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Investment Banking

PICPA Annual Convention

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INTRODUCTION

- Many investment banking and corporate finance opportunities exist especially with the growing economy.
- The Accounting and Investment Banking professions are partners and will benefit from these activities.
- This presentation summarizes the state of investment banking and the capital markets so you can position yourself and advantage of opportunities.

OVERALL TRENDS

POWER OF BANKS

- As of 8.2009, total financial resources of the Phil. Financial System was P7.4 trillion.
 - The banks accounted for **81%** or P5.98 trillion.
 - **88% of bank resources were with the Unibanks and Commercial Banks**, 9% with Thrift Banks and 3% with Rural Banks.
- Total loans of banks reached P2.96 trillion and **total deposits P 4.32 trillion**. Compare this to the Philippine stock market which has around 250 listed companies with **a total market capitalization of P1.02 trillion**.

LOTS OF CAPITAL NEEDS

3Q08 - 3Q09 Growth		
	PHP BNs	%
LOANS "demand"	460	20%
DEPOSITS "supply"	796	19%

- Despite tight credit, a lot of loans continue to get booked.
- Deposits continue to surge as remittances increase (\$17.3bn in 09). Special Deposit Accounts (SDAs) also estimated at P1Trn.

INCREASING BOND ISSUANCES

2009 issues

ROP	\$1.5Bn	RTB	P117Bn
Globe	P5.0Bn	Robinsons Land	P10Bn
BDO Tier 2	P2.5Bn	Megaworld	P10Bn
SBTC Tier 2	P3Bn	Filinvest	P5Bn
RCBC Tier 2	P4Bn	JG Summit	P9Bn
Aboitiz Power	P3Bn		
SMB	P39Bn		
HGC/NHMFC	P1.86Bn		
Petron*	P10Bn		
SMIC	P10Bn		
EDC*	P7.5Bn		

* privately placed corporate note



INCREASING BOND ISSUANCES

2010 issues

EDC	P12Bn	RTB	P100Bn
Tanduay	P5Bn	OFW Bond	\$500mm
Petron Pref	P10bn	ROP Global	\$1Bn
Ayala	P10bn		

- Investors looking to diversity out of traditional deposits and this accelerated growth of local bond markets.
- All of existing bond issuances though for strong operating companies with long track records.

FIXED INCOME

- Majority of funding still comes from private placements through banks – bilateral or syndicated loans. Banks are very liquid and continue to look for loans.
- However, large corporates are reaching their Single Borrower Limits (SBL) so need to issue securities. Hence increasing bonds, preferreds, etc.
- Over P200bn in bonds have been issued in 2009 and around P100bn is expected til end of the year.

LOCAL FUNDING AND ABSORPTIVE CAPACITY

	5 Years Ago	Today
Tenor	5 yrs	12 yrs
Amount	P3Bn	P20Bn
Type	Plain vanilla corp	Non recourse PF
Bank's SBL	P1Bn	P15Bn

INFRASTRUCTURE NEEDS

- The large capital needs of the private sector are mainly in infrastructure.
- The problem here is that these are mainly start-ups.
- Even “brownfield” projects (as opposed to “greenfield”) are more project finance in nature and therefore best raised via syndicated loans.
- Mature infrastructure projects are *currently* the ones who can tap the bond and equity markets.

POTENTIAL EQUITY DEALS*

Project	Loan Amount
Toll Road spur in Luzon	P 2-2.5 B
600 MW Coal Power Plant in Luzon	US\$700 M
225 MW Hydroelectric Power Plant in Mindanao	US\$350 M
Toll Road in Luzon	Up to P10B
Toll Road in Luzon	P 8-9 B
MRT 7	US\$ 400M

* Typical structure of 70% debt and 30% equity. These are sample announced deals.

POTENTIAL EQUITY DEALS

OTHER DEALS IN THE PIPELINE:

- Many other project finance and PPP projects identified by Govt. week. These are likely to be use private equity and bank financing
- Many IPOs next few months such as IP Converge, SL Agritech, Megawide Construction, Semiconductor, Retail, Financing, Real Estate companies.

EQUITY ISSUES

- In the US, equities have historically yielded higher than fixed income securities. This is consistent with axiom of higher risk, higher yield.
- Problem in the Philippines is erratic market over certain periods.
- Foreign venture capital firms want 25-30% returns on their local investments. Other large local conglomerates want at least 15% return for their projects (compared to around 8% for ROP bonds).
- Retail investors have no access to foreign equity.

INVESTMENT BANKING INDUSTRY & ACTIVITIES

INTRODUCTION TO INDUSTRY

- 40+ Investment Houses in the Philippines
- Minimum capitalization of P300mm
- Regulated by SEC. Banks subs and those with quasi banking (QB) and trust licenses also under BSP
- Universal banks have investment banking powers and some do not set up separate subs
- Although industry has P28bn in capital and over P50bn in total assets, it helps raise capital for the government and corporates in multi billions
- Works a lot with SEC, BSP and PSE for actual issues

COMPARISON TO BANKING

	Investment House	Commercial Bank
<i>Min Capitalization</i>	P300mm	P3bn (KB) P5bn (EKB)
<i>Main Revenue Sources</i>	Fees from advisory and underwriting	Interest income from lending
<i>Main Funding Sources</i>	Borrowing	Deposits
<i>Regulator</i>	SEC (also BSP for some)	BSP
<i>Liquidity Support</i>	None	BSP

MAJOR ACTIVITIES

- Financial advisory
- Capital raising
- Trading and underwriting of securities
- Investments*
- Trust*

*same functions as bank

Each Investment House has its own specialty. The smaller ones usually focus on advisory.

FINANCIAL ADVISORY (Corporate Finance)

- Advisories include:
 - Corporate restructuring
 - Mergers & Acquisitions (M&A)
 - Sale or spin-off of businesses/divisions
 - Project financing
- Entails less capital but expertise and track records are a must to differentiate oneself.
- Local IH's dominate local advisories while foreign IH's do more of the large M&As especially when foreign investors are required.
- Fees usually consist of retainers and success

CAPITAL RAISING

- An IH can have multiple roles which can include being advisor, arranger, participant and even agent and trustee.
 - Arrangers can charge 0.3% - 1.5% (smaller IH's only arrange and don't lend)
 - Participants can get 0.1% - 1.0% (depending on level)
 - As part of capital raising, IH's play an important role in providing disintermediation.

TRADING & UNDERWRITING

- IH's will underwrite select government and corporate transactions such as bonds and equities.
- Underwriting is a real risk and taken seriously. Syndicates usually formed for larger deals. An IH can underwrite up to 20 times its capital.
- Underwriting fees are usually a fixed spread, e.g. 0.5-1% for debt and 1.5-3% for equity.

INVESTMENTS & TRUST

- Some IH's manage funds and make investments:
 - Put in equity pre IPO (ala venture capital) or listed (as portfolio or part of fund)
 - Invest in special projects like e-commerce start ups, special new ventures, industrial parks, turn around companies, etc.
- They make fees from successful investments and for managing investments. Can also earn when a company goes public and they sell hopefully with significant upside.
- Some IH's with adequate funding also make loans to select companies.

CAPITAL RAISING OPTIONS

- Senior Debt (private and public)
- Mezzanine
- Preferred Shares
- Convertibles
- Common Shares
 - Private Placement
 - Initial Public Offer (“IPO”)
 - Listing by Introduction (“LBI”)
 - Rights Offer
 - Follow On Offer (“FOO”)
 - Backdoor Listing

ISSUES TO CONSIDER

- Story Line and Purpose
- Structure
- Valuation
- Timing
- Fees and Costs

WHAT'S YOUR STORY?

- Profitable fast growing companies may need equity to support growth.
- Stable mature companies may not need equity but may want to list for inheritance purposes.
- If you are a sinking ship, why will someone inject equity? They might value your shares very low and gain control.
- The ideal equity raising candidate is when you have:
 - A good business story – “strong business model with competitive advantage”
 - Quality management and directors
 - Robust growth strategy in growing market
 - Established processes and governance
 - Audited financials from established auditors

ISSUE SIZE & STRUCTURE

DEBT

- Size
- Tenor
- Amortization
- Pricing
- Covenants
- Credit Rating

ISSUE SIZE & STRUCTURE

EQUITY

- Determine mix of primary and secondary. A secondary tranche enables the existing shareholders to sell, increases issue size and liquidity of stock and also reduces the IPO tax.
- Consider impact on dilution and control and also on foreign ownership limits.
- Value in having 67% (for super majority) or at least 33% (to be block for super majority)
- You will be in radar screen of foreign investors once your market cap reaches \$300mm. They invest \$5-50mm so want stocks with large liquidity.

VALUATION

- Investors will look at P/E and other trading comparables like P/EBITDA, P/B or P/NAV. Discounted Cash Flow (DCF) can also be used when a company is not yet making money.

Segment	P/E	
Utilities	10-14	
Oil	7-9	
Food/Beverage	20	
Conglomerates	24	
Large RE	28	also uses NAV
Media	24	
Banks	18-24	more P/B

- An IPO can usually yield the highest value for a company.
- FOO also usually a discount to trading price, e.g. 3-10%.

VALUATION (cont)

- PP usually has large discount to listed peers as pre-IPO discount and to give them upside. Have seen deals priced at 5-7x EBITDA.
- Rights usually have larger discount than IPO/FOO to incentivize existing investors to invest. Allows them to average down. Can be priced even up to half market price or at par.
- Convertibles priced at discount to trading price in return for lower coupon.

TIMING

- Best time to do public offer early December (when budgets have not been filled) and Jan-Feb (when new budgets just given)
- Avoid “Ghost Month” and second half of December.
- IPO/FOO/Backdoor longest to do while PP/Rights can be done faster.
- Private placements can be done in days or up to 2 months.
- Assuming housekeeping issues done, a public offer can be done in 3 months from mandate:
 - 6 weeks for prospectus preparation and filing
 - 4 weeks for PSE/SEC approval
 - 2 weeks for Offer Period
 - 1 week for clearing/settlement/listing

OTHER ISSUES

- **Need to do housekeeping regardless of instrument:**
 - Need to show “real numbers” and may need to change auditors. May need to have interim audit and projections.
 - Consider possible tax amnesty
 - Install corporate governance (independent directors, board composition and various required committees)
 - Set dividend policy
 - Remove leakages, document all third party and related transactions, and make these all arms length.

CONCLUSION

- Many opportunities for the Accounting profession to partner with the Investment Banking/Corporate Finance side.
- The underwriting and trust activities require specific licenses but the corporate and advisory side is really open to the Accounting Profession.
- SEC/PSE would require audits for public issues so you have a major role for IPOs, Bonds, Preferred, etc.

CONCLUSION

- You can also develop new businesses doing:
 - Due diligence
 - Review of acquisition numbers and recasting if necessary
 - Fairness Opinions
 - Valuation
 - Advisory
 - Assisting in housekeeping
- **Suggest you be pro active and bring your clients to Investment Bankers for potential capital raising or M&A. You will handle the audit and your other partners can do some of the advisory work.**

CONTACT DETAILS

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FinanceAsia.com

Best Investment Bank
in the Philippines-2006-2010

Best Equity House in the
Philippines-2006, 2007, 2009

Best Bond House in the
Philippines-2007-2010



Best Domestic Investment Bank
in the Philippines-2006-2010

Best Equity House in the
Philippines-2010



ASIAMONEY

Best Debt House in the
Philippines – 2006-2010

Best Equity House in the
Philippines - 2006-2010



Outstanding Local
Underwriter-2006



Best Investment Bank in
the Philippines-2007-2009

Best Bond House in the
Philippines-2007-2009

Best Equity House in
the Philippines-2008



BACKGROUND

- Head of Investment Banking and Securities Subsidiaries of Country's Largest Bank
- Capital Market Development Council of the Philippines (CMDCC) Co-Chair with DOF and SEC
- Investment Houses Association of the Philippines (IHAP) Board Member
- Philippine Stock Exchange (PSE) Trading Nominee
- Management Association of the Phils. (MAP) Governor
- Financial Executives Institute of the Philippines (FINEX) Past President