



Raising Capital in Global Financial Markets

Fall 2013

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What are Capital Markets?

- Capital markets facilitate the issuance and subsequent trade of financial securities.
 - The financial securities are generally stocks and bonds.
 - They are used by companies and governments to *raise* funds and pension funds, hedge funds etc. to *invest* funds.
- Financial regulators (e.g., the SEC in the U.S., CSA or OSC in Canada, SFC in Hong Kong etc.) ensure investors are protected when buying/selling financial securities.
 - Most regulations require disclosure to ensure investors have the information they require when making decisions.

How Important Are Capital Markets?

- Firms need money to implement their business strategies.
 - Any other reasons to require capital?
 - What is important to the firm when raising capital?
 - What are the rights and responsibilities of firms?
Regulators? Governments?
- Recent headlines:
 - “Time for Plan Z: Blackberry is set to go private”
 - “Alibaba to see US IPO after HK talks breakdown”
 - “JP Morgan Eyes \$4bn ‘Pay for Peace’ Deal”

Capital Market Development

- Although firms have raised capital globally for centuries, until the 1980's the majority was debt.
- Some exceptions ...
 - During Roman times, the empire contracted out services to private groups who sold shares traded throughout the empire.
 - The Dutch East India Company was the first multinational and the first to issue stock as we know it in 1602.
- The demand for international equities changed when British institutional investors (among others) were allowed to have more foreign content in their portfolios in the early 1980's.

Why Do Stock Exchanges Develop?

- Using Canada as an example, until the mid-1800s, businesses and governments in Canada primarily accessed capital from European markets.
- By 1852, several Toronto businessmen were periodically meeting to exchange shares, mortgages and other loans.
- In 1861, twenty-four businessmen created the Toronto Stock Exchange.
 - To trade individuals had to be members.
 - Fewer than two dozen companies were listed. Trading was limited to half-hour sessions and only two or three transactions occurred per day.
- In 1878 it was growing so it moved to a permanent location and started to expand its membership.

Why Raise Funds Globally?

- Diversification
 - Smoothes out non-systematic risks.
 - Overcomes differences in valuation (i.e., market saturation, market segmentation).
- Types of diversification
 - Location: Domestic, International
 - Asset classes: Bonds, Commodities, Equities, Real Estate
 - Others: Financial innovation
- Risks / Returns
 - Volatility – from information arrival (or not).
 - Liquidity.

Why Go Global? An Example

Bell Canada Enterprises

- Since 1975 its shares traded in Canada and abroad.
 - It established an international reputation by listing on the NYSE and six European stock exchanges.
- In 1983 it issued new shares on the TSE, NYSE and European exchanges: a "trailblazing new concept". It used three underwriting syndicates (Canada, US and Europe)
- Why do this, it had access to sufficient capital in Canada?
 - It heightened Bell Canada's visibility in Europe as the firm's largest subsidiary, Northern Telecom, was pushing into the British telephone switching market.

Summary: Why Go Global?

- Increased size of potential capital.
- Lower costs due to the potential segmentation across markets and saturation of domestic markets.
- Diversification and management of country risk (and associated economic risks).
- Modify foreign exchange risk.
- Increased global recognition.
- Tax reduction/avoidance.

Financing Strategies: General Rules

Choose the corporate financing strategy that:

1. Minimizes the expected after-tax cost of financing, and
2. Maintains the level of different types of risk within acceptable levels.

These effects may be more difficult to assess in an international setting, but there are also more opportunities. Some of the issues:

- Institutional and regulatory differences
- Tax laws differ across countries
- Political risks, cultural risks, etc.

Global Financing Options

Equity Financing:

- Cross-listing – e.g. an Israeli firm on the NYSE
- Global Depositary Receipts – e.g. ADR's
- Euro-equity market

Debt Financing:

- Foreign bank loans
- Foreign bonds – e.g. Yankee Bonds and GDN's (like ADRs)
- Euromarket bonds – e.g. EuroYen bonds

Derivatives:

- Using futures, options or swaps to change cashflows and thus economic exposure.

Major Global Financial Centres

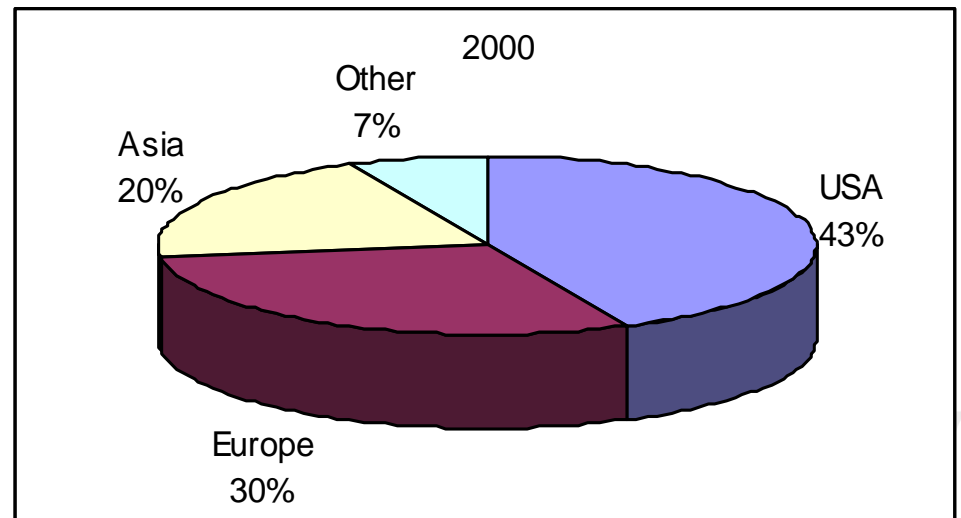
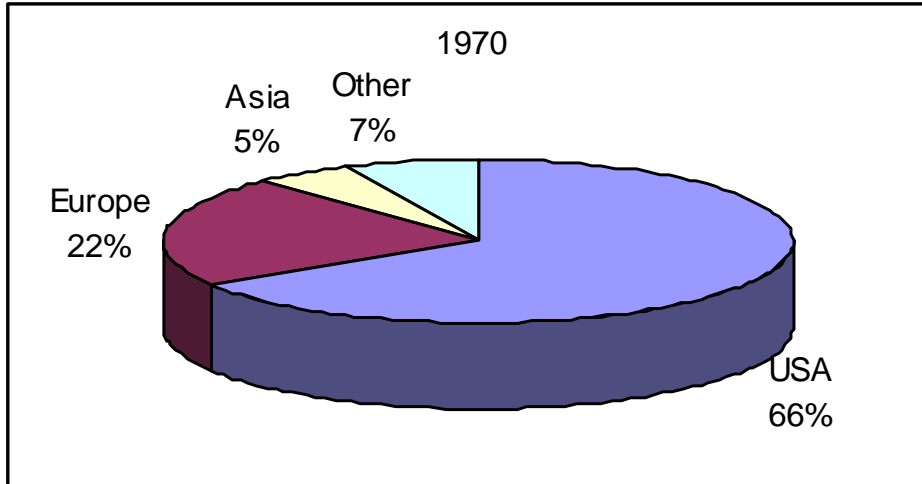
PRIMARY:

**NEW YORK
LONDON
TOKYO**

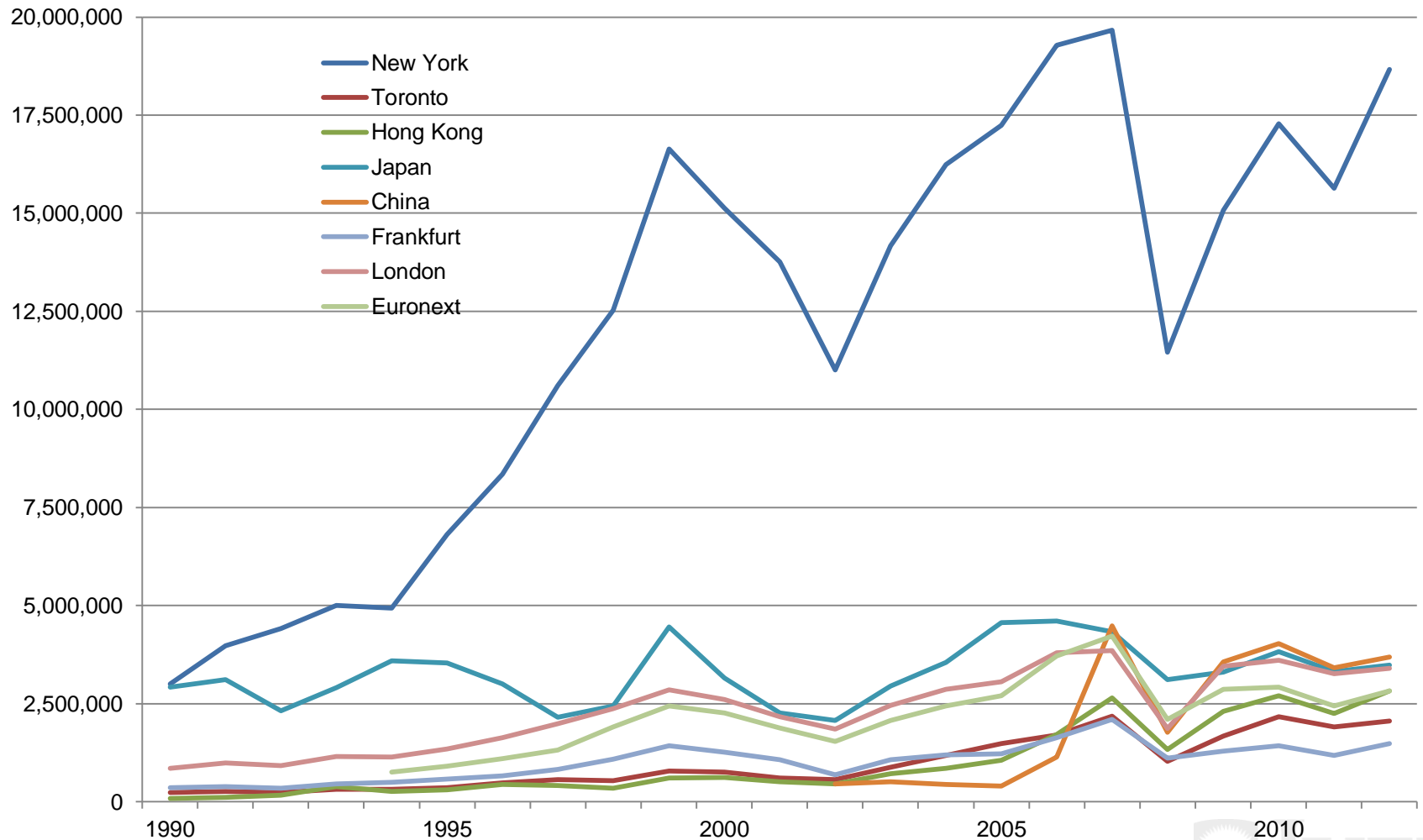
SECONDARY:

**FRANKFURT
ZURICH
LUXEMBURG
HONG KONG
PARIS
SINGAPORE
TORONTO**

World Market Capitalization



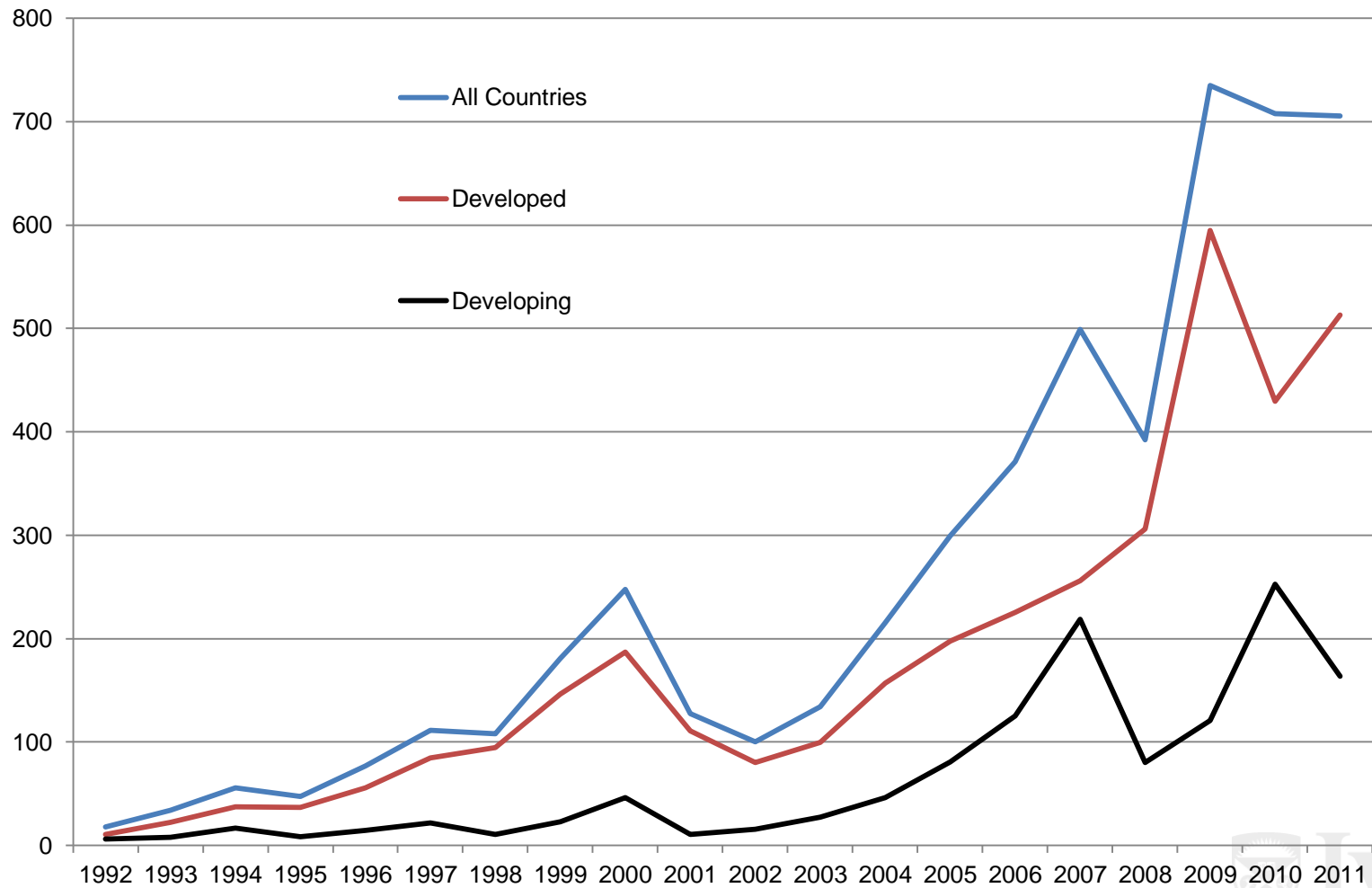
Stock Market Capitalizations 1990-2012



•Source: World Federation of Exchanges

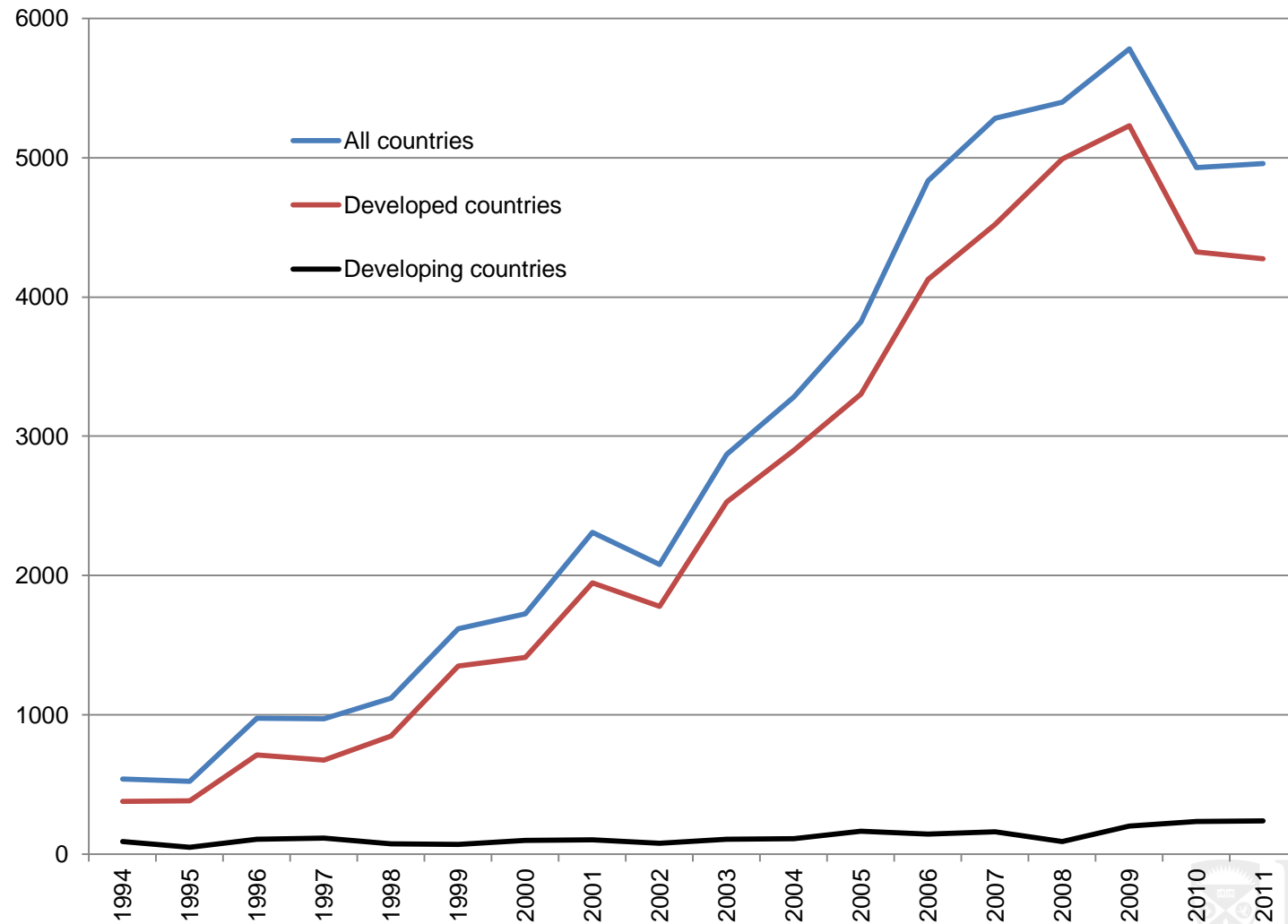


International Equity Issues (billions USD)



Source: Bank for International Settlements

International Debt Issues (billions USD)



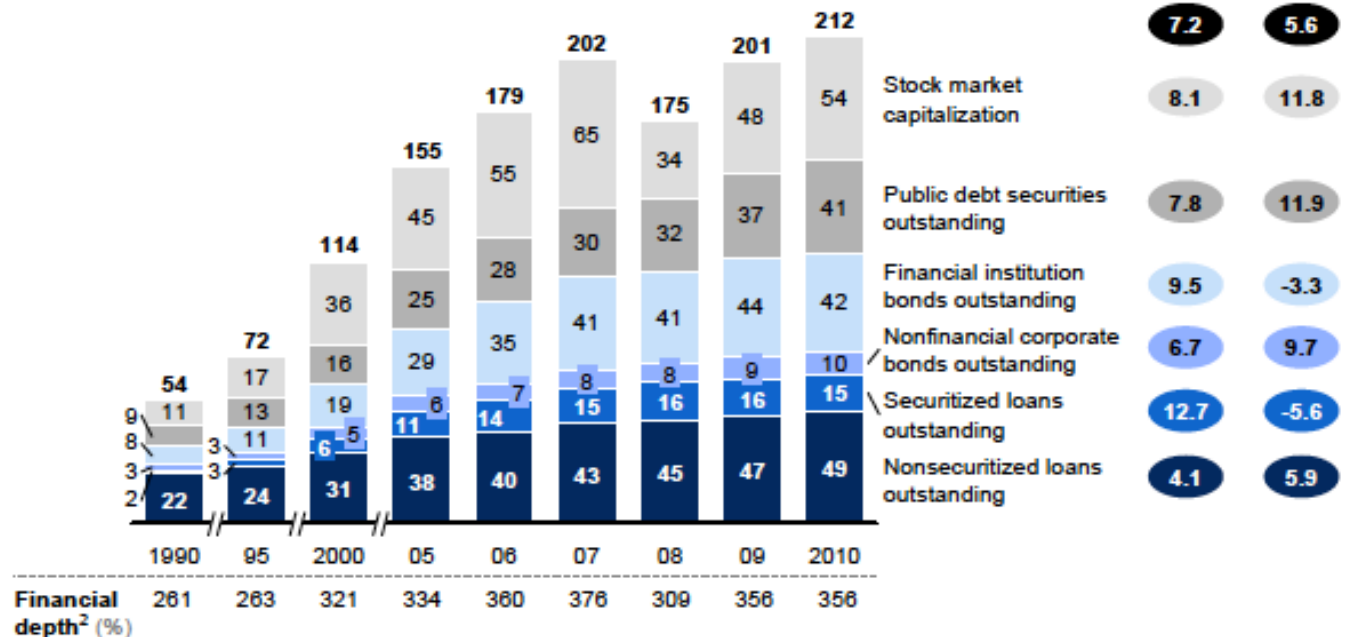
Source: Bank for International Settlements

International Capital Issues (trillions USD)

Global financial stock has surpassed pre-crisis heights, totaling \$212 trillion in 2010

Global stock of debt and equity outstanding¹

\$ trillion, end of period, constant 2010 exchange rates



1 Based on a sample of 79 countries.

2 Calculated as global debt and equity outstanding divided by global GDP.

NOTE: Numbers may not sum due to rounding.

SOURCE: Bank for International Settlements; Dealogic; SIFMA; Standard & Poor's; McKinsey Global Banking Pools; McKinsey Global Institute analysis

International Equity: Cross-listing

To list shares on a foreign exchange companies must:

1. Qualify for listing according to the standards set for overseas companies by the exchanges.
 - For the NYSE foreign firms must have a *pre-tax income* of over \$25M (for domestic firms it is only \$2.5M), and a market value of *publicly held* shares of over \$100M (\$40M for US).
 - Arrange same settlement facilities as domestic issuers.
2. Register with the local securities commission therefore they must conform to local GAAP etc. and pay the necessary fees.
 - Note: Canadian and Israeli companies can list their shares on the US exchanges “like” US companies.

Why Crosslist?

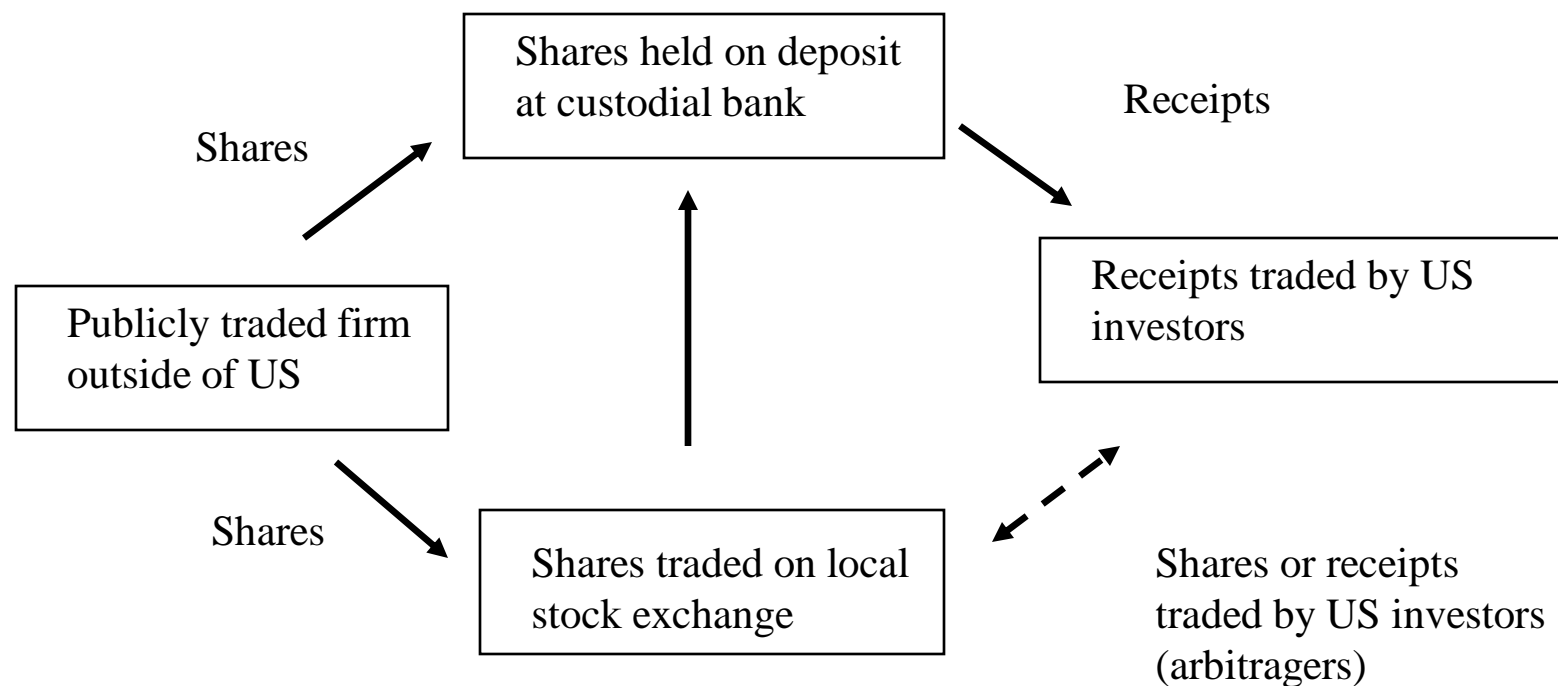
1. Improves the liquidity of your shares.
2. Helps overcome mispricings due to illiquid capital markets, governance concerns or market segmentation.
3. Increases visibility in foreign markets.
4. Establishes a market for shares to perform transactions such as acquisitions in the host market.
5. Establishes a secondary market to compensate management and employees of subsidiaries in the foreign country.

International Equity: Depositary Receipts

An alternative to overseas listings

- DR's are certificates representing ownership of shares
 - They represent ownership of a specific number of underlying shares held in trust at a custodian bank.
- American Depositary Receipts (ADR's) were developed by JP Morgan in 1927 so Americans could invest in the British retailer Selfridge & Co.
- Since it was conceived and initially only used in the US, ADRs are the best known. They allow non-U.S. companies to offer and trade their shares in the U.S.
 - Increasing use of Global Depositary Receipts (GDR's).
 - Indian firms represent the largest number of DRs. There are now also Hong Kong Depositary Receipts, Indian Depositary Receipts, ...

Trading of (American) Depositary Receipts



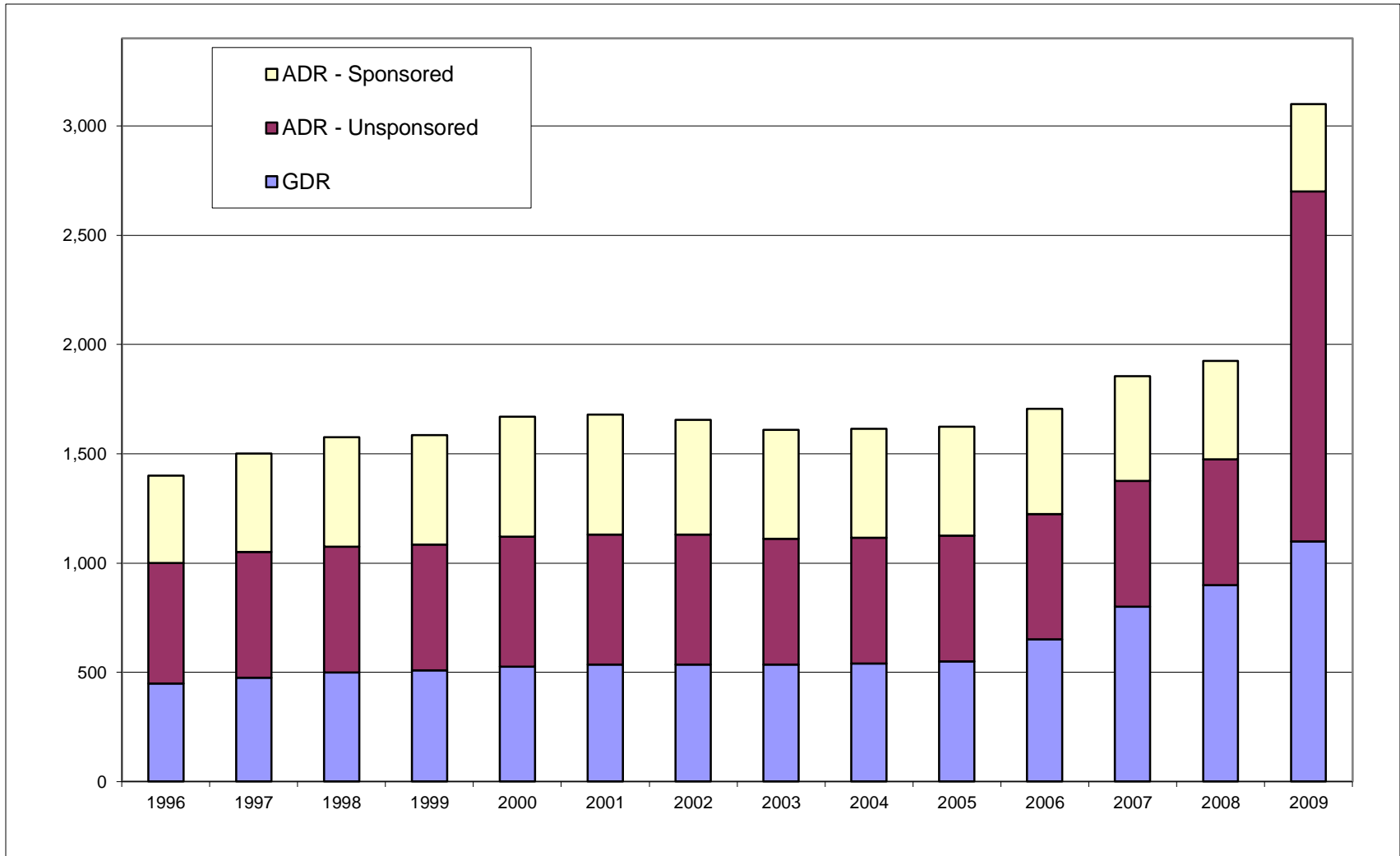
International Equity: ADR (cont'd)

- Depositary banks hold the securities in the country of origin and convert all dividends and other payments into US dollars.
 - US investors bear all of the currency risk and pay fees to the depositary bank for their services.
- Usually pre-existing shares that are just held at the depositary bank and the ADR trades as its “proxy” on the US exchange.
- Advantages:
 - Cost efficiency, trade execution in US, avoids foreign investor exclusion laws, avoids unusual foreign market practices, visibility in the US ...
- Disadvantages:
 - “Information risk” – foreign firms may be less transparent and may have less or no US analyst coverage.
 - Currency risk, political risk.

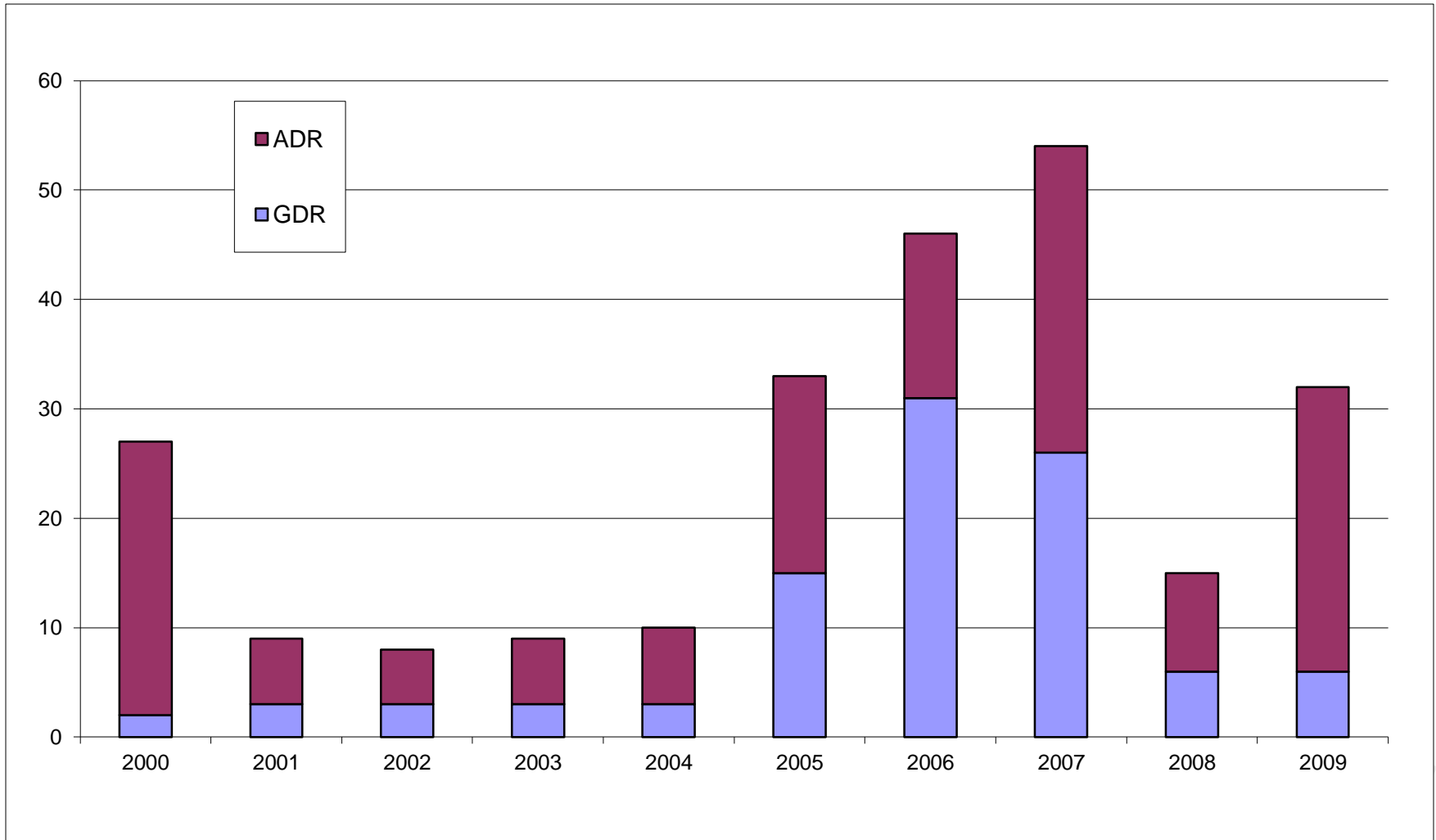
International Equity: ADR (cont'd)

- *Un-sponsored ADR's* – the non-US shares are offered to US investors without the firm's active participation (e.g., Selfridge). Rule amendments in October 2008 renewed interest in setting these up.
- *Sponsored ADR's* – the firm approaches a depositary bank to manage their shares in the U.S. They have to, at least partially, reconcile to US GAAP.
- *Sponsored ADR's* can range from:
 - Level 1: trade OTC with limited disclosure (over 75% in quantity)
 - Level 2 & 3: trade on exchanges. More disclosure required.
 - Rule 144A

Number of DR programs



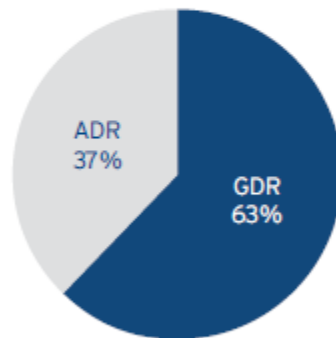
New Capital Raised by DR's (billions of USD)



New Capital Raised by DR's

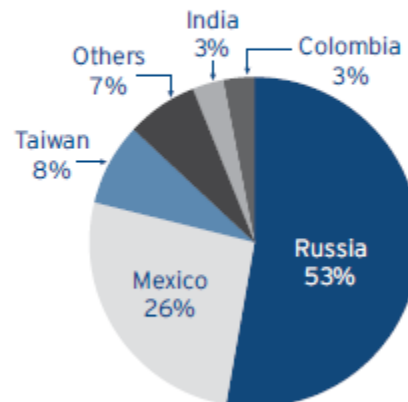
2012 Capital Raising

By Type



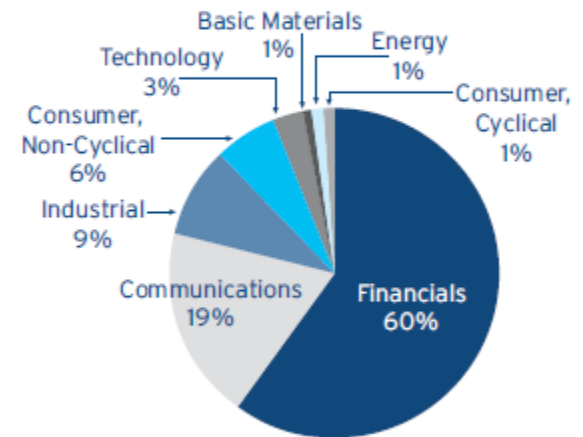
Value: \$12.4 Billion

By Country



Value: \$12.4 Billion

By Industry



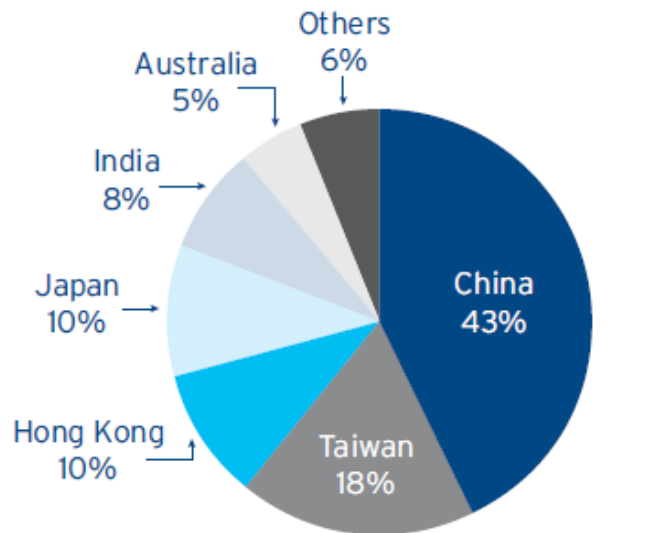
Value: \$12.4 Billion

Source: Bloomberg Financial Markets and Depositary Data Interchange

Source: Citi DR Annual Report 2012

Trading Activity in DR's 2012

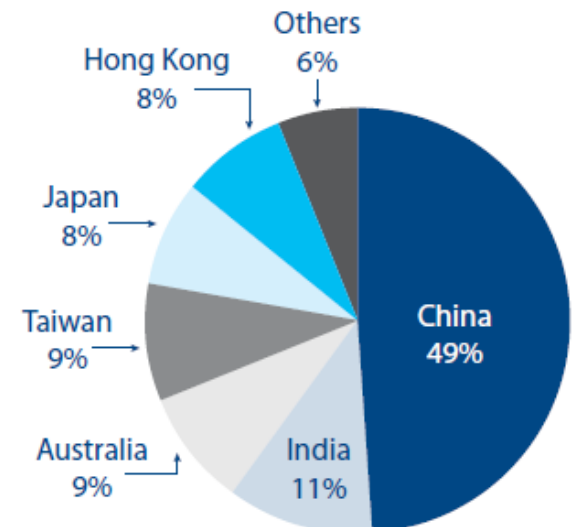
By Country



Trading Volumes: 25.5 Billion DRs

Source: Bloomberg Financial Markets

By Country



Trading Value: \$0.57 Trillion

Source: Bloomberg Financial Markets

Source: Citi DR Annual Report 2012

Example: Indian Depository Receipt

- Standard Chartered plc was the first foreign company to have expressed interest in an IDR issue. The company is already listed in London and Hong Kong.
- Neeraj Swaroop, CEO - South Asia at Standard Chartered Bank, said that the decision to list in India through an Indian depository receipts (IDR) issue, was not about raising capital but rather about sending a message of commitment to India.
- The IDRs opened at the Bombay Stock Exchange and National Stock Exchange on June 11, 2010.

International Equity: Euroequity

- Euro-equity are shares issued outside the firm's home country.
- The shares are distributed to investors by a syndicate of international banks (i.e., not traded on an exchange).
- Usually a portion issued in the home country. The Euro portion is not subject to regulatory approval.
- Because of the domestic component, the issue is still regulated (home market rules).
- Most shares are eventually sold back in the home market after the mandatory holding period ("flowback")



Global Equity Offering

Ordinary Shares

Euro-equity

elf aquitaine

ADR

Société Nationale Elf Aquitaine

Global Offering 8,000,000 Ordinary Shares

2,600,000 Ordinary Shares

This portion of the offering was offered in France by the undersigned.

Banque Nationale de Paris
Banque Indosuez
Caisse des Dépôts et
Consignations
Caisse Nationale de Crédit Agricole
Banque de Neufilze,
Schlumberger, Mallet
Banque du Phenix
Banque pour l'Industrie Française
Banque OBC-Odier Bungener Courvoisier
Banque Stern
L'Européenne de Banque
Crédit Lyonnais
Société Générale
Caisse Centrale des
Banques Populaires
Crédit Commercial de France
Banque Worms
J. P. Morgan et Cie SA
Banque Française du
Commerce Extérieur
Crédit du Nord
Banque Eurofin
Banque Pallas France
Compagnie Financière de CIC et de l'Union Européenne
Sofabanque

1,800,000 Ordinary Shares

*This portion of the offering was offered outside France and the United States
by the undersigned*

Paribas Capital Markets Group
Barclays de Zoete Wedd Limited
Credit Suisse First Boston France S.A.
County NatWest Limited
Deutsche Bank
Aktiengesellschaft
Enskilda Securities
Skandinaviska Enskilda Limited
Lehman Brothers International
Morgan Stanley International
RBC Dominion Securities
international
Swiss Bank Corporation
S.G. Warburg Securities
Banque Indosuez
BNP Capital Markets Limited
ABN AMRO
Daiva Europe Limited
Dresdner Bank
Aktiengesellschaft
Kleinwort Benson Limited
Merrill Lynch International Limited
Nomura International
Salomon Brothers
International Limited
UBS Phillips & Drew Securities Limited
Yamaichi International (Europe) Limited

7,200,000 American Depositary Shares
Representing 3,600,000 Ordinary Shares

This portion of the offering was offered in the United States by the undersigned.

Goldman, Sachs & Co.
Merrill Lynch & Co.
Salomon Brothers Inc.
Alex. Brown & Sons
Incorporated
The First Boston
Corporation
Bear, Stearns & Co. Inc.
Crédit Lyonnais Securities (USA) Inc.
Dillon, Read & Co. Inc.
Donaldson, Lufkin & Jenrette
Securities Corporation
A. G. Edwards & Sons, Inc.
Kemper Securities Group, Inc.
Kidder,
Peabody & Co.
Incorporated
Lazard Frères & Co.
Lehman Brothers
Montgomery
Securities
J. P. Morgan Securities Inc.
Morgan Stanley & Co.
Incorporated
Oppenheimer & Co., Inc.
PaineWebber
Incorporated
Paribas Corporation
Prudential Securities Incorporated
Smith Barney, Harris Upham & Co.
Incorporated
Société Générale
Securities Corporation
S.G. Warburg Securities
Wertheim Schroder & Co.
Incorporated
Dean Witter Reynolds Inc.
Howard, Well, Labouisse, Friedrichs
Incorporated
Advest, Inc.
Arnhold and S. Bleichroeder, Inc.
William Blair & Company
J. C. Bradford & Co.
Piper, Jaffray &
Hopwood
Incorporated
Rauscher Pierce Refanes, Inc.
Sutro & Co. Incorporated
Wheat First Butcher & Singer
Capital Markets
First Southwest Company
Furman Selz
Incorporated
Interstate/Johnson Lane
Corporation
Janney Montgomery Scott Inc.
Johnston,
Lemon & Co.
Incorporated
The Ohio Company

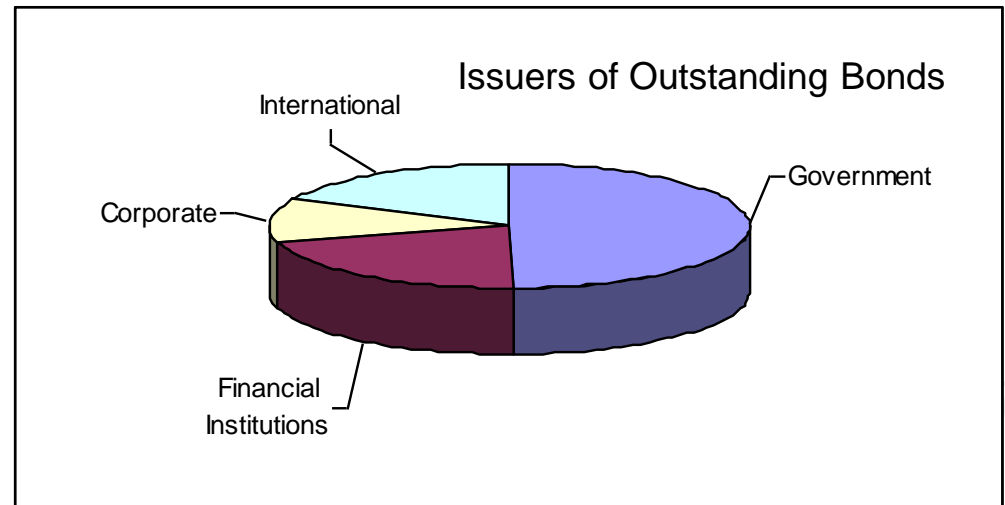
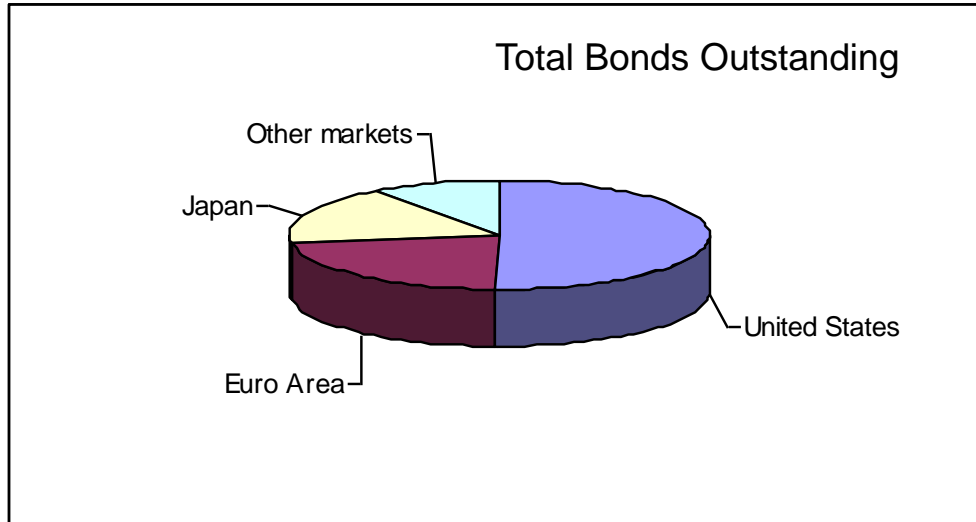
Joint Global Coordinators

Paribas Capital Markets Group
Goldman Sachs International Limited

June, 1991

EY

International Bond Markets



Source: IMF

International Debt: Foreign Bonds

International or foreign bonds are:

1. Issued under the regulations of a specific country,
2. Denominated in the currency of that country, **but**
3. The issuer is a non-resident.

Examples:

- USD obligations of non-US firms that are underwritten and issued in the US are called *Yankee bonds*.
- Yen obligations of non-Japanese firms underwritten and issued in Japan are called *Samurai bonds*.
- British Pound Sterling obligations of non-UK firms that are underwritten and issued in the UK are called *Bulldog bonds*.



Eurobonds and the Euromarket

- Developed after World War II based on the need to hold deposits in foreign currencies, especially U.S. dollars, in different locations (e.g. outside the US).
 - These deposits are free from domestic regulations such as interest rate ceilings, reserve requirements and deposit-insurance requirements since the currency is held outside its home country.
- This market really took off with the floating of exchange rates in the early 1970's.
- Investors can choose from overnight Eurocurrency deposits to 50 year Eurobonds.

Euromarket Tools

- Eurobonds and Euronotes
 - Bonds that are similar to a domestic-bond issue except that they are issued outside the jurisdiction of the country of the currency of the bond.
- Eurocommercial paper
 - Similar to domestic commercial paper (short-term unsecured notes issued by corporations), except that it is only sold outside the jurisdiction of the country of the currency of issue. Issuers are generally large American or European organizations.

Euromarket Attractions

- Large capital base (arguably the largest in the world).
- *May be* lower cost for some firms - fewer registration and disclosure requirements, fewer fees.
- Can issue in different currencies to hedge foreign exchange exposure.
- Fewer restrictions because not issued in a specific market:
 - Foreign bonds listed on a specific market must meet that market's restrictions.
 - Bonds in US need to be rated, not always the case in the Euromarkets. However, this imposes other restrictions.

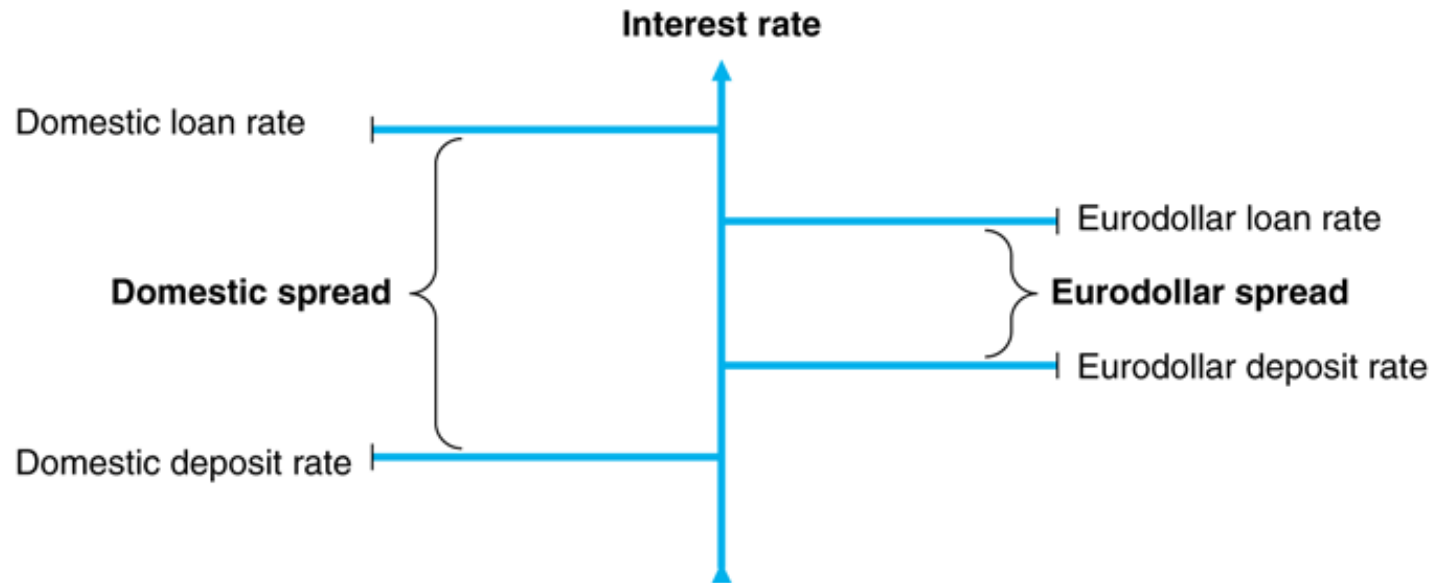
Derivatives

- As global investment has increased, the market has developed tools to increase access to capital and mitigate the associated risks that not all investors and firms want to be exposed to:
 - Interest rate risk
 - Currency and interest rate swaps (credit default swaps?)
 - Foreign Exchange Risk
 - Currency forwards, options and swaps
 - Political risk
 - Political risk insurance

Euromarket: Examples

	US\$	Yen
Domestic	US Bank Deposit US T-Bills and T-Bonds US Corporate Bonds US Regulation	Japanese Bank Deposit Japanese Government Bonds Japanese Corporate Bonds Japanese Regulation
Offshore	Euro-\$ Deposit Euro-\$ Bond (corporate and sovereign) BIS General Guidelines	Euro-Yen Deposit Euro-Yen Bond (corporate and sovereign) BIS General Guidelines

Euronote Spreads vs Domestic Spreads

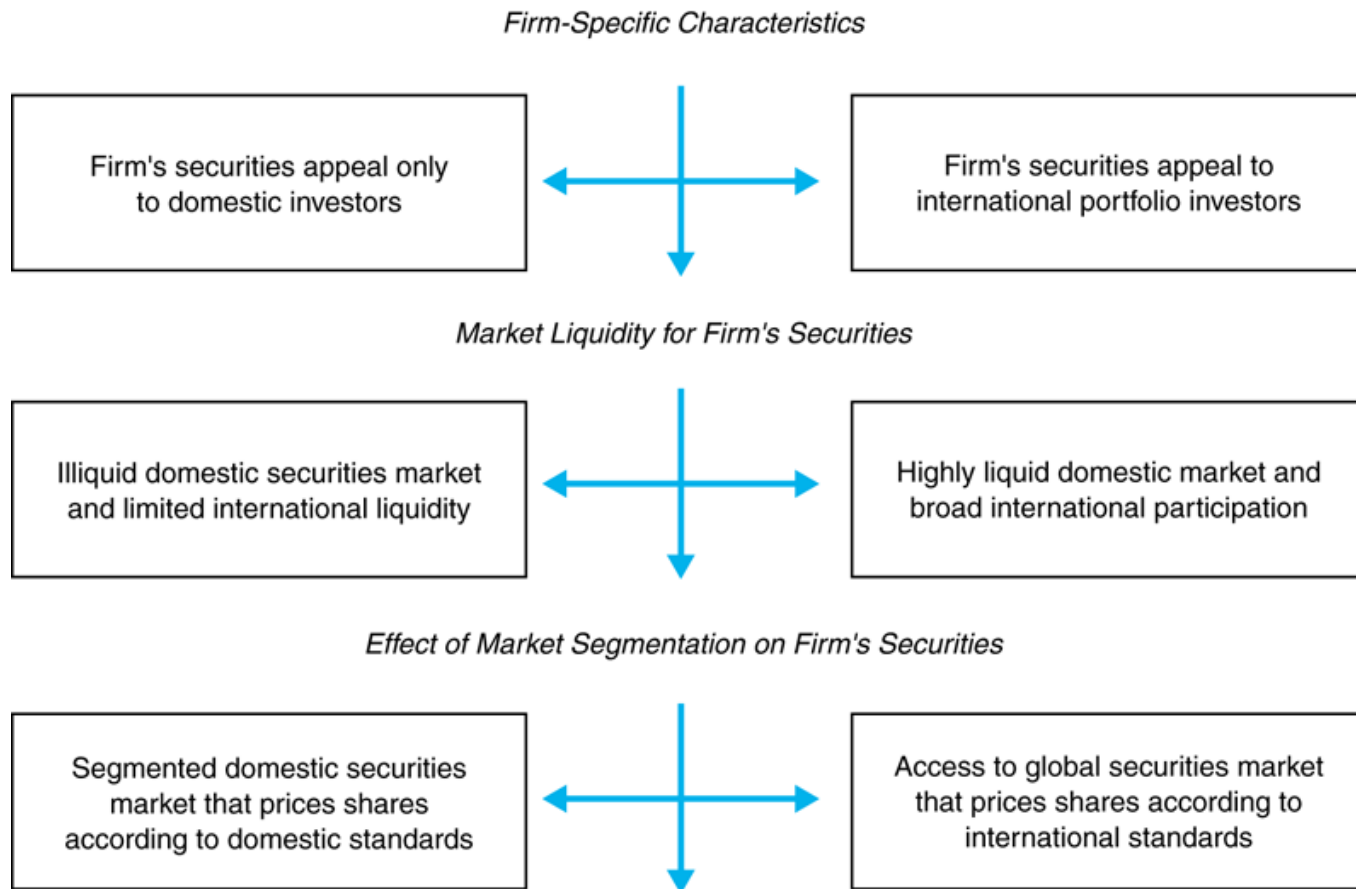


Eurodollar deposit rates are higher and Eurodollar loan rates are lower than their corresponding domestic deposit and loan rates due to the absence of banking restrictions such as reserve requirements and deposit insurance fees, and the wholesale nature of the market.

Occasions Requiring Foreign Capital

- Cross-border ventures
- International joint ventures
- International mergers or acquisitions
- Foreign spin-offs or divestitures

Where to Raise Capital



Other Factors: Country Risk Ratings

Risk Ratings	Indonesia	Finland	Brazil	Russia	Mexico
Currency:					
Unit	rupiah	euro	real	ruble	peso
Arrangement	floating	EMU	floating	managed float	floating
S&P's Rating	CCC+	AA	B+	SD	BB
Moody's Rating	B3	Aaa	B2	B3	B2
Fitch IBCA	B-	AAA	B	CCC	BB
Economist Intelligence Unit:					
Rating	D	B	D	D	C
Score	67	35	62	79	53
Euromoney:					
Rank	88	12	76	161	47
Score	36.4	90.9	41.7	20.9	55.2
Institutional Investor:					
Rank	86	14	65	104	49
Score	27.9	82.2	37.4	20.0	46.0
Trend	Negative	Positive	Negative	Negative	Positive
International Country Risk Guide:					
Political	42.0	90.0	66.0	54.0	69.0
Financial	22.0	39.0	31.5	25.5	31.0
Economic	18.0	45.5	33.0	18.5	35.0
Milken Institute Capital-Access Index:					
Score	37.8		61.65	57.81	61.65
Quantitative	56.6		52.38	71.15	52.38
Risk measures	26.3		29.41	43.59	31.25
Qualitative	0.0		36.36	31.03	34.76
Overseas Private Investment Corporation	Yes	No	Yes	Yes	No

Adapted by authors from the sources listed. All values for March 1999.



Summary

- Global markets offer CFO a wide range of funding opportunities:
 - Usual funding issues:
 - Availability
 - Cost
 - Degree of leverage
 - Interest coverage
 - Control considerations
 - Added considerations:
 - Political risk
 - Choice of currency
 - Hedging requirements
 - Institutional differences