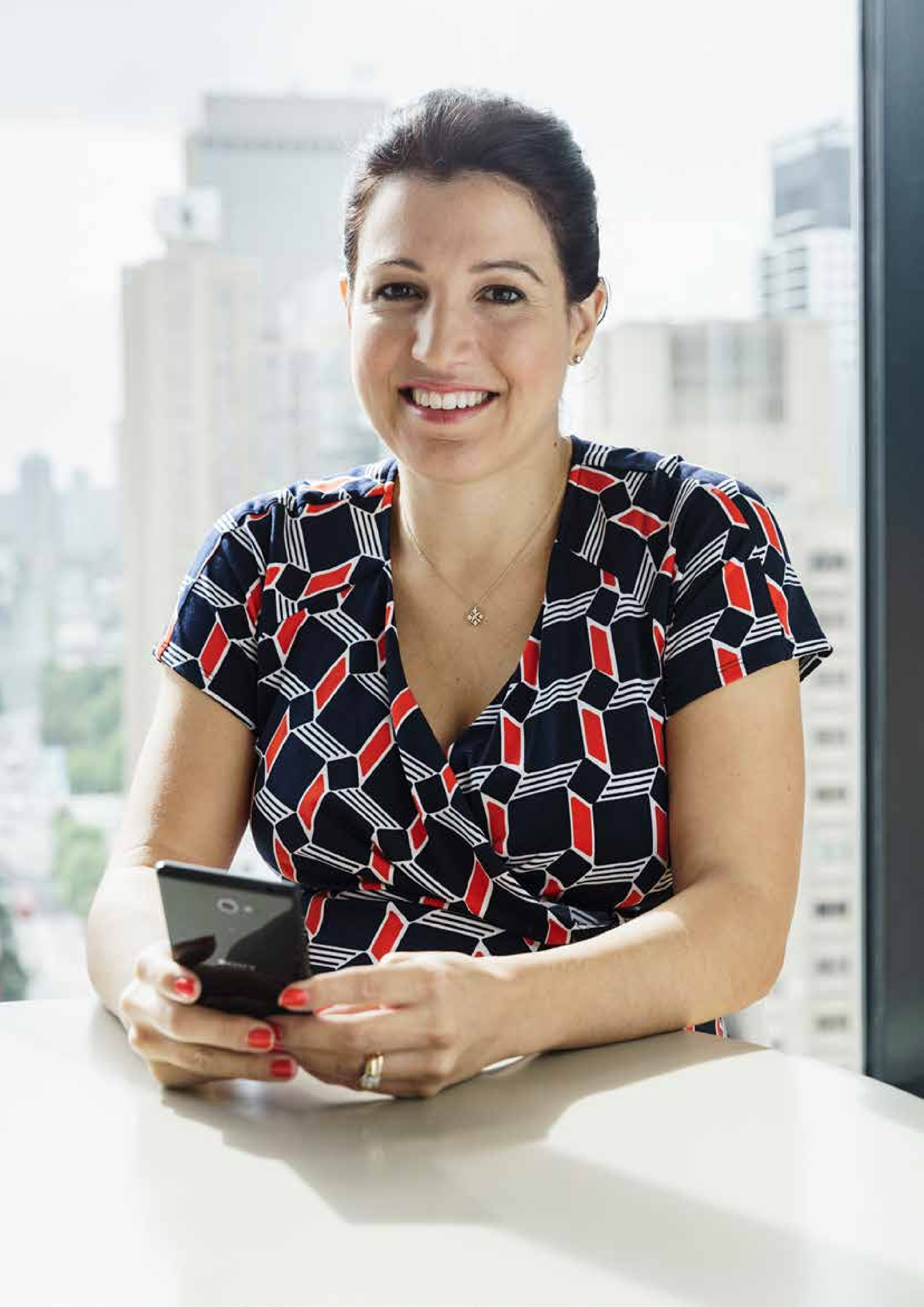
- The larger borrowers were the most active in managing their debt profile with 56% this segment having either lengthened or shortened it.
- The smaller borrower category was slightly more active (34% of sample segment) than medium sized borrowers (31%).
- Whether these active borrowers lengthened or shortened their debt profile seems to be dependent on their borrowing levels. For example, 78% of active large borrowers lengthened their debt profile with a similar proportion (73%) of active medium sized borrowers reporting having taken the same action. However, only 48% of active smaller borrowers lengthened their debt profile, with the other 52% having actively shortened their debt profile. As these smaller borrowers typically have a greater reliance on bank debt for funding, the increase in bank debt pricing (particularly for tenors greater than three years) over the past two years may have caused these borrowers to naturally shorten their funding tenors. In addition to this, larger more sophisticated borrowers are also more likely to have Board approved funding maturity policies that would require ongoing term maintenance. Such conclusions are further evidenced by our finding that 89% of those active in the debt capital markets lengthened their debt profile, yet only 53% of those inactive in the debt capital markets took the same action. As the debt capital markets continue to offer attractive and relatively low pricing for longer tenors it is likely that this has impacted on borrower funding decisions.

Securing debt funding

Respondents were asked whether it was easier, harder or if there had been no change in their ability to secure debt funding when compared to two years ago.

Given the significant increase in credit margins on bank debt lending (the primary funding source for the majority of respondents) over the past two years, we were interested in responses to this question to understand whether organisations were noticing similar funding constraints. However, it appears that most borrowers have not, with 53% reporting not having noticed any changes to debt funding conditions.

As most borrowers commonly select a debt tenor of between three and five years, it may therefore be that this



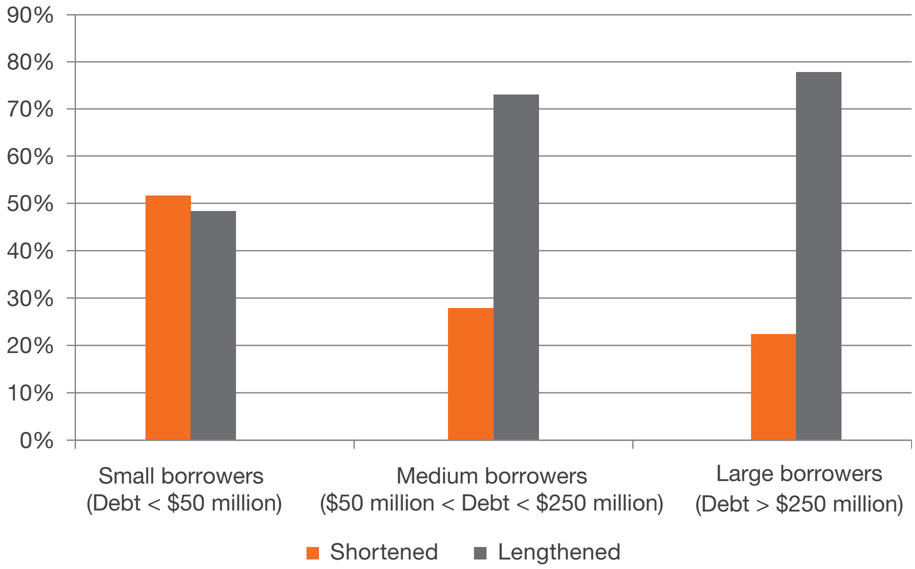
General funding issues continued

response is a function of timing with most respondents unlikely to have refinanced over the past two years. This point is substantiated by the fact that over this two year period, 64% of respondents have either made no changes to their debt profile or seen it shorten by the passing of time. They could therefore be unaware of any change in funding conditions. With credit margins on bank debt appearing to have plateaued for the moment, at elevated levels, it would be interesting to view responses in a further two years' time when more refinancing has taken place.

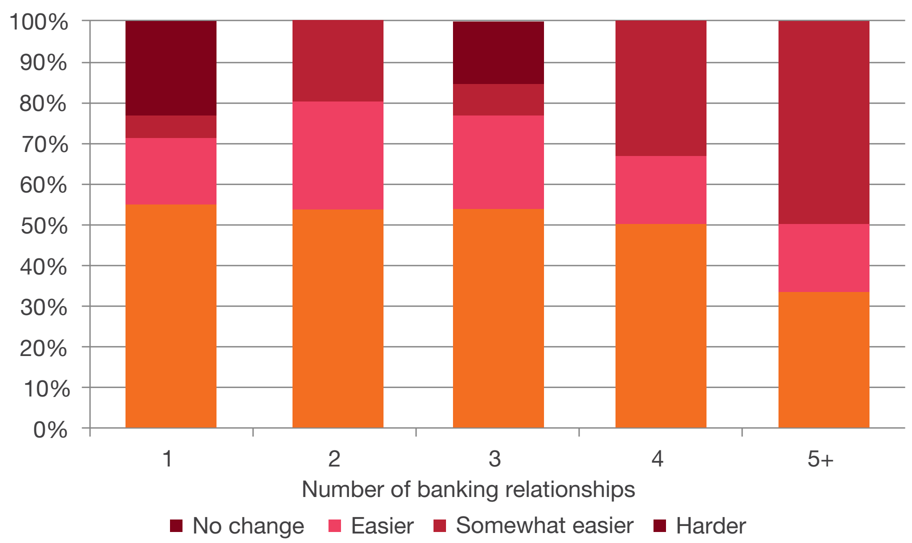
Other pertinent observations in relation to this question are displayed below:

- Larger borrowers (when measured by the number of banking relationships) have over the past two years found securing debt funding the hardest. This is surprising, given these organisations would likely be considered the most financially stable and least susceptible to increased pricing. However, this finding is likely related to borrower activity in proactively managing their debt maturity profile. As these borrowers have a greater amount of debt tranches to manage, it is likely that at least one has required refinancing over the past two years, making it more probable they have been confronted by higher pricing and potential lending capacity issues from the banks.
- Only 23% of participants reported it was somewhat easier to secure debt funding when compared to two years ago.
- It appears that funding constraints are limited to the banking sector with only 18% of those active in the debt capital markets reporting it as being harder to obtain debt funding.

'Active' borrower actions by borrower segment



Securing debt funding based on number of banking relationships



Bank funding

2 Introduction

All respondents had some form of banking relationship with organisations on average receiving over 50% of their total debt funding from banks. This section explores how respondents are managing their bank debt arrangements. As part of this, we have considered the following aspects of participant's bank funding:

- *Tenor*
- *Security*
- *Facility type*
- *Ability to secure debt funding*
- *Banking relationships*
- *Covenants*
- *Facility structure*

Some of our key findings in relation to this section are highlighted below:

- Debt facility pricing remains the most important banking attribute for borrowers, featuring in 86% of respondents' top five most important banking criteria.
- 16% of smaller borrowers noted that their security arrangements were not commensurate with their risk profile.
- 38% of our larger borrower segment are interested in increasing their bank lending panel.
- 33% of those respondents with four or more banking relationships suggested they would have liked to receive longer dated funding.
- 24% of borrowers with three or more banking relationships were likely to increase their banking relationships in the future whereas only 10% of respondents with two banking relationships or less indicated a similar interest.
- 81% of participants reported having an average maturity of bank borrowings of three years or less which may be due to the significant increase in bank pricing for tenors longer than this time period.

Borrower segment	Average proportion of bank debt funding
Small	91%
Medium	73%
Large	53%

Number of banks used for funding

Respondents were asked how many core banks they were using to provide debt facilities.

- A surprising 51% of our medium sized borrowers are single banked, indicating that they may not be adequately diversified in their banking relationships. This is 15 percentage points higher than our findings for similar sized borrowers in 2015 and may indicate that there has been some consolidation in banking relationships over the past two years. It may be prudent for these borrowers to consider adding another bank to their lending panel to minimise the impact of any bank specific price and funding constraints.
- As one may expect, there is a strong positive relationship for an organisation between the number of banking relationships and debt levels. Bank exposure limits may be responsible for part of this as they encourage larger borrowers to expand their banking relationship to reduce their own risk. Facility pricing is increased reflecting a risk premium that is not included in other banks pricing offers.
- Those already in multi-banked relationships appear more comfortable with the prospect of further increases to their lending panel. When asked how the number of core banks was likely to change in the future, 24% with three or more core banks, advised that the number was likely to increase. Just 10% of respondents with two banking relationships or less provided the same answer.
- Only three organisations reported that their number of banking relationships was likely to decrease in the future, suggesting one of two things. Firstly, that organisations are relatively comfortable with the service provided by banks. Secondly, that organisations do not see their debt financing reducing by such an amount that they would be justified in reducing their banking relationships. Alternatively it may mean that debt levels are likely to increase.

When might you want to use more than one bank?

Typically, organisations may want to consider adding a second bank to their lending relationships when debt levels exceed $50 to $80 million. Introducing another lender can provide ease of access to additional lending capacity in the event your incumbent bank finds itself with lending capacity. This will also create a pricing tension which may lead to lower debt pricing. As part of this, achieving lender diversification also reduces a borrower's exposure to a single bank's cost of funds. It also allows the borrower to leverage individual bank relationships, credit appetite and services.

How is the number of core banks used likely to change in the future?

Respondents were asked whether they would like to increase or decrease the number of banks they used for funding, or maintain the same.

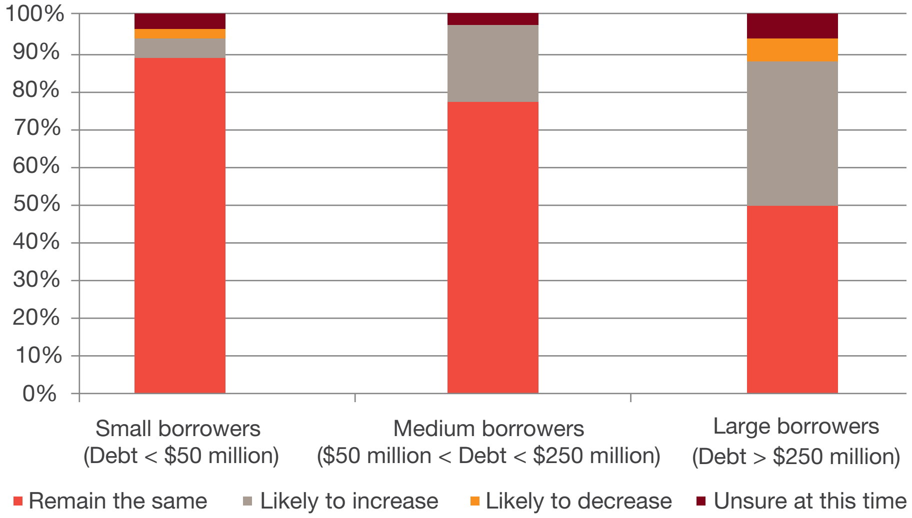
The majority of borrowers indicated they were content with the number of banks providing debt financing, with 81% of respondents specifying that the number of core banks would likely remain the same.

Borrowers using three banks or less were seemingly the most comfortable with these arrangements, as 84% of respondents noted the numbers of banks was likely to stay the same versus 50% of borrowers with four or more banks.

Our larger borrower segment was the most interested in increasing their lending panel with 38% of those respondents with debt greater than $250 million specifying that an increase was likely. Typically, changing the number of banks is driven by one of the four factors identified below:

- Changes in the amount of outstanding debt
- To install more competitive tension
- To become less reliant on the existing pool of lenders by increasing diversification
- The commitment of the bank lenders to the company and/or industry sector.

How is the number of core banks likely to change in the future?



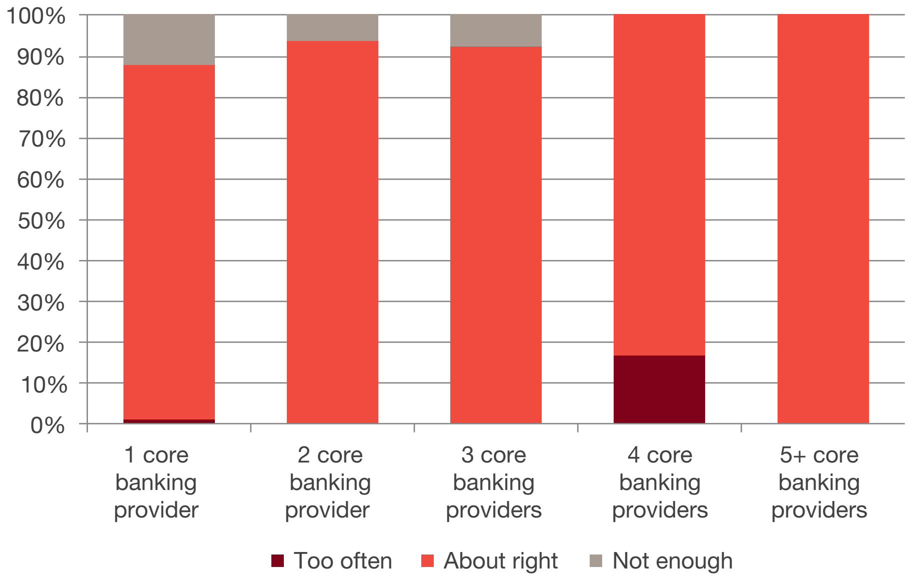
How often do banks talk to organisations about their funding needs?

Respondents were asked how often banks they used for funding proactively approached them to discuss funding needs. They were asked whether this was too often, about right or not often enough.

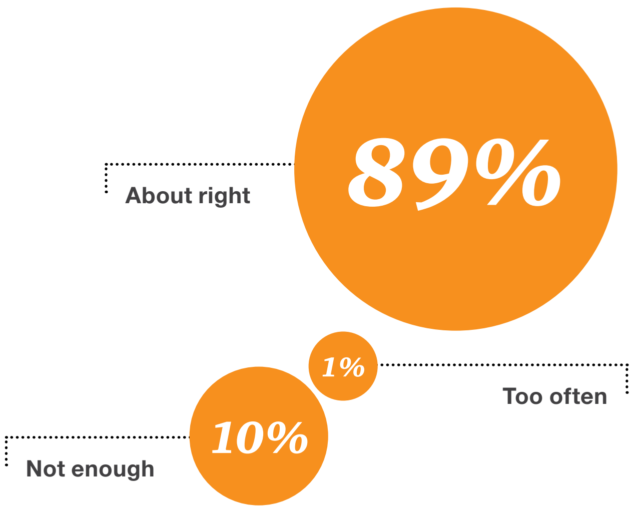
A resounding 89% signalled that the frequency of contact with their banks was about right which is broadly similar to our 2013 survey when 92% of participants provided this response. Such consistently strong scores suggest banks are continuing to do a good job in their engagement and communication with borrowers.

At times keeping up regular communication with borrowers can be challenging for banks as they seek to maintain a strong relationship and provide support to an organisation, whilst being cognisant of customer time pressures and overall strategic priorities. Contact between banks and borrowers must also be varied given borrower industry and circumstance. For example, a bank may be justified in getting in touch more regularly for a period of time if the organisation is completing an acquisition or divestment. Borrowers operating in industries where there is more cyclicality in demand, might experience less contact during seasonally quiet periods.

How often do banks get in touch given number of core banking providers?



How often do banks get in touch?



Current tenor of bank funding

Respondents were asked about the current average maturity of their bank funding.

When determining the maturity of bank debt funding, organisations typically face a trade-off between attaining funding certainty and the increased pricing such certainty commands. 81% of participants reported having an average maturity of bank borrowings of three years or less. As only 20% of this group indicated that their funding maturity had become shorter with the passing of time. There appears to be a clear preference to accept cheaper shorter dated funding. At the risk of labouring the point, the significant increase in bank pricing for tenors greater than three years is the likely reason for this.

Of those respondents with an average bank debt maturity of less than one year, the overwhelming majority (83%) came from our small borrower category with large borrowers comprising only 8% of this group. A possible reason behind this finding is that the small borrower segment is comprised of organisations with a low core debt requirement that requires a working capital facility to fund stock and debtors. Alternatively, it may be that large borrowers are taking a more proactive approach to debt management. For example, 21% of our smaller segment with funding less than one year signalled there had not been a change to the tenor of their debt funding over the past two years versus none of our large borrowers with a similar tenor. There could be a number of additional reasons for these results:

- It may be that these small borrowers are simply rolling over their facilities on a yearly basis to minimise pricing without paying much attention to any refinancing risk.
- This group of borrowers likely represents organisations smaller than their peers and it may be that they lack sufficient resources to pay attention to their debt maturities.
- These borrowers do not view their term debt as material enough to benefit from any of the advantages associated with having longer dated funding in place.

As debt levels increased, there was a noticeable trend towards longer dated bank debt facilities. For example, only 11% of small borrowers reported having maturities of three years or longer compared to 29% of medium borrowers and 38% of large borrowers.

These differences may be representative of banks being more willing to offer longer dated funding at more attractive pricing to large borrowers. The increases in bank funding costs over the last two years may have incentivised banks to take this action as the large borrower credit risk may be perceived to be better.

Original tenor of bank funding

Respondents were asked about the maximum tenor of bank funding available at their most recent bank debt refinancing.

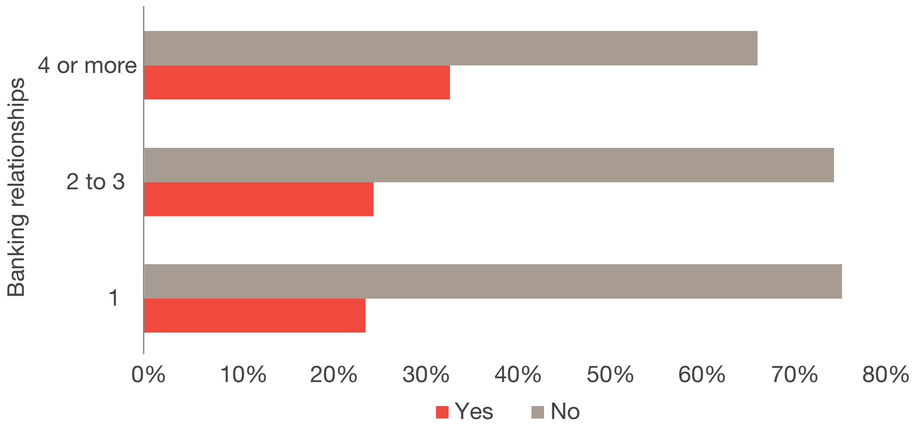
Despite 60% reporting a maximum tenor of three years or less, there does not appear to have been a significant decrease in bank credit appetite, as measured by tenor. Only 25% of all respondents signalled a desire to have achieved longer dated funding.

With respect to tenor, three years and five years were the most common funding tenors available for most respondents at 23% and 22% respectively.

It was also notable that twenty respondents indicated having received a maximum funding offer of less than one year. However, as only three of these borrowers signalled wanting a longer facility tenor, it may be that the facilities were used to fund seasonal working capital only.

Interestingly, when measuring respondent size by the number of banking relationships, it appears as though large borrowers were the most disappointed by the lack of tenor available. 33% of those respondents with four or more banking relationships suggested they would have liked to receive longer dated funding. This would continue to support our view that the debt capital markets should be explored for rated and non-rated organisations where bank debt exceeds $300 million.

Would you have liked the tenor of funding available to have been longer than the tenors received based on the number of banking relationships?



Bank facility features

In this question set, respondents were asked a range of questions about their banking facilities. Topics covered include bank facility structure, security requirements, financial covenants and respondents' most important banking attributes.

Facility structure

Organisations were asked about the bank facility structures they utilised whether these be syndicated, bilateral, club type arrangements or a combination of these facility types. Bilateral facilities were by far the most commonly employed with 51% of borrowers indicating they have one in place. This was followed by a syndicated structure (29%).

The advantage of bilateral facilities is evident in that it is easier for an entity to negotiate and take advantage of differential pricing (i.e. they can take advantage of individual bank pricing rather than being subjected to a collective pricing agreement). It also allows an organisation to draw down on the facility they choose (presumably the most cost efficient), rather than pro-rata across a panel of banks. However, the primary drawback with a bilateral arrangement across multiple banks is that if the terms and conditions are different, it increases the administrative time involved in managing debt funding and makes compliance a more complex issue. In such instances, banks normally insist on a club structure where terms, conditions and documentation is the same across all the lenders.

Syndicated facilities are aimed at reducing the time spent administering the facilities via the employment of a facility agent who interacts with lending banks on the borrower's behalf. For this reason, these facilities are typically only used by borrowers with a more complex credit situation which requires a spreading of risk across multiple banks or where the organisation has more than three banks in its lending panel and debt levels are generally higher. The most frequently cited disadvantages associated with syndicated facilities are the lack of flexible bank and facility management and the concern that the average clearing price for all lenders may not be as low as the average procured in bilateral negotiations.

Security

Consistent with our 2013 survey, the majority (85%) of respondents indicated that they did offer security to lenders. For the most part, this security was held under a General Security Agreement (GSA), though some borrowers, and particularly those with smaller financing requirements, did secure their facilities against specific revenue streams.

Interestingly, since 2013, organisations with a negative pledge arrangement in place have reduced by 15 percentage points, which may suggest that banks are becoming less willing to forgo security. Our recent bank debt observations suggest that with some banks, a five year unsecured facility is approximately 20 basis points more expensive than one with security in place. For most borrowers, it's likely that this is viewed as too steep a price to pay for the flexibility a negative pledge offers.

What is a syndicated facility?

A syndicated facility is a where a group of bank lenders (referred to as a syndicate) work together to provide funds for a single borrower. The main goal of syndicated lending is to spread the risk of a borrower defaulting across multiple lenders.

Effectively the banks pool their bilateral commitments to a borrower under the same terms and conditions and is managed by a facility agent who is typically one of the lending banks. It can involve a fixed amount of funds, a credit line or a combination of the two.

Drawdowns are done on a proportional allocation based on each banks total commitment. Syndicated facilities can either be unsecured or governed by a security trust deed where security is shared amongst the syndicate lenders. The facility agent will normally act as the security agent.

With respect to borrower 'happiness' with their security arrangements, we are pleased to report that on the whole, respondents seemed content as indicated by the 88% who felt their security arrangements were commensurate with their organisations risk profile. Perhaps most aggrieved were smaller borrowers (those with debt less than $50m) as 16% of this group suggested that their security was too restrictive.

A possible reasoning for this may be due to the borrower believing that the banks requirements are too intrusive. Conversely, as these borrowers are likely operating at a smaller scale, the bank may view it as necessary to offset any credit risk.

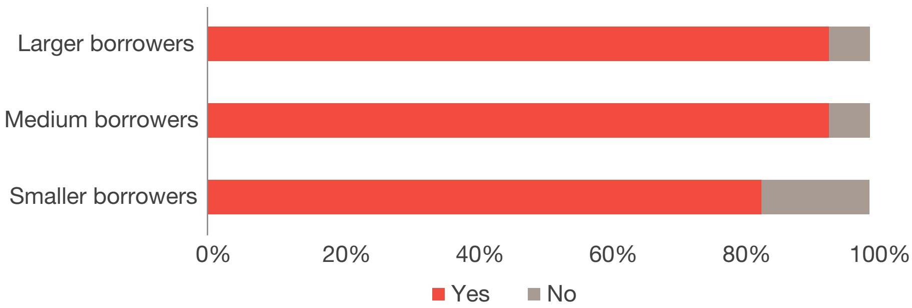
Covenants

The average number of financial covenants per respondent was 2.5, which indicates lenders value having multiple monitoring ratios in place. The most common covenants utilised by lenders were the EBITDA / Interest Coverage ratio (35% of borrowers) and Debt to Capital ratio (28%), which gives lenders comfort across both serviceability and solvency metrics. This also provides lenders with a more comprehensive view of both short and long-term credit risk.

For the most part, participants appear relatively content with their covenants and their respective limits, as indicated by the 88% who believe they are commensurate with their organisation's risk profile.

16% of smaller borrowers reported that their covenants are not appropriate. However, given that this borrower group only had slightly more covenants than our other borrower segments (2.6 vs 2.4) it may be that this is associated with covenant levels as opposed to the actual covenants. We did not ask respondents to report such thresholds as these absolute numerical levels, at which various covenants are set, would be largely reflective of borrower credit worthiness as well as sector.

Do you feel as though your security arrangements are commensurate with your organisations risk grade?



Covenant	Number of borrowers
EBITDA/Interest expense	46
EBIT/Interest expense	23
EBITDAF/Interest expense	4
Loan to value ratio	17
Debt/Total Assets or total tangible assets	35
Debt/Debt + Equity	37
Total liabilities/Total assets or total tangible assets	12
Stock and Debtors/Debt	20
Debt/EBITDA	29
Minimum equity must be maintained	16
Working capital covenants	12
Restrictions on the level of dividend distributions	21
Fixed charge cover ratio	10
Maximum capital expenditure level	9

Average covenants per borrower category

Borrower category	Average covenants per borrower
Small (Debt less than $50m)	2.6
Medium (Debt between $50m and $250m)	2.4
Large (Debt greater than $250m)	2.3

Facility type

Revolving credit and stand-by facilities were the two most utilised facilities, collectively featuring in 78% of responses.

Out of the two, the revolving credit facility was the most favoured (utilised by 65% of respondents), most likely for the flexibility it provides. When compared to other possible lending structures, such as a term loan, the revolving credit facility may be preferred as it allows borrowers to draw down on funds and repay them at their own convenience, enabling the minimisation of interest expense. Such optionality is particularly valuable for those borrowers with 'lumpy', seasonal or uncertain financing requirements.

As a stand-by facility is one which is not generally used except in a liquidity event, its prominent use implies some prudence on organisations' behalf in having another source of funding in place. Given that such facilities often have a low commitment fee and high lending margin; it is likely combined with other debt mechanisms. Alternatively, these facilities are used to stand behind commercial paper programmes.

What was surprising to us in this section was the relatively small number of respondents using committed or uncommitted seasonal and working capital facilities, with only 34% of respondents reporting having one. Given that these facilities are structured to minimise financing costs over periods in which organisations have a net cash balance, its lack of uptake suggests borrowers may not be cognisant of its benefits.

Bank attributes

Respondents were asked to rank the five most important attributes with respect to their banking relationships. To do so, they were asked to select from the following list:

- Counterparty risk (i.e. the credit worthiness of the bank/bank credit rating)
- Quality and coverage of service/advice including innovation (e.g. structure of a facility), customer service supporting geographical coverage
- Competitiveness of derivative/hedge pricing (e.g. swap and FX)
- Continuity and stability of bank relationship managers
- Knowledge of business/industry sector
- Pricing of debt facilities (fees and margins)
- Diversified banking group
- Historical loyalty to, and support of, the business in difficult times
- Flexibility, covenants, speed of response and execution
- Committed amount offered
- Tenor
- Minimum credit rating requirement

The following observations were made in relation to this question.

- Debt facility pricing was the most selected option, appearing in 86% of respondents' top five and most commonly as the top attribute. A possible reason for this may be that it provides borrowers with an easy way to differentiate amongst banks, providing the most compelling reason for lender selection. It could also be interpreted as showing there is a greater variance in bank debt pricing on offer from banks, making this factor more material to borrowers than other factors (such as funding tenor which should in theory be comparable across lenders).
- Flexibility, covenants, speed of response and execution were also highly regarded, with 71% of respondents selecting this option within their top five. From this, it's clear that a bank's service offering and ability to meet customer needs is a strong consideration for borrowers. In this instance, a strong reputation in market may precede banks and become an important consideration during a competitive refinancing process.
- Only 17% of respondents ranking counterparty risk as the most important attribute was a surprise and perhaps indicates some concern around the creditworthiness of financial institutions. Increased media coverage of debt crises may have been partly responsible for this in bringing some greater awareness to the health of the financial sector.
- It's also clear that relationships are greatly valued. To evidence this, consider that 61% reported continuity and stability of bank relationship managers as one of their top five most important attributes. Further to this 53% selected historical loyalty and support to the business in difficult times as an important attribute.

Placing of considerations in respondent's top five most important attributes

	1	2	3	4	5
Counterparty risk (i.e. the credit worthiness of the bank/bank credit rating)	17%	2%	5%	6%	9%
Quality and coverage of service/advice including innovation (e.g. structure of a facility), customer service support geographical coverage	11%	10%	8%	11%	10%
Competitiveness of derivative/hedge pricing	2%	6%	10%	5%	5%
Continuity and stability of bank relationship managers	5%	15%	11%	16%	14%
Knowledge of your business/industry sector	11%	16%	11%	13%	15%
Pricing of debt facilities (fees and margins)	27%	20%	20%	11%	8%
Diversified banking group	1%	1%	2%	2%	2%
Historical loyalty to, and support of the business in difficult times	15%	7%	9%	11%	11%
Flexibility, covenants, speed of response and execution	9%	16%	17%	12%	17%
Committed amount offered	2%	5%	6%	7%	4%
Tenor	-	2%	1%	5%	3%
Minimum credit rating requirement	-	-	-	1%	2%

3 Introduction

The intention of this section is to explore our respondents' interaction with the debt capital markets, specifically in relation to the following:

- *respondent activity in the debt capital markets*
- *lead arranger selection*
- *rationale for using the debt capital markets*

Some of our key findings in relation to this section are highlighted below:

58% of larger borrowers (average debt greater than $250m) indicated that they had found debt funding harder to attain when compared to two years ago. Comparatively, only 11% of debt capital market issuers in the same category noted facing such constraints.

43% of issuers in the debt capital markets identified as either a government or local government body.

71% of participants noted the most important reason for completing a debt capital markets issuance was due to the pricing.

Of those organisations issuing in the debt capital markets, 65% reported having a credit rating.

29% of those respondents active in the debt capital markets specified that the pricing indication received was their most important consideration when selecting a lead arranger. However, as this was closely followed by an arranger's track record and the strength of an arranger's wholesale and retail distribution channels, it does suggest that borrowers are pragmatic in seeking evidence that arrangers are able to deliver on the pricing expectation.

Do you utilise the debt capital markets for funding?

The vast majority of respondents (87%) do not use the debt capital markets. The most common reasons these organisations cited were the size of the debt requirements (53%) and that banks are comfortably providing the necessary funding (46%). Although these findings are unsurprising, they do emphasise the importance of scale in completing a debt capital markets transaction, which is particularly pertinent for organisations whose total debt levels are less than $100 million as they would likely struggle to generate adequate investor interest.

Those organisations with smaller debt requirements are also unlikely to have a credit rating, theoretically leaving them to rely on the banking market. Given these considerations, it appears likely that most domestic borrower's preference is to use bank debt until funding requirements are such that the banking market is unable to satisfy them. The debt capital markets and a credit rating may then be considered for larger subsequent transactions. To illustrate this, consider that of the respondents active in the debt capital markets, 71% had debt levels greater than $100 million.

It's also interesting to observe that 58% of larger borrowers (average debt greater than $250m) indicated that they had found debt funding harder to attain when compared to two years ago. Comparatively, only 11% of debt capital market issuers in the same category noted facing such constraints. Such a disparity in funding conditions for similar-sized borrowers alludes to there being some funding constraints in the banking sector when single counterparty debt requirements surpass $250 to $500 million (sector dependent).

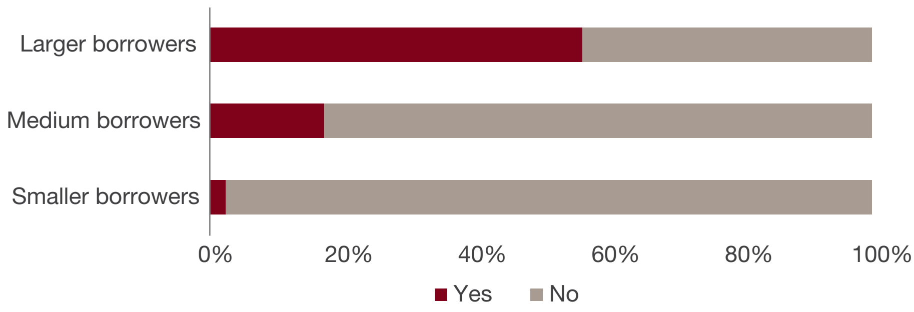
We observe that large borrowers access the debt capital markets as it continues to offer cheaper funding than bank loans and greater funding diversification. Although the debt capital markets have generally offered relatively cheaper debt pricing compared to bank funding, the spread difference between the two has become more pronounced over the past year. The reason why is associated with banks having to increase their debt pricing due to regulatory changes while bond pricing has been supported by investors searching for yield and diversification. As such, the case for a debt capital markets issuance appears attractive.

Further observations in relation to the debt capital markets are outlined below:

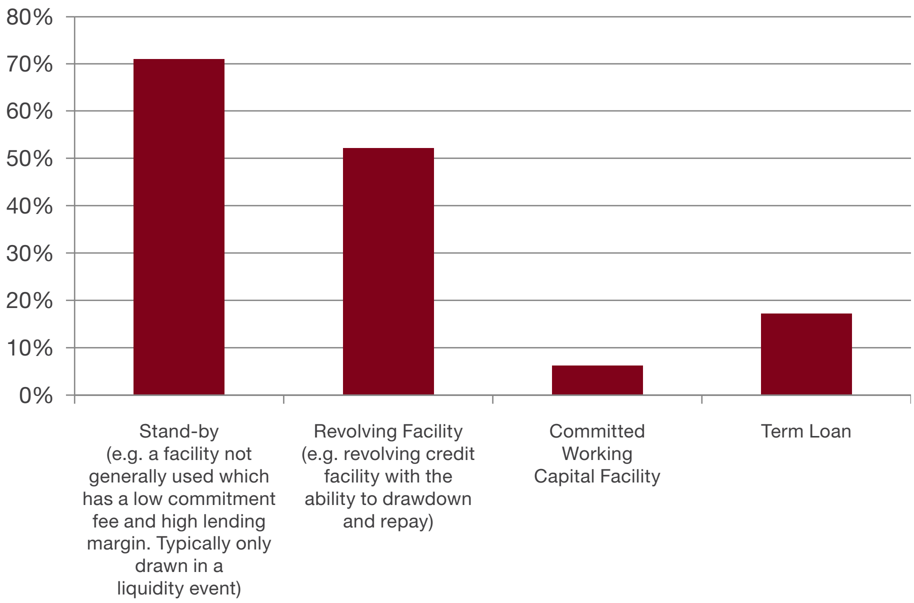
- Of those organisations issuing in the debt capital markets, 65% reported having a credit rating. The likely reason behind this is the improved access to debt markets such as the CP and wholesale markets, which see investors requiring a formal credit rating. Unrated issuers are able to access the domestic retail bond and US Private Placement markets; however, the lack of transparency associated with their risk rating means that investors in these markets may require higher pricing as compensation.
- By industry classification, 43% of issuers in the debt capital markets identified as either a government or local government body. The ability for local authorities to fund efficiently and at pricing lower than bank debt via the Local Government Funding Agency (LGFA) is the likely reason for this.
- 15% of those not currently issuing in the debt capital markets reported some form of interest in a future issuance. Of these respondents, 30% indicated seeking longer bank debt funding at their most recent bank debt refinancing. It may be that procuring longer dated funding is one of the key drivers behind this interest in the debt capital markets.

Debt Capital Markets continued

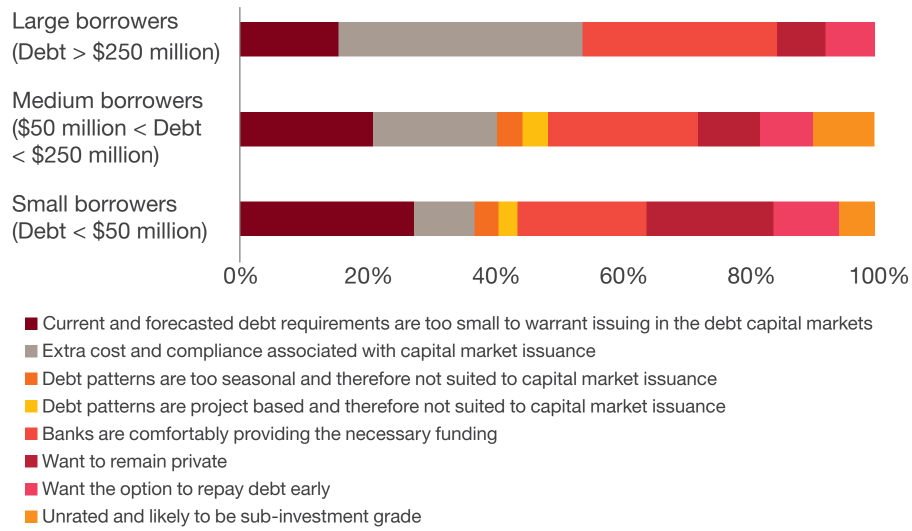
Do you issue in the Debt Capital Markets?



Bank debt facilities used by those active In DCM



Why don't you issue in Debt Capital Markets?



How is a lead arranger chosen?

Respondents were asked to rank their top five most important considerations with respect to the selection of an arranger for a debt capital markets issue.

The considerations that respondents were asked to rank are shown below:

- Track record of arranging debt issues (e.g. league table ranking)
- Pricing indication
- Relationship with bank
- Relationship with individual
- Arranger fees
- Rotation
- Strength of wholesale and retail distribution channels
- Reward arrangers who proactively bring innovative funding ideas to the organisation.

Our observations were:

- An arranger's pricing indication was noted as the most important determinant, earning 29% of all number one considerations, with such findings in stark contrast to our 2013 survey when it earned only 6%. This perhaps indicates a growing importance of arrangers in influencing the pricing outcome through their positioning of the credit story.
- An arranger's track record and the strength of an arranger's wholesale and retail distribution channels was the second most important attribute.
- Despite the keen focus on an arranger's capabilities and pricing, the only consideration to feature in every respondent's top five was banking relationships. This emphasises the importance issuers place on trust when executing a transaction and perhaps indicates issuers seek a degree of comfort in the sense of knowing how the arranger operates. It's also likely that establishing these bank relationships allows banks to have a greater understanding of the organisation and its requirements, making any transactions more 'light touch' for the issuer.
- Arranger rotation was found to be the least important consideration, appearing in only one respondent's top five. This is perhaps unsurprising as it's the opposite of selecting an arranger based on banking relationships, which scored strongly. It may also suggest that our respondents are not issuing regularly enough into the market for this factor to be an important consideration and instead prefer to stick with their primary relationship bank(s) when they do.
- Arranger fees appeared only once as an issuer's top consideration. The likely reason behind this finding is the high level of comparability between fees charged by arrangers.

What is the role of a lead arranger in a debt capital markets transaction?

The lead arranger is responsible for arranging and managing the bond issue process. This involves providing advice to the issuer around items such as issuance structure, timing and indicative pricing. Lead arrangers are also responsible for generating investor demand and holding investment roadshows so that major investors/brokers can understand more about the issuer. To complete such tasks, it's imperative that a lead arranger has a deep understanding of the issuer's business and credit profile.

Placing of considerations in respondent's top 5 most important lead arranger attributes

	1	2	3	4	5
Track record of arranging debt issues (e.g. league table ranking)	23%	18%	6%	29%	6%
Pricing indication	29%	24%	24%	6%	-
Relationship with bank	12%	23%	23%	12%	29%
Relationship with individual	6%	6%	6%	-	35%
Arranger fees	6%	-	17%	12%	12%
Rotation	-	6%	-	-	-
Strength of wholesale and retail distribution channels	18%	23%	6%	24%	6%
Reward arrangers who proactively bring innovative funding ideas to the organisation	6%	-	18%	17%	12%

Rationale for using the Debt Capital Markets

Respondents were asked to rank five considerations, from most important (ranked 1) to least (ranked 5), regarding why they chose debt capital markets funding over bank funding. With 15 points to allocate across the five categories, 3 represents an average score. The mean was then determined for the responses in each category and ranked in order of importance.

The five considerations were cost; diversification; the availability of longer tenor; the size of respondents funding requirements; and the marketability of the issue.

70% of participants ranked the pricing of debt capital market issuances as the most important. This was 14 percentage points higher than our 2013 survey where the consideration also received the top ranking. The increased divergence in bank debt pricing and debt capital market pricing over this period, is the likely reasoning for this result, with such issues now procuring a greater pricing benefit.

The tenor of funding available in the debt capital markets, which earned a mean score of 2.4, was the second most important consideration. As domestic bank debt lending is typically only available for a maximum tenor of five years, this is understandable as investors in the domestic debt capital markets are willing to lend funds for up to 12 years. Although in the US Private Placement market, the funding tenors available may be up to 20 years.

With a mean score of 2.9, diversification also scored lower than the average score of 3 and received the greatest amount of second-placed considerations at 41%. Awareness of having access to a variety of debt funding sources has increased significantly since the Global Financial Crisis when some borrowers were unable to procure debt funding.

Marketability was overwhelmingly the least important consideration, which suggests there is little concern around the liquidity in the domestic market. Low liquidity manifests itself in higher debt pricing with investors seeking a liquidity premium as compensation for this risk.

Placing of considerations in respondent's rationale for DCM issuances

	Mean score	1	2	3	4	5
Price	1.6	70%	12%	12%	-	6%
Maturity	2.4	18%	29%	47%	6%	-
Diversification	2.9	6%	41%	23%	12%	18%
Size	3.5	6%	12%	18%	53%	11%
Marketability	4.5	-	6%	-	29%	65%

Treasury policies relating to debt funding

4 Introduction

Survey participants were asked a number of questions concerning internal governance, focusing on liquidity and funding policies usually contained within formal treasury policies. We were interested in the level of board governance associated with these policies.

Some of our key findings in relation to this section are highlighted below:

43% of all borrowers had a formal debt financing policy.
- However, when observing borrowers with debt over $50 million, 67% have a formal refinancing policy.

54% of borrowers with a formal refinancing policy sought to prefund or refinance within a year of the debt maturing.

52% of Government/local government participants have adopted a formal refinancing policy.
- This is higher than the 32% of Government/local government respondents in our 2013 survey, suggesting an increasing priority for certainty around liquidity and debt pricing.

40% of 'all other organisations' had a formal refinancing policy.

44% of participants highlighted that they have a formalised liquidity headroom policy.

For companies with turnover less than $50 million, only 26% have a policy requiring a minimum level of committed liquidity headroom.

Only 44% of borrowers have a policy that requires the spreading of debt maturities.
- However, there is a strong link between the debt maturity requirement and debt size with 78% of participants with debt over $100 million reporting a formal debt maturity spreading policy.

74% of government/local government organisations have a policy requiring the spreading of debt maturities, compared to only 34% of 'all other entities'.

For organisations with turnover less than $50 million, only 26% have a policy that requires a minimum level of committed liquidity headroom.

For organisations witha formal liquidity buffer, 26% use a percentage of peak debt over a defined period and 24% a fixed dollar amount.

Of organisations with a formal liquidity buffer, 57% use both rolling forecasts and intra-month peak net cash flows, while 12% use neither.

Prefunding

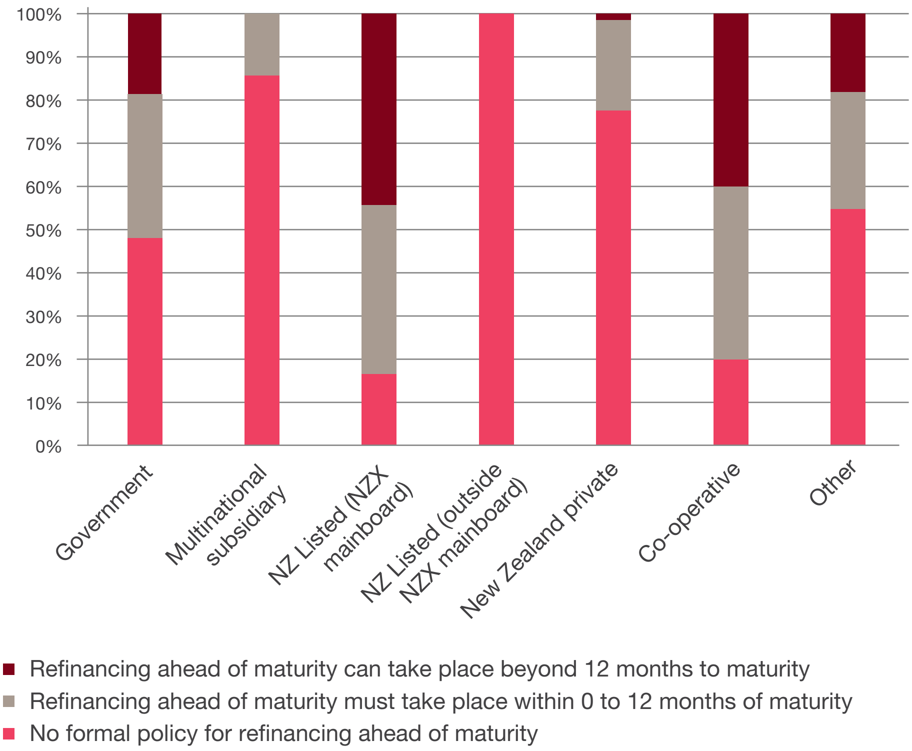
Prefunding is used by borrowers to manage refinancing and repricing risk. The purpose is for borrowers to have committed debt financing by the time debt facilities mature so there is surety around the continuity of liquidity and known debt pricing. When completed early enough, it also prevents long term liabilities from becoming current, which can impact financial reporting.

Of our respondent base, 43% indicated that they had some form of refinancing policy with most borrowers seeking to prefund or refinance within the year of their debt maturing. Of the 57% of respondents without a formal prefunding policy, 77% had debt levels less than $50 million, which perhaps indicates the lack of materiality of their debt. When observing those respondents with debt greater than $50 million, the percentage of respondents that have some form of refinancing policy in place increases to 67%.

It is interesting to note that 52% of Government/local government participants have adopted a formal refinancing policy, up from 32% in our 2013 survey. This is higher than all other entities of whom only 40% have a formal policy in place. 71% of the Government/local government respondents had debt levels greater than $50 million which has likely encouraged these organisations to become more prudent around their refinancing risk.

Analysing results across sectors produces some interesting insights. Our findings show that listed companies are most likely to have a formal refinancing policy. It is likely a combination of the accounting treatment of non-current liabilities for financial reporting purposes, solvency tests as well as the comfort provided to shareholders around ongoing balance sheet funding. Conversely, only 22% of private companies reported having a formal policy. The result is lower than what we would expect for private companies, especially considering 83% of this category reported that pricing of debt facilities was an important attribute with respect to banking relationships. However, this is not to say that refinancing is not a priority for private companies as it may be that an 'informal' policy is in place.

Refinancing policy by sector



Spreading of debt maturities

This question focuses on an organisation's refinancing policy. In particular, it aims to understand which respondents have an established debt management policy to manage refinancing risk.

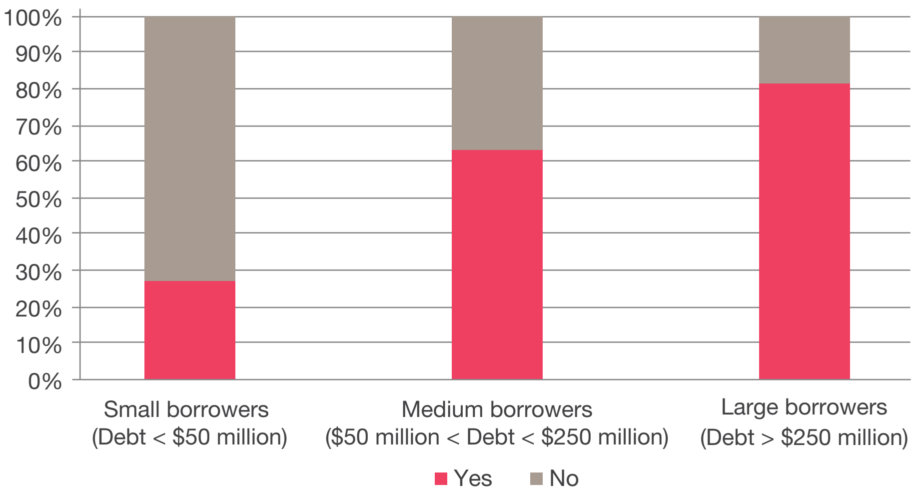
A key factor and objective of funding risk management is to control, spread and reduce concentration of risk at one point in time so that the overall interest cost is not unnecessarily increased and funding flexibility restricted.

Despite similarities with the refinancing question, a surprising 56% of borrowers indicated that they did not have a policy that requires the spreading of debt maturities. When compared to our 2013 survey, this is 11 percent higher and means the majority of our respondents now operate without a formal policy in place. However, it's important to note that the level of debt appears to be an important determinant in whether there is a policy. For example, only 28% of our respondents with debt less than $50 million had a policy, compared to 69% of those with debt levels greater than $50 million.

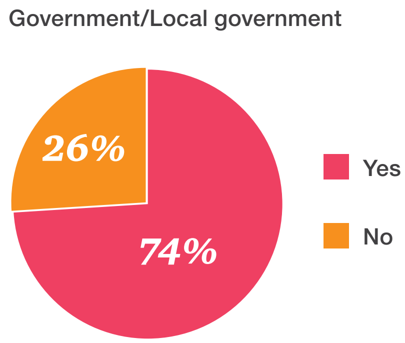
It is clear that the absolute level of debt is a significant driver of the importance placed upon debt management and the desire to manage refinancing risk. Given the size of the New Zealand debt market, these larger borrowers are more susceptible to investor disruptions through credit constraints, insufficient liquidity and/or appetite for large amounts of debt. This reinforces the need for formal debt maturity and specific debt market frameworks. It may also be that these larger borrowers have greater resources to put towards designing, implementing and monitoring such procedures. We also suspect that most 'smaller' borrowers are likely to have only a single debt facility so see no need for a formal policy.

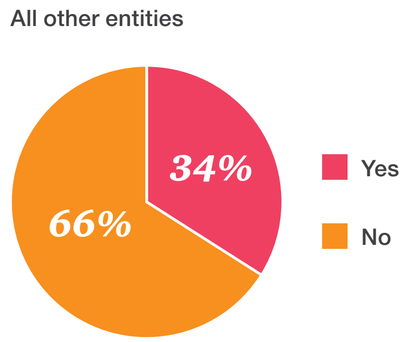
In relation to how borrowers spread their debt maturities, most use either a maximum annual amount or a bucketed approach stipulating minimum and maximum percentages of debt maturing across certain time buckets. Also, tenor availability constraints in the New Zealand debt market can restrict the use of longer dated time buckets. This provides borrowers with greater flexibility in managing their debt maturities and may be favoured by larger borrowers due to it providing more discretion to opportunistically raise funds at 'sweet spots' in the credit curve. The larger debt amounts may also make it too administratively burdensome for an organisation to maintain compliance with debt maturity financing buckets.

Does your organisation have a policy that requires the spreading of debt maturities?



Does your organisation have a policy that requires the spreading of debt maturities?





Regarding sector types, the results again vary significantly between the government/local government sector and 'all other entities'. 74% of government/local government organisations have a formal policy in place requiring the spreading of debt maturities, compared to only 34% of 'all other entities'.

Liquidity

Respondents were asked if they have a policy that requires a minimum level of committed liquidity headroom in the facilities and cash held. Headroom is the total amount of undrawn committed facilities or cash that an organisation is able to access to absorb unexpected shortfalls in cashflow.

Only 44% of survey participants have a formalised liquidity headroom policy. However, this percentage increases to 71% when observing participants with debt above $50 million. Through economies of scale, larger debt holders may be able to carry excess liquidity at a lower cost than smaller organisations.

Still, it's equally important that smaller businesses maintain a prudent liquidity buffer. Only 26% of surveyed participants with turnover less than $50 million have a policy that requires a minimum level of committed liquidity headroom. However, it can often be the case that these organisations have a greater need for such a policy given they may be more susceptible to liquidity constraints from a downturn in revenue (i.e. a decrease in cashflow has a larger impact on serviceability and solvency ratios). As such, a liquidity headroom requirement remains an essential aspect of any robust Treasury Policy.

There is however a cost to having excess liquidity (e.g. commitment fees on committed borrowing facilities) or holding cash. Perhaps this is a barrier to more organisations having a minimum liquidity buffer in place. Setting an appropriate liquidity buffer that measures the cost of excess liquidity with the risks of insufficient access to liquid funds is critical. Of those that do maintain a minimum liquidity buffer requirement, there is a relatively even spread as to how these are calculated as illustrated on the chart below.

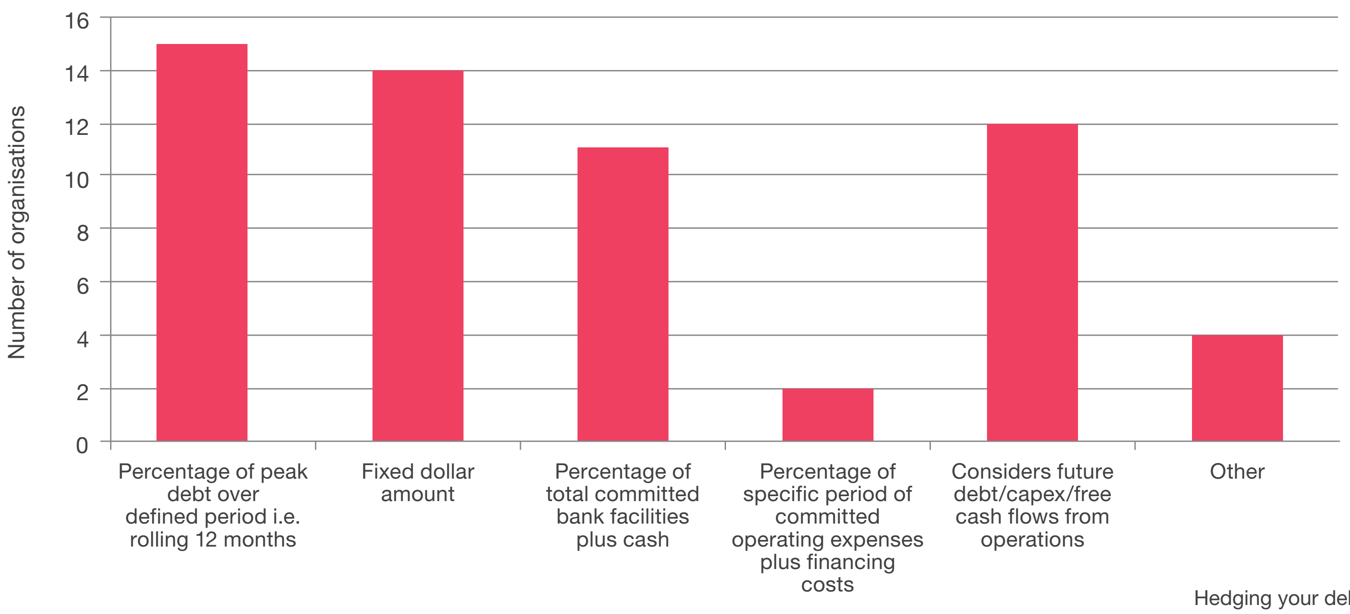
There is no right or wrong approach to calculating the minimum liquidity buffer. It is a bespoke procedure that will depend on the nature and size of the organisation and its industry. The two most common measures identified from the survey were a percentage of peak debt over a defined period (26%) and a fixed dollar amount (24%).

For example, the fixed dollar limit may be well suited to a mature company in a developed industry that has a stable debt forecast. However, it may be less appropriate for a company at an earlier stage of its life cycle with a growing debt forecast where the initial dollar limit will quickly become disproportionate to the size of the organisation's debt.

Variations will also be observed in the size of the liquidity buffer, which is to be expected. Entities with smoother, more predictable cash flows could carry a smaller buffer amount than those that may have more volatility in their cashflows or a greater degree of forecast uncertainty.

Regardless of the method, all require a robust debt forecasting process. The 58 participants whose policy includes a minimum liquidity buffer requirement were asked whether rolling forecasts and intra-month peak net cash flows were considered when determining the size of the buffer. Of the 58 participants, only seven did not consider either of these elements while 33 considered both. The majority of these seven participants tended to use a percentage of total committed bank facilities plus cash as their formal liquidity buffer. Incorporating month end debt levels as opposed to intra month peak debt levels within the peak debt forecast is often an overlooked discrepancy, which can lead to an understatement of future debt requirements due to intra-month debt fluctuations. Typically, these intra-month fluctuations are due to the timings of working capital cash flow during the month.

How is your liquidity headroom amount derived?



Net working capital

5 Introduction

Respondents were asked a variety of questions relating to their net working capital position and about any difficulty in forecasting net working capital.

Some of our key findings in relation to this section are highlighted below:

58% of borrowers signalling that working capital was positive in each quarter of the year which reduces to 25% when assessing borrowers with debt above $100 million.

10% of borrowers have a negative working capital balance in each quarter of the year.

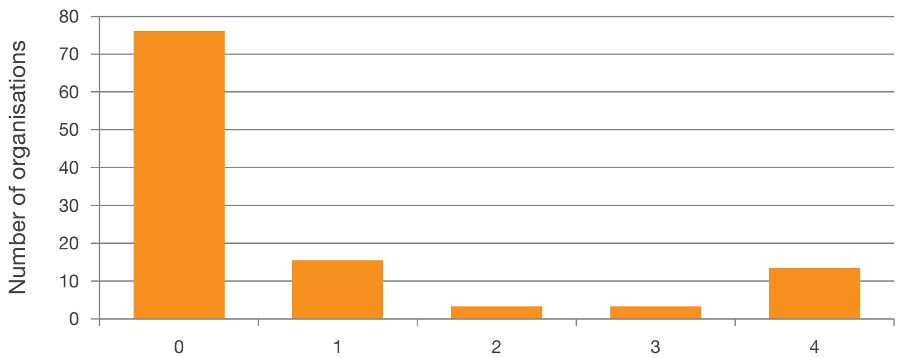
The retail industry experiences the largest degree of seasonal working capital fluctuations, followed by the agribusiness sector.

18% of all organisations had difficulty forecasting their net working capital.
- only 46% of respondents who had difficulty forecasting net working capital had a policy in place that requires a minimum liquidity buffer.
- 32% of the government/local government participants had difficulty in net working capital forecasting.

7% utilise a committed seasonal facility and 22% utilise a committed working capital facility.

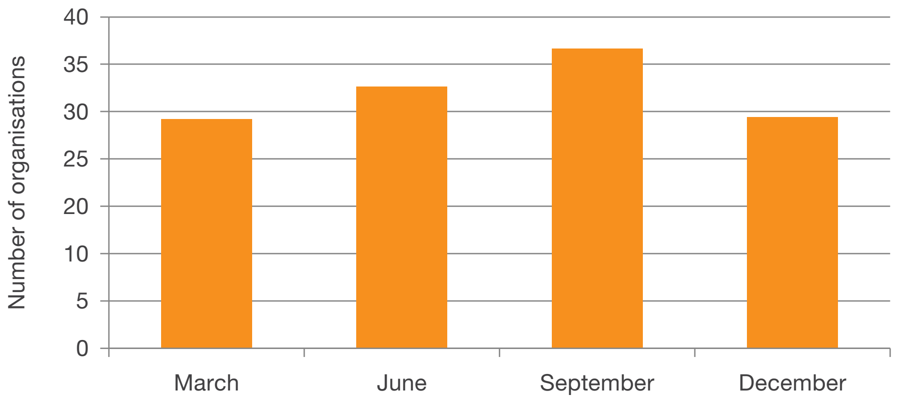
85% of companies using seasonal/working capital facilities thought pricing was commensurate with the organisation's risk.

Number of quarters each organisation has a negative working capital balance



Analysing the results on a quarterly basis across all survey participants, there is a relatively even spread in working capital balances throughout the year. The quarter where participants most frequently reported a negative working capital balance was September, although this was only slightly higher than the low in March.

Number of organisations with a negative working capital balance by quarter



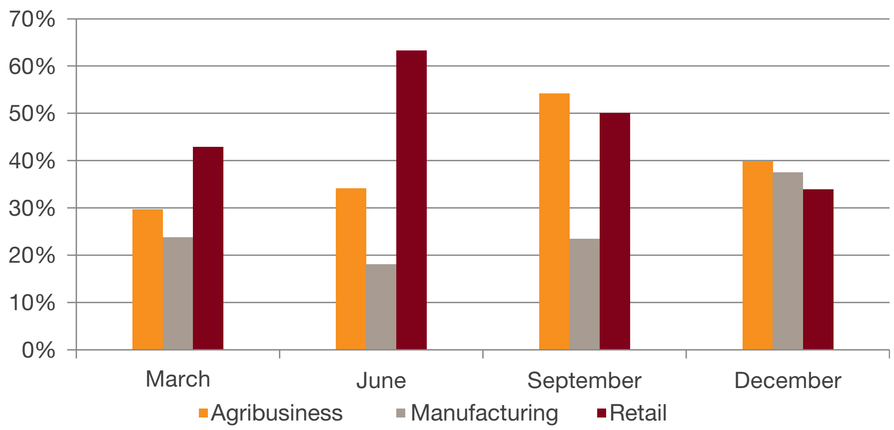
However, when we break down the results by sector, we can see that certain sectors are more vulnerable to seasonal working capital fluctuations than others. For instance, the retail sector experiences the largest seasonal fluctuations, with 64% of retail participants reporting negative working capital in the June quarter (buying ahead of the upcoming summer season), up from a December low of 36%. The result is not surprising given the seasonal nature of consumer spending patterns and the associated importance of inventory management.

Seasonal working capital fluctuations are also a characteristic of the agribusiness sector with 55% of agribusiness participants experiencing negative working capital in the September quarter, up from a March low of 30%. One potential reason for this is that September marks the change of dairy season where dairy participants within the agribusiness sector may draw down available cash and cash equivalents to invest in stock, technology, equipment etc. ahead of the upcoming season.

The manufacturing sector also shows seasonal fluctuations, although these are muted compared to retail and agribusiness. 38% of manufacturing participants experienced negative working capital in December where credit terms may be extended over the Christmas period, compared to only 19% in June.

Net working capital continued

% of sector participants with negative working capital by quarter



Given the relatively even spread in working capital balances throughout the year for most sectors, there is less appetite than initially expected for seasonal facilities in the New Zealand market. Only 7% of respondents utilising a committed seasonal facility and 22% utilising a committed working capital facility.

Of the 29% of respondents with either a committed seasonal or working capital facility, 63% operated on a fixed facility limit throughout the year with the remaining 37% opting for a variable limit at specific times of the year. Despite the flexibility associated with these facility types, 82% of those with fixed facility limits and 90% of those with a variable limit reported that pricing was commensurate with the organisation's risk profile.

As a follow up question, respondents were asked if they had any difficulty in forecasting their net working capital. Of these, only 18% of respondents said this was an area they struggled with.

Given that 58% of all respondents reported a consistently positive working capital position, it may be that across the survey participants, the net working capital balance is relatively predictable or movements are not material enough to draw concern.

The government/local government participants observed the highest level of forecast uncertainty with 32% of the sector reporting difficulty in net working capital forecasting. One possible reason for this could be the varying degrees of reliance on Government grants for net working capital funding, which have historically had a significant aspect of timing uncertainty. Local authorities also have significant difficulty in forecasting debt amounts associated with their capital programmes.

The 18% of participants that noted having difficulty forecasting their net working capital were subsequently questioned about the key driver of this difficulty. These results indicated there was no primary driver with revenue volatility, accounts payable, inventory management and accounts receivable all attracting a similar amount of justification. Within these responses, the only definitive conclusion is that smaller borrowers were seemingly more affected by revenue volatility as 56% of respondents with debt less than $10 million selected this as the primary reason why. It is likely that these smaller operations are more susceptible to changes in customer demand and less able to benefit from economies of scale in sector downturns.

What's more, it's worth noting that only 46% of respondents who had difficulty forecasting net working capital had a policy in place that requires a minimum liquidity buffer. A liquidity buffer amount is one way an organisation can manage forecast uncertainty in working capital cashflows.

Respondent profile

6 Organisation ownership

Respondents were asked to categorise which entity type their organisation primarily sits within.

The respondents covered a wide range of publicly listed, government and private entities. The strong response rate has ensured that all categories have a significant population. It should also be noted that the government category is predominantly made up of local authorities. For comparative purposes we have provided the respondent composition for our last two treasury surveys as well.

Participant organisation profile	%	2015 Survey %	2013 Survey %
New Zealand private	44	43	23
Government (including local government, council controlled organisations and state owned enterprises)	21	20	39
New Zealand Listed (NZX mainboard listed)	14	12	38
Other	8	12	
Multinational subsidiary	5	11	
Co-operative	4	-	
Foreign owned private (not multinational subsidiary)	3	2	
New Zealand Listed (outside NZX mainboard)	1	-	

Industry sector:

Respondents were asked to categorise which industry sectors their organisation identifies operating within.

The results show a wide distribution of responses across all industries with the top five industries being government/local government (24%), manufacturing (16%), agribusiness (15%), property/real estate (11%) and retail (11%). The breakdown is similar to that of the 2015 survey with manufacturing, agribusiness and government/local government in the top five of both surveys.

Respondent industry sector composition from our 2015 survey has also been provided in the table below. We have been unable to provide our 2013 survey composition due to changes in the way respondents were grouped.

Participant organisation profile	%	2015 Survey %
Government/Local Government	24	9
Manufacturing	16	13
Agribusiness	15	11
Property/real estate	11	2
Retail	11	3
Transportation, logistics and infrastructure	10	7
Energy and utilities	8	11
Construction	5	5
Financial services	5	6
Healthcare	5	4
Consumer products	5	4
Food services	4	1
Aged care	3	1
Education	3	11
Asset management	2	
Electronic and technology	2	3
Automotive/machinery	2	1
Business services	2	
Forestry	2	
Telecommunications	2	3
Tourism and hotels	2	1
Other	8	10

PwC Treasury and Debt Advisory

Our Debt Advisory service covers all aspects of debt and capital markets, helping borrowers and shareholders achieve their financing objectives. We advise across the cycle – including working capital solutions to fund seasonal demand, refinancing existing debt facilities to support growth or raising new debt for capital projects.

We specialise in assessing a borrower's credit metrics and undertake shadow credit rating processes.

Debt raising and refinancing advice

- Independent advice on bank facility structure, pricing, security structure, covenants and strategy – separate from funding sources.
- Independent market benchmarking of bank debt pricing and terms/conditions.
- Assistance with debt RFP/tender projects.
- Advice on structured financing, securitisation, project financing, senior and mezzanine debt.

Capital management/gearing review

- Balance sheet gearing reviews - determining debt-sizing, optimising shareholder returns and capital structure.
- Capital management strategies and policies.
- Funding risk policies – debt tenor and sources.
- Evaluation of credit metrics and providing shadow credit rating opinions.

Debt Capital Markets advisory

- Advisory and arrangement roles for debt capital market issues.
- Global and domestic debt market analysis/insights.
- US Private Placement debt market agent capability.
- Assistance with transaction marketing and legal documentation.

Cash & Fixed Interest Investment Portfolios

- Independent advice to wholesale clients who invest directly into bank deposits, bonds and fixed interest securities.
- Design and review of investment policies.
- Specific recommendations on security selection and transaction execution.
- Portfolio valuation, performance benchmarking and reporting.

PwC's retained treasury advisory relationship will provide a disciplined framework to manage financial and commodity market risks, a valuable input when treasury management is only a part of your finance responsibilities. We pride ourselves on offering proactive hedging advice – not simply financial market updates – so that you can see and measure the value that we add.

We also deliver market best-practice advice on treasury policy and hedging strategy design and reviews. Our debt, investment, interest rate and foreign exchange advice provides comfort and assurance to management and the Board when making important financial decisions.

Treasury policy design/review

- Applying global best practice and governance to entities of all sizes.
- Business risk analysis and advanced modelling to support hedging limits.
- Testing of controls, procedures and reporting requirements.
- Performance measurement methods.
- Documenting of policy statements.
- Asset and liability management: maturity and interest rate gap analysis

Derivatives and financial instruments

- Independent price checking/verification.
- Pricing of alternative hedging methods and techniques.
- Analysis of cash flow implications, accounting treatment and credit usage.
- Restructuring of derivative portfolios.
- Treasury management training courses.

Treasury systems/operations

- Review of treasury management software systems (TMS) requirements.
- Assistance with RFP/tender process for TMS.
- Review of internal controls and operational risks.
- Treasury department structure and scope.
- Treasury procedures manuals.
- Seconding of treasury staff resources.

Hedging solutions and programmes

- Foreign exchange, interest rate and commodity price risk management solutions.
- Client specific hedging recommendations.
- Monitoring of exposure/hedged positions.
- Retained advisory role ensures disciplined approach, continuity and commitment.
- Proactive advice and risk management strategies.

Get in touch

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