

# ORB LISTING GUIDE



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# ORB Listing Guide

“ORB has proved popular with a wide range of investors, providing easier access to an attractive asset class”

“ORB aims to offer retail investors efficient access to an on-screen secondary market in London-listed debt instruments”

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# Introduction

## London Stock Exchange

### **An overview of the main steps required to list and admit a bond to ORB**

In February 2010, London Stock Exchange launched an electronic, order-driven trading service for UK government, corporate and supranational bonds. The Order book for Retail Bonds (ORB) aims to offer retail investors efficient access to an on-screen secondary market in London-listed debt instruments. This new trading service was introduced in response to demand from private investors in the UK for a cost-effective and transparent mechanism for gaining access to fixed-income securities and to develop the market for retail-denominated bonds in the UK.

For issuers, a listing in London provides the prestige of admission to trading on a globally recognised exchange, alongside the opportunity to offer retail bonds to UK investors in a cost-effective and efficient way. Investors appreciate that a regulated, liquid secondary market will be available post-listing and that price and security information will be easily accessible on the London Stock Exchange website. Admission to ORB offers a high-profile route to market and helps issuers reach a wide investment audience.

This introduction provides an overview of the main steps required to admit a bond on to ORB. More details about the procedures can be found in the following chapters of this guide. Issuers should also note that most of the practical procedures required to issue and list retail bonds will be managed by their appointed advisers, namely the lead managers and the legal counsel.

**“A listing in London provides the prestige of admission to trading on a globally recognised exchange”**

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ORB is made up of three segments to accommodate trading of different types of bonds

Segment code	Product	Sector code	Product	Maximum spread (%)	Maximum volume (EMS)	Quoting
UKGT	ORB gilts	UKG1	Gilts	1.5	40,000	Clean
		UKG2	Gilts	3	40,000	Clean
UKCP	ORB UK corporate and other bonds	UKC1	Corporates	3	25,000	Clean
		UKC2	Corporates	3	25,000	Clean
		UKC3	Corporates	10	25,000	Clean
		UKS1	Supranationals	3	25,000	Clean
		UKD1	Corporates – Dirty price quoting	5	25,000	Dirty
INCP	ORB international corporate and other bonds	INC1	Corporates	3	25,000	Clean
		INC2	Corporates	5	25,000	Clean
		INC3	Corporates	10	25,000	Clean

**The market structure**

ORB is the trading service for retail bonds within London Stock Exchange’s wider Fixed Income Market. As detailed in the table above, it is made up of three different segments to accommodate trading of different types of bonds. Every segment is then broken down in different sectors; where securities are admitted according to various parameters.

**Requirements for admission to ORB**

To ensure that all securities admitted to ORB are suitable for the retail market, there are some key requirements that must be met before admission:

- The bond must be listed in London through the Financial Conduct Authority (FCA) and admitted to the Main Market of London Stock Exchange
- The bond must have a committed market maker willing to provide electronic two-way prices throughout the trading day within the required spread
- The bond must be tradable in units of no larger than £10,000. Bonds on ORB are typically tradable in units of £100 or £1,000
- The bond must meet the minimum disclosure requirements for the retail regime as set out in Annex IV and V of the Prospectus Rules
- In most cases, the bond must be set up for settlement in the CREST settlement system (Euroclear UK & Ireland)

**Listing and admission to the Main Market**

The admission process in the UK is made up of two stages: listing and admission to trading. Admission of companies to the Official List is controlled by the FCA, a division of the Financial Conduct Authority (FCA). The FCA retains responsibility for the approval of prospectuses; however, issuers seeking admission to the Official List will also need to submit listing particulars to the FCA. London Stock Exchange is responsible for admitting securities to trading on the Main Market.

A debt issuer seeking a London listing for its securities must apply for admission to the Official List (a ‘listing’) through the FCA. The listing is also dependent on the securities gaining admission to trading on the Main Market through satisfying the exchange’s Admission and Disclosure Standards.



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## Documentation is due to the Admissions team 10 days before the admission date

The listing process itself can take as little as three days depending on the complexity of the transaction and the completeness of the listing document submitted for approval. Appointing advisers with extensive experience of listing and agreeing the timetable well in advance should help shorten the process. We would also recommend engaging with London Stock Exchange and the FCA as early as possible to ensure the timetable for listing can be accommodated.

Full information on the Listing and Prospectus Rules can be found on the FCA's website: <https://www.fca.org.uk/firms>. Any further guidance required on the Listing or Prospectus Rules must be submitted in writing to the FCA, for further details, see: <https://www.fca.org.uk/markets/primary-markets/knowledge-base>.

For admission to London Stock Exchange's Main Market, the advisers will manage all the various procedures, as detailed below.

The Admissions team requires the following documentation to be submitted at least 10 working days before the admission date:

- An electronic copy of the Base Prospectus and the relevant Pricing Supplement/Final Terms document
- A copy of the relevant Board Minutes relating to the issue
- A copy of the Regulatory Information Service (e.g., RNS) announcement relating to the admission
- A completed Form 1 document, available at: <https://view.officeapps.live.com/op/view.aspx?src=https%3A%2F%2Fdocs.londonstockexchange.com%2Fsites%2Fdefault%2Ffiles%2Fdocuments%2Forb-form.xls&wdOrigin=BROWSELINK>

For admission to the ORB, the Admissions team will also require:

- Confirmation of the market maker who will be supporting the security
- The relevant segment/sector for the security to elect the maximum spread requirement
- An indicative opening price for the security.

As soon as possible in the admission process, it is necessary to arrange for the creation of the relevant trading codes:

- ISIN/SEDOL – ISINs are normally allocated by the country of domicile of the issuer. London Stock Exchange is then responsible for allocating a SEDOL code, which is a unique instrument identifier. Email the Pricing Supplement(s) to [smfnewissues@lseg.com](mailto:smfnewissues@lseg.com) and allow 48 hours for these to be assigned.
- TIDM – a Tradable Instrument Display Mnemonic (TIDM) is the three- or four-character identifier specific to London Stock Exchange. Issuers may request a specific TIDM, which will be issued provided it is not already in use or reserved. Once reserved, these are held for a period of six months. Requests should be made to the Admissions Team by emailing the issuer name and the instrument name, making it clear that it is a TIDM request, to [admissions@lseg.com](mailto:admissions@lseg.com)

**London Stock Exchange encourages issuers interested in admitting bonds to this market to discuss their plans with the Fixed Income team as early in the project as possible. We can be contacted at [bonds@lseg.com](mailto:bonds@lseg.com)**

“The listing process can take as little as three days depending on the complexity of the transaction”

# Welcome to ORB

ORB, the Order book for Retail Bonds from London Stock Exchange, gives companies - from ambitious SMEs to large multinationals - access to the capital they need for growth. As the UK's only regulated retail bond platform, it enables businesses to access additional investors and an entirely new source of funding. With ORB, you can take the direct route to a high profile liquid market - and a wider investment audience.

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To download the latest ORB guide and contact us, visit:

[londonstockexchange.com/orbguide](https://londonstockexchange.com/orbguide)



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“ORB can complement bank finance and provide solutions for the entire spectrum of issuers”

# Raising capital on ORB

## Investec

Ian Dixon, Head of Debt Capital Markets

### Why retail bonds are a good option for corporate funding

As a result of the financial crisis, the UK's banking and lending environment has changed dramatically. Participants need to deal with an evolving landscape, which includes an evolving regulatory environment. This situation encourages banks to reshape balance sheets and change their attitudes towards risk.

As part of a long-term trend, there has been a marked decline in the availability of bank financing to UK businesses – especially small and medium-sized enterprises. One reason for this is the increase in regulation across the financial markets. In contrast, banks continue to be more willing to lend to large corporates, which have access to the greatest diversity of financing opportunities.

The capital markets have not historically been top of the list, but this is changing. Furthermore, the Order book for Retail Bonds (ORB) has, and can continue to, alter this perception. Although traditional short-term bank finance will remain the backbone of most corporates' funding structures, ORB can complement bank finance and provide solutions for the entire spectrum of issuers – from the largest FTSE 100 corporate to private enterprises.

Retail bonds provide a core, strategic, long-term financing tool that gives issuers a greater choice of debt financing from bank facilities and introduces a new investor base.

**“Retail bonds provide a core, strategic, long-term financing tool that gives issuers greater choice”**

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The longest-dated ORB-dedicated issue, in years

## Big names on ORB

Following its establishment in February 2010, large companies dominated ORB. Lloyds TSB, Tesco Personal Finance and National Grid were all household names that tapped the market in its early days, but its evolution has seen increasingly diverse issuers approach the retail bond space, increasing opportunities for investors and fostering the development of the market. Investors relish the diversification of their corporate bond portfolio, while issuers recognise the market's receptiveness to various sectors and industries, as well as the possible relevance for their funding requirements.

The broad range of issuers all have individual reasons for approaching the capital markets. For instance, Tesco Personal Finance wanted to diversify its funding structure, while property companies such as St. Modwen Properties or Workspace Group needed the flexibility an unsecured retail bond could bring to their capital structure. However, the common denominator is the provision of strategic, core, long-term financing at rates not currently offered by banks.

The capital markets and ORB, in particular, offer the opportunity for corporates to issue debt that is markedly longer than that offered by banks. Retail bonds have been issued in tenors of anything between five and a half to 12 years, with the majority between seven - and nine - year maturities. This offers a notable extension over the prevailing terms of bank finance currently available to the average UK company.

	Retail public bonds <sup>1</sup>
Issue size	£25/30 million +
Listing	London Stock Exchange ORB platform
Documentation	Public offering memorandum – retail bond compliant
Minimum denomination	£100/£1,000 (typical £2,000 minimum primary purchase)
Law	UK law
Maturity	Flexible (12 years is the longest ORB-dedicated bond issued)
Ranking	Unsecured/secured
Structure	Bullet
Coupon	Fixed rate, semi-annual pay, index-linked and floating
Ratings	Not necessary, but marketing is assisted with ratings
Marketing process	Up to two weeks
Covenant package	More flexible than bank and private placement covenants
Early redemption	Make-whole provision
Investors	Typically (though not limited to) retail investors. There has also been some participation from institutional investors

<sup>1</sup> None of the information listed in this table is a strict requirement – either from London Stock Exchange or the regulator. However, it does reflect standard market practice.

The capital markets have been around for years, but UK PLC has, all too often, been locked out - with the exception of major players in the FTSE 100. This is where ORB genuinely comes into its own. It offers all the benefits of the wider capital markets (diversification, flexibility and core debt), but also carries wider accessibility for a greater number of issuers.

Perhaps the biggest opportunity offered by the retail bond market is that it supports smaller deal sizes than are typically seen in broader wholesale bond markets. Since its inception, ORB has been exceedingly receptive to small issues. The average bond raised is only slightly larger than £95m and the smallest issue just £25.2m. The wholesale public bond market appears to be uninterested in these types of deals for a number of reasons:

- Small bonds are considered illiquid – wholesale investors want aftermarket liquidity and believe this aim is better satisfied by buying into larger bonds
- Small bonds do not make the indices – demand for a small bond among wholesale market fund managers who track bond indices will be limited if it is not included in an index
- A small-bond market has not been developed, because there was no prior need, as the needs of smaller borrowers have previously been met by the banks

With the ability to raise less than £100m, the retail bond market creates an opportunity for issuers looking to borrow on a smaller scale if they have previously been locked out of the wholesale bond market or, if investment grade, turned to the US dollar private placement market. If not, the options are further narrowed to bank debt or some form of asset finance.

However, small bonds can also make sense for larger borrowers. Although a large borrower may be able to issue a benchmark-size bond, it may not want (or need) to do so. For example, the issuer may want to refinance a bank facility that is not of benchmark size or raise money for an acquisition. Until the wholesale market starts to look at smaller deals (and there is not much sign of this in Europe), midcaps will remain locked out of the market. However, the UK retail bond market is able to handle smaller deals, providing a new financing choice for many corporate borrowers.

It is important to note, the market is not limited to small issues and can also accommodate larger issue sizes. London Stock Exchange Group's 2012 retail bond issue, for example, raised £300m, while the National Grid retail bond issued in 2011 raised £282.5m.

# £95m

**The average bond raised  
since ORB's inception**

FTSE 250 and small to midcap companies have also driven the growth of ORB. The success of private companies such as Bruntwood, A2Dominion and Alpha Plus Holdings not only highlights ORB's attraction for these sectors of the UK economy, but also its effectiveness at satisfying financing requirements. The low size threshold for bond issuance makes ORB a great alternative to banks for small to midcap companies. Despite this, there are regulatory requirements private companies must consider before approaching the retail bond market.

#### **Requirements to list on ORB**

The requirements for listing on ORB are manageable for public companies that have already accessed the capital markets:

- IFRS-compliant, audited annual financial statements
- Unaudited summary semi-annual accounts
- Other possible documents, such as valuation reports, depending on the nature of the transaction

However, private companies need to give serious consideration as to whether they are content with the additional disclosure required by the UK Listing Rules and the market more generally, as well as the additional resources that may be required.

#### **The 'go-to' market**

In its current guise, ORB may be perfectly placed to become the 'go-to' capital market for UK companies, but there is still a disconnection between investors' expectations and reality. In a low interest rate environment, the pre-eminent pursuit of investors is yield. ORB satisfies this demand with its current offering, but investors continue to prefer marquee, blue-chip names, which have slowed since the initial days of ORB. There are seemingly two key reasons for this – pricing and timescale.

Retail bonds, partly because of the nature of issuers, have paid coupons close to 5%, with high-profile examples including London Stock Exchange Group and A2Dominion. At this point, ORB is not compelling to high-quality issuers on a price basis. Investors will need to settle for lower yields to have the opportunity to invest in top-grade corporate debt.

ORB presents great opportunities for strong credits to efficiently tap the capital markets for debt in sizes that would otherwise be considered sub-scale in the wholesale markets. It is up to lead managers, in dialogue with stockbrokers, to develop a successful execution platform that facilitates retail participation in high-quality corporate bonds.

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**“The low size threshold makes ORB a great alternative to banks for small to midcap companies”**

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# 5%

Retail bonds  
have paid  
coupons  
close to 5%

## The marketing process

Aside from the strategic benefits provided by securing long-dated debt, there is the additional publicity and exposure generated as a consequence of the retail bond. The marketing process of all retail bonds has been supported by strong media coverage to draw the public's attention, which has the added benefit of stirring curiosity among the wider business community.

For example, Bruntwood, a regional property company in the north of England, became a focus for investors from across the UK through this process. The broad participation in the company's bond has led to a significant diversification of its investor base and facilitated public investment in an otherwise private company. For larger, better-known companies, the marketing process allows greater interaction with the customer base. Through a retail bond, Tesco Personal Finance was not only able to raise funding, but also get additional publicity for its offering and products.

Moreover, the retail bond issuance process also has synergies with the company's equity story. Investec has noted the strong correlation between improved equity price performance and the launch of a retail bond for the vast majority of bond issuers. This relationship should be of no surprise, given the nature of the retail bond marketing process. The core investor base for ORB transactions is stockbrokers and investment advisers who have historically specialised in equity.

The retail bond roadshow allows issuers to engage with a variety of retail intermediaries and stockbrokers who may not otherwise have been familiar with the credit story. This education process is obviously principally aimed at selling the bond proposal, but also supports the issuer's equity story. A greater understanding of the issuer among investors, therefore, not only has potentially positive implications for the reception of a retail bond, but also follow-on interest in the equity market.

ORB was modelled on Borsa Italiana's MOT, the most successful and liquid electronic bond market in Europe. ORB provides retail investors with a cost-effective, transparent and efficient mechanism for trading bonds.

Market makers provide bid-offers to the ORB platform. The live, two-way, continuous price for securities offered by multiple market makers provides transparency and improved confidence for market traders and participants. It also seeks to create a more accurate historical picture of price action for a bond, facilitating relative value judgements and trading strategies. It enables investors to have a granular approach to building a fixed-income portfolio, rather than relying on a bond fund. The investor can tailor duration, maturity, income and risk to their specific requirements. It also enables the speculative investor to trade ranges and relative value.

### The secondary market

The highly transparent and efficient secondary market provided by ORB also has significant benefits for issuers. The secondary market provides an effective benchmark for repeat issuers, enabling them to see where existing issues are currently trading and price new issues appropriately, in line with those levels.

Returning issuers can develop their own curve and also price subsequent deals at increasingly attractive levels.

For instance, Tesco Personal Finance's debut £125m issue was priced at a coupon of 5.2% for a seven-and-a-half-year maturity in 2011. When the company returned with an additional fixed-rate deal in May 2012, it was able to raise £200m at 5% for eight and a half years.

The Debt Capital Markets team at Investec is proud to have helped ORB grow, advising on issues and assisting many of our clients to access the non-bank market. We are focused on bringing alternative sectors to the retail bond market to help the diversity of bonds currently traded on ORB. We are a firm believer in ensuring the retail bond market remains active and provides a serious alternative to bank debt for UK corporates.

**“Today in the UK we have an ageing population and an increasingly sophisticated investing public that has a desire for more control and choice over its investments. At the same time, we have a universe of very willing borrowers that would benefit from tapping into this vast client base that they wouldn't ordinarily have access to. LSE's ORB provides an elegant solution for the needs of the borrower, the advisor and the investor. We at Investec have supported the ORB from day one and are privileged to be a part of this maturing marketplace.”**

Matt Bennie, Fixed Income Trader, Investec

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**“Returning issuers can develop their own curve and also price subsequent deals at increasingly attractive levels”**

“This guide addresses the legal considerations for a corporate issuer planning on issuing low-denomination bonds”

# The legal and regulatory framework

## Slaughter and May

Charles Harvey-Kelly, Partner

Eric Phillips, Professional Support Lawyer

**A look at the legal requirements for bonds admitted to the ORB platform**

The Order book for Retail Bonds (ORB) is an electronic trading platform for low denomination gilts, corporate bonds and supranational bonds operated by London Stock Exchange. ORB is not a separate market, but a distinct platform within the Main Market. This guide addresses the legal considerations for a corporate issuer planning on issuing low-denomination bonds (for example, securities with denominations of £100 or £1,000), which are normally called retail bonds<sup>1</sup>. Issuers may offer their retail bonds to investors via specialist brokers and those retail investors may subsequently trade them on ORB.

In order to access ORB, issuers are required to comply with the general legal and regulatory requirements that apply to all bonds admitted to the Main Market and also some additional ORB-specific requirements.

### **Admission to ORB**

The Main Market is a regulated market for the purposes of the EU-wide regulatory framework governing primary and secondary securities markets within the EU. This means retail bonds issued on ORB are subject to a high degree of regulatory oversight in the same way as all other securities listed on EU-regulated markets. In order to have bonds admitted to trading on an EU-regulated market, an issuer must first publish a prospectus, containing disclosure relating to the issuer and the bonds. The UK's Financial Conduct Authority (FCA) is the competent authority that approves prospectuses for which the UK is the home member state<sup>2</sup>.

**“ORB is not a separate market, but a distinct platform within the Main Market”**

- <sup>1</sup> The term 'retail bond' is sometimes used to describe all bonds in low denominations, including those low-denomination bonds that are aimed at qualified investors and typically do not need to be admitted to ORB. In this guide, 'retail bond' only describes those low-denomination bonds aimed at true retail investors.
- <sup>2</sup> Under the Prospectus Directive, in certain circumstances an issuer of retail bonds may have its prospectus approved by an overseas competent authority and then 'passport' back into the UK for the purposes of admission to ORB. The majority of prospectuses related to retail bonds admitted to trading on ORB are approved by the Financial Conduct Authority rather than by an overseas competent authority.

In addition to being an EU-regulated market, the Main Market operates exclusively for listed securities. Therefore, all securities admitted to the Main Market must also be admitted to the UK's Official List. The UK's Official List is operated by the Financial Conduct Authority (FCA) and the listing regime requires listed issuers to comply with a further set of rules on governance and investor protection measures specific to the UK. The FCA is generally referred to as the FCA in both its function of approving prospectuses and operating the Official List.

Access to the Main Market is therefore a two-stage process:

- 1.) Admission to listing, in relation to the UK's Official List, managed by the FCA
- 2.) Admission to trading, in relation to the Main Market, managed by London Stock Exchange's Admissions team

The Main Market is governed by:

- EU securities laws, including various directives and regulations
- The UK transposition of those laws, primarily through the Financial Services and Markets Act 2000 (FSMA)
- The FCA's listing rules, prospectus rules and disclosure and transparency rules
- Guidance published by both the European Securities and Markets Authority (ESMA) and by the FCA
- London Stock Exchange's own Admission and Disclosure Standards.

In addition to the above, retail bonds admitted to ORB have to comply with certain other ORB-specific requirements.

All of these laws, regulations and rules impose certain obligations on issuers. These obligations are frequently broken down into those that must be satisfied on initial admission (listing and eligibility requirements) and those that must be satisfied on an ongoing basis (continuing obligations).

#### **The structure of the offer**

There are two main methods of issuing retail bonds. An issuer may choose either to establish a programme for the issuance of debt from time to time (a debt issuance programme) or issue debt on a one-off basis (a standalone issuance). There are advantages and disadvantages to both methods. Typically, a frequent issuer may find a debt issuance programme will be cheaper and allow access to the markets at shorter notice, while an infrequent issuer may instead opt for a standalone issuance. The choice will affect the transaction process and the contents of the prospectus.

#### **Preparing a prospectus for retail bonds**

Under the Prospectus Directive<sup>3</sup>, an issuer is required to publish a prospectus if it is:

- Offering securities to the public within the EU, or
- Seeking the admission of securities to trading on an EU-regulated market.

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**“Retail bonds admitted to ORB have to comply with certain other ORB-specific requirements”**

<sup>3</sup> Directive 2003/71/EC, as amended.

There are certain exemptions to the requirement to publish a prospectus, but typically none of the exemptions will apply in the context of an offer of retail bonds admitted to ORB. The issuer will be obliged to publish a prospectus that complies with the Prospectus Directive and other related regulation and guidance (prospectus regime). The prospectus is required to be published electronically and it may be accessed by a wide selection of investors.

The prospectus is the key document underpinning the entire offer and admission process. It is crucial the issuer and its advisers spend time getting it right, both in relation to its contents and style. A prospectus for retail bonds is highly regulated and extensively reviewed by the FCA to ensure it contains the specific disclosure requirements of the prospectus regime and is drafted in a style appropriate for retail investors.

The issuer is typically required to take responsibility for the contents of the prospectus and, under both common law and FSMA, issuers may be liable to investors who suffer loss as a result of any untrue or misleading statement in the prospectus or any omissions. By ensuring that the prospectus is true, accurate and not misleading, an issuer is able to reduce potential liability.

#### **The contents requirements of a retail prospectus**

The general contents requirements for prospectuses are governed by the Prospectus Directive (PD), while the specific contents requirements are contained within the PD Regulation.<sup>4</sup> As a starting point, issuers need to consider the general duty of disclosure under article 5(1) of the Prospectus Directive:

**“The prospectus shall contain all information which, according to the particular nature of the issuer and of the securities offered to the public or admitted to trading on a regulated market, is necessary to enable investors to make an informed assessment of the assets and liabilities, financial position, profit and losses, and prospects of the issuer and of any guarantor, and of the rights attaching to such securities.”**

Likewise, the issuer also needs to consider the specific content requirements set out in the relevant annexes to the PD Regulation. Prospectuses for retail bonds will always need to include disclosure in relation to annexes IV (registration document for retail debt), V (securities note for retail debt), XXII (disclosure requirements for summaries) and XXX (information concerning consent to use the prospectus). Other annexes may also be relevant depending on the nature of the offer: for example, VI (disclosure related to the guarantor) will be relevant if retail bonds are guaranteed, and annex XX (information that may be included in the final terms) will be relevant in the case of the admission of a programme rather than a standalone.

#### **The summary**

All retail prospectuses are required to include a summary section, setting out certain key information. The contents and form requirements for summaries are prescribed in detail by annex XXII and ESMA guidance, and therefore leave issuers with very little flexibility. In the case of a debt issuance programme, an issuer is also required to prepare a summary for each individual issue to be annexed to the final terms for that issue. For certain cross-border retail offers, the summary may need to be translated into local languages.

<sup>4</sup> Regulation 809/2004/EC, as amended.

### The final terms

A prospectus for a debt issuance programme (a base prospectus) is required to include a 'pro forma final terms', in which disclosure related to the commercial features of any bonds to be issued under the programme - such as interest rate, denominations and size of the detail - is left in blank for completion at the time of the individual issue. The contents of the final terms and the way that the final terms interact with the underlying terms and conditions within the base prospectus are extensively regulated under the prospectus regime, particularly by annex XX. The final terms for an individual issuance, once signed, are required to be filed with the FCA and London Stock Exchange and then published.

### The consent legend

Under a new consent regime that took effect from July 2012, a financial intermediary (also referred to as an authorised distributor) is able to use the issuer's prospectus to make offers to retail investors if the issuer has consented to this in writing. The PD Regulation envisages two alternative methods for this consent to be given and disclosed within the prospectus:

- 1.) Specific consent, in which the names of the financial intermediaries to whom consent is given are specified within the prospectus or the relevant final terms

- 2.) General consent, in which the consent is granted to all financial intermediaries within a specified jurisdiction or jurisdictions that meet certain clear and objective conditions

There are advantages and disadvantages to both methods, though the general consent method is more commonly used. The specific consent regime allows the issuers and managers greater control over the distribution of the prospectus and gives the issuer a clear contractual relationship with the financial intermediaries, while the general consent regime has greater flexibility and potentially allows the issuer to access a wider pool of investors and therefore obtain a better price.

There are challenges inherent in documenting both methods: with the specific consent method, there are sensitivities with the inclusion of specified named distributors in public documents and the need to keep these lists updated. With the general consent method, it is difficult to ensure that the financial intermediary is bound by distribution conditions. It is prudent for the issuer to consider (with its advisers) the appropriate distribution method and how it will be documented at an early stage in the transaction.

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**“It is currently market standard for retail bond prospectuses to include certain risk factors that are not seen in other conventional bonds”**

### The requirements of the markets

In addition to being regulated by law, the contents of prospectuses are subject to market expectations, the requirements of investors and the recommendations of industry bodies. When issuers come to prepare their prospectuses, they generally consider the prospectuses of similar issuers or securities to ensure their disclosure is consistent with market expectations. It is currently market standard for retail bond prospectuses to include certain risk factors that are not seen in other conventional bonds – for example, a risk factor highlighting that retail bonds (unlike a bank deposit) are not protected by the Financial Services Compensation Scheme. It is also standard for retail bond prospectuses to include disclosure relating to the fact that the bond holders hold interests in the bonds via the issuance of dematerialised depository interests held, settled and transferred through CREST<sup>5</sup>.

### The style requirements of a retail prospectus

The style requirements of prospectuses are also governed by the Prospectus Directive and, in particular, article 5(1)<sup>6</sup>, which states in relation to the contents:

**“This information shall be presented in an easily analysable and comprehensible form.”**

The view of the FCA<sup>7</sup> is that retail bond prospectuses should look significantly different from prospectuses aimed at professional investors, because the level of knowledge and sophistication of a retail bond investor may be very different from that of a wholesale investor. The FCA has published guidance setting out certain considerations for an issuer of retail bonds in order to ensure its prospectus is “easily analysable and comprehensible” to a retail investor.

There have also been a number of discussions among market participants related to this issue and a market practice has been established. In particular, a retail bond issuer should consider:

- Language of drafting: retail prospectuses should not “place excessive reliance on the use of defined terms, technical language or market jargon”. Where such language is used, it will have to be clearly explained. This requirement for appropriate non-legal language drafting does not apply to the terms and conditions of the securities, for which the drafting style may remain unchanged
- Sign-posting and FAQs: the FCA has suggested a number of navigational tools, not typically used in prospectuses for retail debt securities in the past, to guide a retail investor through the prospectus. These include clear instructions for investors, setting out which sections of a prospectus apply to a particular security or a ‘frequently asked questions’ section
- Structural features of the retail bonds: issuers are required to describe, either using a clear narrative or a diagram with accompanying text, certain structural features related to the retail bonds, such as any security arrangements, consequences of default and structural subordination.

Issuers should also consider the nature of the securities and the prospectus as a whole, as well as the expectations of the market, when drafting prospectuses for retail investors.

<sup>5</sup> The securities settlement system for Jersey, Guernsey, Ireland, the Isle of Man, UK equities and UK gilts.

<sup>6</sup> All details relating to regulation were correct at the time of writing.

<sup>7</sup> In October 2013, the FCA launched a consultation regarding the style requirements for retail bonds, in which it set out its proposed new policy for ensuring retail bond prospectuses are drafted in a style appropriate for retail investors.

**The transaction process**

The parties, documentation and timetable for a retail bond will, in many respects, be the same as the transaction process for any other conventional bond, though there are also some important differences.

**Parties to a retail bond issue**

As with any other conventional bond issue, the main parties to a retail bond issue include:

- The lead manager who arranges the transaction and manages the transaction process (in the case of a debt issuance programme, this role will be performed by the arranger)
- Other managers who subscribe for and underwrite the issue (in the case of a debt issuance programme, the managers will typically be dealers on the programme)
- The fiscal agent or trustee, depending on whether a fiscal agency structure is chosen or a trustee structure is chosen. The fiscal agent is an agent of the issuer who is responsible for paying interest to the bond holders and performing certain other administrative functions, while the trustee represents the interests of the bond holders and owes them a fiduciary duty. If a trustee structure is chosen, there will typically be a separate paying agent appointed to make payments

- Auditors who review the financial disclosure in the prospectus and provide separate comfort to the managers in relation to the time between prospectus publication and the date of the issue
- Legal advisers who draft the prospectus and other documentation and liaise with the FCA and London Stock Exchange. Overseas legal advisors may also be required for cross-border offers.

In the case of a retail bond, there will also be:

- Authorised distributors who have been approved by the issuer to act as financial intermediaries between the issuers and managers on the one hand and retail investors on the other. Authorised distributors distribute the prospectus and the information booklet and are regulated for such purposes by the FCA. This requires them to comply with certain business standards; for example, 'know your customer' obligations
- A market maker who provides electronic two-way prices throughout the trading day, supporting the trading of the retail bonds on an ongoing basis.

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“In the case of a retail bond, there will also be authorised distributors and a market maker”

**Retail bond documentation**

As with any conventional bond issue, the main documentation for a retail bond includes:

- The prospectus, which is the key document underpinning the transaction; disclosing information relating to the issuer and the retail bonds. In the case of a debt issuance programme, this document will be called a base prospectus and there will also be final terms setting out the commercial provisions of each individual issuance.
- The subscription agreement that governs the relationship between the issuer and the managers, obliging the issuer to issue the retail bonds and the managers to subscribe for them. In the case of a debt issuance programme, this relationship will typically be underpinned by the dealership agreement, which will include, as a schedule, a short-form pro forma subscription agreement to be signed at the time of each individual issuance under the programme.
- The trust deed (if a trustee structure is used) creates the trust relationship between the trustee and the bond holders, whereas the fiscal agency agreement and the deed of covenant (if a fiscal agency structure is used) provide the obligations of the fiscal agent and give the bond holders direct rights against the issuer.
- The bonds, usually issued in global form, attaching the terms and conditions.
- Auditors' comfort letters, which are typically conditions precedent to the transaction going ahead, addressed to the managers and containing comfort in relation to the issuer's financial condition.
- Legal opinions, which are also typically conditions precedent to the transaction going ahead and addressed to the managers, containing comfort that the issuer has the capacity and authority to enter the transaction and that the obligations of the issuer under the transaction documents are legal, valid, binding and enforceable.
- Admission to listing and trading forms and checklists, which are administrative documents required by the FCA and London Stock Exchange in order to process the applications for admission to listing and trading. These include checklists as to the contents of the prospectus, application forms for both listing and trading, contact details of the issuer, document publication forms, details of payment of fees and so forth.

In the case of retail bonds, additional documentation is required to reflect the appointment and role of authorised distributors. Separately, a market practice has built up in which a range of documentation complementing the prospectus to market the bonds to retail investors is produced, as follows:

- The distribution agreement and various sub-distribution agreements that govern the relationship between the issuer, the managers and the authorised distributors and contain a number of conditions regulating the conduct of the authorised distributors
- An information booklet provided to the retail investors by the authorised distributors setting out certain summarised information in relation to the issuer and the retail bonds. The information booklet does not go through a regulatory approval process and is not intended to be used as the basis for an investment decision. It should, therefore, be heavily scrutinised by the managers, financial intermediaries and the legal advisers to ensure that it complies with all regulatory requirements and is not inconsistent with the prospectus. It should also contain a number of prominent disclaimers relating to its regulatory status. The information booklet is a financial promotion for the purposes of the UK’s financial promotion regime, which means that it must be approved by an “authorised person” regulated by the FCA and be “fair, clear and not misleading” and generally in compliance with the FCA’s Conduct of Business Rules. The information booklet is also an advertisement for the purposes of the prospectus regime and, as such, is required to be consistent with the information contained in the prospectus and not be inaccurate or misleading and inform investors where the prospectus is published. The information booklet should warn investors that it is not in itself an offer and that any investment decision should be made on the basis of the information in the prospectus
- A dedicated webpage containing links to the prospectus and the information booklet and the contact details of certain authorised distributors. Prior to accessing this webpage, investors will be directed to a landing page requiring them to accept a disclaimer relating to their jurisdiction, their acknowledgement of risks related to any investment and so forth
- An advertisement in a national newspaper with certain brief information relating to the retail bond and directing investors to the webpage. This advertisement will also need to contain appropriate disclaimers and legends, and will constitute a financial promotion

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**“The issuer should consider the more extensive and detailed review of the prospectus carried out by the FCA”**

**Retail bond timetable**

Typically, the time from initial mandate to transaction closing for a conventional standalone bond may be in the region of six to eight weeks and it may take up to three months to establish a debt issuance programme. In order to stay current once it is established, it must be updated each year, taking up to two months. An individual issuance under a programme may be completed in approximately two weeks.

When planning a retail bond, an issuer should ensure the timetable can accommodate the additional requirements for a retail bond. In particular, the issuer should consider the more extensive and detailed review of the prospectus carried out by the FCA and the marketing process to retail investors – for example, planning for roadshows.

The FCA currently commits to four working days to review the first submission of a bond prospectus and two clear working days to review each subsequent submission. The FCA has indicated it intends to lengthen these timescales to five and three days respectively in the case of a prospectus for retail bonds.

An issuer that already has securities admitted to the Official List must submit documents related to the approval of the prospectus to the FCA 10 clear working days before the intended approval date of the prospectus. This timescale is extended to 20 clear working days in relation to a new issuer. (In practice, the FCA does not always strictly apply this rule.) Once the prospectus has been approved, the FCA requires documents related to the listing to be submitted 48 hours before it considers the application.

Under London Stock Exchange's Admission and Disclosure Standards, the issuer must contact London Stock Exchange no later than 10 business

days before the application for admission to trading may be considered. The issuer must also send London Stock Exchange the completed Form 1 (containing information related to the securities), the prospectus and any final terms, alongside the regulatory announcement related to the issue and other supporting documentation, at least two business days prior to the day on which the application will be considered. In the case of an admission to ORB, the issuer will also need to complete ORB Static Data Form, which collates the necessary reference data required by London Stock Exchange's Admissions team so that the bond can be set up for trading on ORB.

**Eligibility requirements for admission to listing and trading**

In order to be admitted to listing, a retail debt issuer is required to comply with the eligibility requirements contained within the FCA's Listing Rules, including in particular:

- Incorporation: the issuer must be duly incorporated according to the relevant laws of its place of incorporation or establishment and operating in conformity with its constitution
- Validity: the securities must conform with the law of the issuer's place of incorporation, be duly authorised according to the requirements of the issuer's constitution and the issuer must have any necessary consents
- Transferability: the securities must be freely transferable
- Market capitalisation: the expected market value of the securities to be listed must be at least £200,000
- Whole class to be listed: the application must relate to all securities in the same class.

There are also some eligibility requirements for admission to trading set out within London Stock Exchange's Admission and Disclosure Standards. Some of these duplicate eligibility requirements for listing, while others are distinct. In particular, London Stock Exchange requires that the retail bonds must be capable of being traded in a fair, orderly and efficient manner. It may refuse an application if it considers that admission may be detrimental to orderly markets.

In addition to the requirements for all bonds admitted to trading on London Stock Exchange, there are some technical requirements for eligibility for ORB, including that the retail bonds can be settled via CREST, are supported by a market maker and are issued in small denominations – the minimum denomination should be no more than £10,000.

#### **Continuing obligations**

Once the retail bond has been admitted to listing and trading, the issuer must comply with continuing obligations in order to maintain the admissions. These are set out in the FCA's Listing Rules and Disclosure and Transparency Rules and London Stock Exchange's Admission and Disclosure Standards, including:

- Annual and half-yearly financial reports: the issuer must publish its audited annual financial report (at the latest four months after the end of the financial

year) and half-yearly financial report (at the latest two months after the end of the relevant financial period). The annual financial statements will have to be audited in compliance with IFRS or national accounting standards.

- Equality of treatment: the issuer must ensure all holders of debt securities ranking *pari passu* are given equal treatment in respect of all the rights attaching to those debt securities.
- Communications with bond holders: the issuer is required to make certain bond holder communications in certain situations, including changes to trust deeds, early redemptions of the bonds, changes to other rights attaching to the securities. The issuer is also required to notify the FCA and London Stock Exchange in relation to amendments to its constitution.
- Control of inside information: the way in which an issuer is required to control and disclose non-public information that may be price sensitive is extensively controlled.

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“Once the retail bond has been admitted, the issuer must comply with continuing obligations”

**Retail debt prospectuses: overview of contents requirements**

This table sets out an overview of some of the specific contents requirements for retail debt prospectuses required by the annexes to the PD Regulation.

Annex IV	Disclosure requirements for the registration document
1	Identity of those responsible for the prospectus and responsibility statement
2	Details about issuer's statutory auditors
3	Selected historical financial information, providing key figures that summarise the financial condition of the issuer
4	Prominent disclosure of risk factors that may affect the issuer's ability to fulfil its obligations under the securities to investors
5.1	History and development of the issuer, including: <ul style="list-style-type: none"> <li data-bbox="483 994 628 1016">– legal name</li> <li data-bbox="483 1028 900 1050">– legal form and country of incorporation</li> <li data-bbox="483 1061 975 1084">– recent events material to the issuer's solvency.</li> </ul>
5.2	Principal investments, including future investments and sources of funds
6	Business overview, including: <ul style="list-style-type: none"> <li data-bbox="483 1173 1018 1196">– principal activities and any significant new activities</li> <li data-bbox="483 1207 692 1229">– principal markets.</li> </ul>
7	Organisational structure, description of the issuer's position within the group
8	Trend information, including: <ul style="list-style-type: none"> <li data-bbox="483 1330 1449 1397">– description of any material adverse change in the issuer's prospects since last audited financial statements, or a negative statement</li> <li data-bbox="483 1408 1422 1464">– known trends likely to have a material effect on the issuer's prospects for at least the current financial year.</li> </ul>
9	Profit forecasts or estimates (if any), including: <ul style="list-style-type: none"> <li data-bbox="483 1509 1150 1532">– principal assumptions on which the forecast or estimate is based</li> <li data-bbox="483 1543 948 1565">– report by accountants on the profit forecast.</li> </ul>
10	Administrative, management and supervisory bodies, including: <ul style="list-style-type: none"> <li data-bbox="483 1621 724 1644">– names and functions</li> <li data-bbox="483 1655 1035 1677">– potential conflicts of interest or a negative statement.</li> </ul>
11	Board practices, including: <ul style="list-style-type: none"> <li data-bbox="483 1733 772 1756">– details of audit committee</li> <li data-bbox="483 1767 1227 1789">– extent to which issuer complies with local corporate governance regime.</li> </ul>
12	Major shareholders and nature of control
13	Financial information concerning the issuer's assets and liabilities, financial position and profits and losses, including: <ul style="list-style-type: none"> <li data-bbox="483 1912 1299 1935">– audited consolidated IFRS (or equivalent) accounts not more than 18 months old</li> <li data-bbox="483 1946 684 1968">– audit information</li> <li data-bbox="483 1980 911 2002">– interim financial information, if published</li> <li data-bbox="483 2024 1426 2092">– information on legal and arbitration proceedings that may have significant effects on financial position or profitability or a negative statement</li> <li data-bbox="483 2103 1426 2125">– significant change in financial or trading position since financial information or negative statement.</li> </ul>

<b>Annex IV</b>	<b>Disclosure requirements for the registration document</b>
14	Details of share capital and objects
15	Description of group contracts that are not ordinary course and could be material to the issuer's obligations under the debt securities
16	Experts' reports, if any
17	Details of documents on display, including articles, documents referred to in the prospectus and financial information

<b>Annex V</b>	<b>Disclosure requirements for the securities note (omitting information already covered by Annex IV)</b>
2	Prominent disclosure of risk factors material to the securities
3.1	Interest of natural and legal persons in the issuer, including conflicting interests
3.2	Reasons for the offer and use of proceeds, including estimated total expenses for the offer
4	Information concerning the securities, including: <ul style="list-style-type: none"> <li>- type, class and ISIN</li> <li>- legal form</li> <li>- currency</li> <li>- ranking and subordination</li> <li>- interest provisions and indication of yield.</li> </ul>
5	Terms and conditions of the offer, including: <ul style="list-style-type: none"> <li>- amount</li> <li>- time period during which offer will remain open</li> <li>- distribution arrangements</li> <li>- pricing arrangements</li> <li>- underwriting arrangements.</li> </ul>
6	Admission to trading and dealing arrangements
7	Additional information, including: <ul style="list-style-type: none"> <li>- capacity of advisers</li> <li>- credit ratings or the issuer or the securities.</li> </ul>

<b>Annex XXX</b>	<b>Information regarding consent to use the prospectus</b>
1	Information regarding consent by the issuer, including: <ul style="list-style-type: none"> <li>- express consent and responsibility for the content of prospectus with respect to placement of securities</li> <li>- period for which consent is given</li> <li>- member states in which consent is given</li> <li>- clear and objective conditions attached to the consent.</li> </ul>
2A	Additional information where consent is given to one or more specified financial intermediaries, including: <ul style="list-style-type: none"> <li>- name and address of financial intermediaries</li> <li>- where new information with respect to the financial intermediaries can be found.</li> </ul>
2B	Additional information where consent is given to all financial intermediaries: <ul style="list-style-type: none"> <li>- notice informing investors that the financial intermediaries using the prospectus have to state on their website that they are using the prospectus in accordance with the consent conditions.</li> </ul>

“Efficient execution,  
marketing and  
book-building are  
the responsibility of  
the lead managers”

# Timetables and the role of lead managers

## Numis Securities

Michael Dyson, Managing Director, Head of Fixed Income Products

### How the lead manager shepherds a retail bond from pitch to final settlement

A successful retail bond issue offers many benefits for the borrower. In addition to raising new capital at competitive rates, with sensible covenants that work for issuer and investor, the deal is likely to be sized at an amount that exactly suits current needs.

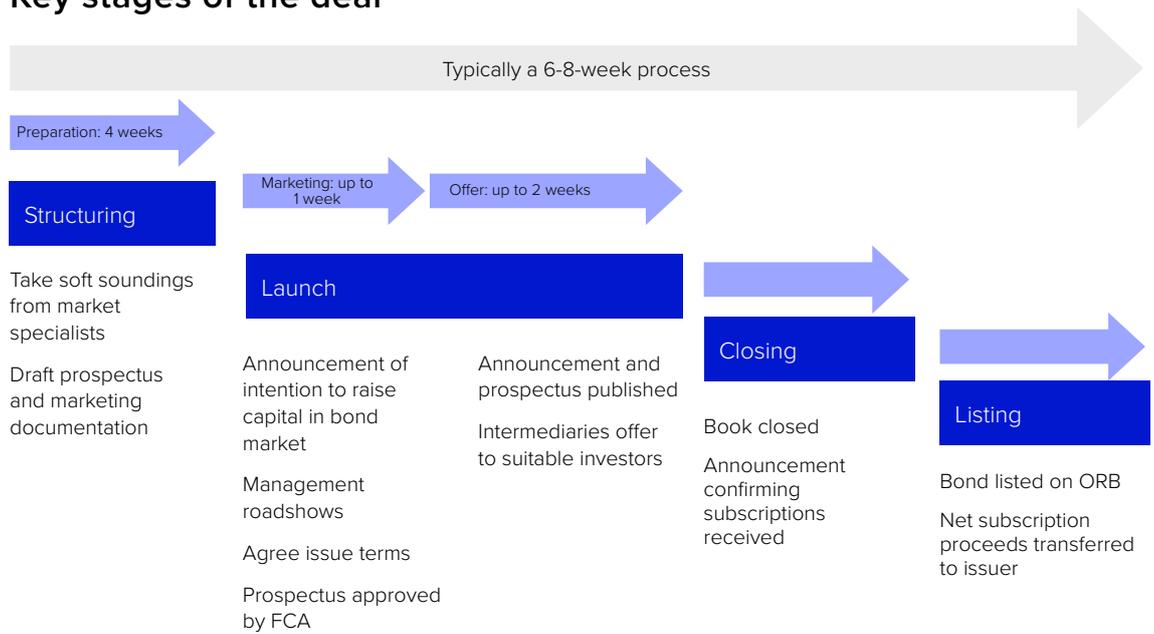
Furthermore, by engaging with investors and the specialist media throughout the process, most issuers benefit from positive coverage and expanded profiles. This new investor base of bond holders may also choose to become shareholders in the company. Many issuers report that publicity can also bring new business opportunities. A strong lead manager will coordinate each angle of this multi-faceted process.

#### From pitch to final settlement

The public announcement of a retail bond is the culmination of several weeks' work. Efficient execution, marketing and book-building are the responsibility of the lead manager(s). He or she will guide the issuer through the various stages – from initial feasibility discussions through to the legal, listing, regulatory and marketing phases. The goal is to minimise the drain on management time and execute the deal to best all-round effect. The ideal bond is one in which both issuer and investor are pleased with the result.

**“The ideal bond is one in which both issuer and investor are pleased with the result”**

## Key stages of the deal



“The public announcement of a retail bond is the culmination of several weeks’ work”

## 6 to 8

The number of weeks it typically takes to go from structuring to listing

### Selecting the lead manager and beginning the process

Most borrowers have several options that include wholesale/high-yield bonds, retail bonds, bank finance, private placement and (possibly) equity or equity-linked offerings such as convertibles.

During the first meeting, the parties discuss the merits and suitability of each option. The lead will demonstrate a proven track record of execution and a strong presence in the target market through primary and secondary distribution and trading.

As with any capital-raising exercise, there are several parties involved. The lead manager works with the issuer to select issuer counsel, lead manager counsel and PR. The kick-off meeting is also an opportunity for all the key parties to introduce themselves and produce a roadmap of the route for final admission to London Stock Exchange's market and settlement of the transaction.

### Finding the right structure

The borrower will have chosen the retail bond product for a number of combined benefits, such as:

- Enhanced public and business profile
- A broader investor base
- Constructive covenants
- Rating requirements (or possibly no rating requirement)
- Size
- Maturity
- coupon.

The first step is to choose the issue type from the following categories:

- A holding company that buys and owns shares in other companies
- An operating company system in which a subsidiary company owns the revenue-generating entities and then leases these back to the parent company
- A special purpose vehicle (SPV) in which a separate legal entity is created specifically for the transfer of assets, protecting a company from financial risks

For a listed company, it is often simplest to launch out of the holding company. While many of the assets, work streams and cash flows may sit in the subsidiaries, issuing a bond out of the same entity from which ordinary shares emanate has several advantages. The issuer will already most likely be fulfilling the regulatory and accounting requirements for ORB by maintaining the equity listing. Furthermore, retail investors may already be familiar with the company through the share issue.

Investors will likely take comfort from the fact that press and brokers comment on listed shares on a regular basis, with much information in the public domain. Nevertheless, the lead should ensure suitable safeguards are in place to protect retail investors. These could include subsidiary guarantees, covenants and any other factors specific to a particular issuer. Derogation from the regulator in relation to the guarantee subsidiaries would be a great benefit at this stage. Such a development would allow for a repeal, or relaxation, of these rules.

There could be many situations in which an SPV is the most suitable issuing entity. This is highly likely to be the case for unlisted companies, such as housing associations or privately owned companies. All types have issued successfully into the market, but private companies (unrated, without equity shares listed on a regulated market and giving early warnings of business cycles and events) may need to offer security. This is often over physical assets.

Using an SPV as the issuing entity is acceptable as long as the bond, the issuer and guarantors satisfy the ORB listing requirements – see page 7 for the full list.

**Coupons: fixed, floating or RPI?**

- Fixed rate: A fixed-rate coupon is the starting point for most issues and provides both sides of the deal (issuer and investor) with certainty over cash flows.<sup>1</sup> For the issuer, which may be offered attractive revolver and similar facilities from its banks, the enthusiasm of the bank lender often fades when the borrower asks for fixed-rate term facilities. Similarly, an investor with a balanced portfolio will benefit from a fixed, regular income. Unlike wholesale markets, many retail market investors look at absolute yield when comparing what is currently available on deposit. Most other bond investors focus on relative value, usually via spreads to benchmark conventions. As a result, the retail bond may price at a rate that reflects the blended demand of both investor groups
- Floating: During times of rising yields and rates, there will be increased demand for retail bonds with floating rate coupons. There is some debate as to whether the coupon would be pegged to LIBOR (as in wholesale markets) or base rates, which may be more familiar to retail borrowers through deposit accounts
- Inflation-linked: In 2011, National Grid launched the first inflation-linked retail bond. Like many utilities, National Grid is a regular borrower in the inflation-linked format as the RPI<sup>2</sup> liability is a good match for its regulated income. At the time of issue, a number of macroeconomic factors were causing concern among investors, a factor that is often a trigger for investors seeking utilities as a safe haven. There was also frequent media commentary claiming inflation was likely to remain high for an extended period. This proved to be an opportune time to launch a utility RPI bond and the product eventually raised £282.5m

The lead manager advising a retail bond issuer should study market variations and steer towards the right structure for the time even if a major investor and media educational effort is required – as was the case with the first RPI issue. There is a time and place for 'linkers' and the lead will advise accordingly.

**Type of maturity**

- Bullet: Bullet (single date) redemptions are most popular with retail investors. However, these may occasionally allow a borrower to smooth or match the redemption profile through a series of redemptions
- Amortising/sinking fund: While this style has existed for many years in wholesale markets, the model is less popular in retail. It is possible that a partial redemption could leave a small investor with an illiquid or irregular size holding. Any valuation reports would also need to reflect that the number of bonds held has reduced or (more likely) that the redemption (par) value is no longer 100. This would then require a reduction in interest payments
- Callable: This system allows the issuer to redeem the bond before maturity. As with wholesale markets, borrowers can expect to include a make-whole provision to compensate investors for any possible loss of income

<sup>1</sup> This stands provided the company does not default.

<sup>2</sup> The Retail Price Index (RPI) is based on the UK's two principal indices of inflation and measures the cost of a basket of goods and services.

**Finding the best structure and optimal maturity**

As with any bond investment, investors must assess three main risks:

- Market risk
- Credit risk
- Liquidity risk

**Tenor of the bond**

The lead manager will listen to the maturity aspirations of the borrower (typically longer than investor expectations) and guide them to a solution that offers long tenor fixed rates for the issuer, but acceptable duration risks for the investor. In recent years, this duration is typically about seven years, but nine-year bonds have been successful if the business has clear long-term assets or activities. Inflation-linked bonds (being primarily a pension asset) are usually issued with longer terms of ten years.

**Credit risk and ratings**

There has been a great deal of debate about ratings. Most wealth managers will undertake a thorough credit analysis via their own means before making a recommendation to clients. From this perspective, a rating is therefore interesting, but not mandatory. The issuer meanwhile is often reluctant to commit to a rating for fear of the process being too costly in terms of time as well as money. Unless the issuer intends to access the markets on a regular basis, the benefits of ratings are questionable. While some wealth managers argue unrated bonds offer better value, the same managers increasingly work under constraints that limit how much of an unrated issue they may hold. A rated bond could arguably provide access to a wider universe of investors.

**Liquidity risk**

Liquidity is a relative concept, but few investors are comfortable with the prospect of being locked into a bond as the result of poor liquidity. The perception of liquidity is important and the lead manager should guide issuers and investors to a size above the perceived threshold. Although there have been issues as small as £25m, investors tend to be more comfortable with larger issue sizes. This is because companies may need to pay a premium for smaller issues. Furthermore, having a broad spread of investors has obvious liquidity benefits over a tight and narrowly held bond. Distribution to a broad investor base is therefore important.

**The role of covenants**

Covenants are frequently born out of bitter experience and should provide the management team with an early warning sign to take action. However, it is relatively easy and common practice for borrowers to discuss financial management needs with banks or other core lenders.

It could be considerably more difficult to discuss financial covenants and possibly arrange a period of leniency with a large group of retail investors and retail bond covenants may be more tolerant than banking covenants. They should offer protection to investors, but not prevent the business from running smoothly – which is in everyone's best interests. Covenants should not stifle the financial director, but must also offer protection to the retail investor community.

Most bonds will include issuer covenants such as:

- Negative pledge – normally restricted to ‘listed instruments’, this condition prohibits the borrower from pledging any of its assets in a way that could jeopardise the bond
- Cross default – provision giving the trustee permission to place all loans into default if the borrower defaults on a single loan
- Change of control – this stipulation allows for certain actions should there be a change in the organisation’s leadership
- Maintenance of listing – obligations that must be met for the listing to remain valid and legitimate.

Financial covenants will often be sector-specific and frequently take their lead from the bank covenants or possibly outstanding bond covenants, but could possibly be adapted as discussed above.

#### **Retail versus retail-eligible**

Early retail bonds were intended specifically for retail investors via discretionary, advisory or execution only-brokers. Despite some early criticism from wholesale managers, demand is growing among yield-seeking funds. This is a positive development. The presence of institutional holders will aid liquidity, verification of price and, of course, help the deal sell. This process is now extending, which means smaller wholesale bonds are being additionally offered to retail and, as a result, gaining the widest audience. Retail-eligible bonds are available to wholesale and retail markets.

#### **Testing market conditions**

With the exception of the lead manager, advisers start charging at an early stage and, if for any reason, the bond is not brought to market, the fees are charged, paid and lost. In order to minimise these risks, the lead should be upfront and realistic about suitability of the name, along with coupon and maturity expectations.

He or she should also arrange a series of introductions to a small number of key investors. The introductions are an opportunity for the borrower to meet the market and hear first-hand, how the offer is likely to be received. Always with a keen eye on compliance, these meetings are ‘non-deal’ and the issuer can honestly say he or she is researching retail bonds as one of several options. A ‘non-deal roadshow’ can allow the treasurer or financial director to accurately advise the board about the marketplace and confidently predict a successful issue.

The investor will then have no further communication with the lead manager or borrower until the release of a regulatory news service some weeks later, which will state that a series of meetings have been arranged and a retail bond may follow.

**The roadshows begin**

The lead manager will arrange sessions with stockbrokers, wealth managers and private banks. These presentations aim to focus on enduring stability and prudent management, rather than the growth story, and are an opportunity to show another facet of the business.

Here is an example itinerary:

- Day one – London: Five one-to-one meetings with the bond specialists among the wealth managers
- Day two – London: Breakfast presentation to a group of wealth managers from various firms, followed by group presentations in Leeds and Manchester
- Day three – Glasgow, Edinburgh and (possibly) Aberdeen
- Day four – Channel Islands

There will also be media sessions and the locations may be increased to include wealth manager meetings in Bristol, Birmingham and Liverpool.

Despite a demanding schedule, the opportunity to explain the business to wealth managers will be time very well spent. Discussions will often be interactive and give the management team a feel for the likely appetite for a live transaction.

# FPO

**The books open: book-building**

Often open for up to two weeks, the book-build process needs careful management. By the time books are opened, the public documents are distributed and include a term sheet, prospectus and information booklet. Full details of the issue are released, including price (usually 100), coupon and maturity. The only unknown will be size, which may be indicated as a range only.

There are a number of things to consider about the book- build process:

- The books should be open long enough to give all investors an opportunity to participate. Funds usually make instant decisions. However, a member of the public buying through an execution-only broker may take a couple of days to hear about the offer and react
- Because the issue size is unknown, midway size announcements can be helpful. These serve to confirm the book is progressing well and may close early. For the many professional investors limited to, say, 5% of an issue, such announcements also help to clarify the proportion their orders represent and if they are able to add further orders
- If the book is oversubscribed, some (or all) orders are scaled back. This process is unpopular in all markets and it is very important that the lead manager offers clear guidance on allocating in a fair and consistent manner

The chart below shows a typical book-build. In this case, the bond sold very quickly and was oversubscribed by the fifth day – hence the scaling back to £80m.

# FPO

**An enjoyable experience**

As with all capital-raising programmes, a retail bond requires effort and discipline from all concerned, but many issuers claim to have enjoyed the process, from early discussions through to the roadshow and even the tense days of the book-building process.

The experienced lead manager will run the process with a clear aim to raise cost-effective funds for the borrower, enhance public image, and (just as importantly) ensure there is a good investor experience throughout the life of the bond, not just at launch.

“ORB has drawn significant attention to a thriving market in which retail investors can now participate”

# Targeting the right investors

## Canaccord Genuity

Mark Glowrey, Fixed Income Sales

Morton Llewellyn, Debt Markets

Henrietta Podd, Debt Markets

**A guide to engaging with ORB's diversified investor base**

Who invests in retail bonds? Will the investor base grow? What is the investment goal? Will these bonds still exist in five years? These are all questions that first-time issuers who are looking to raise funds through London Stock Exchange's Order book for Retail Bonds (ORB) trading platform justifiably ask. This guide covers underlying investor profiles, the value of a diversified investor base, how ORB has become relevant to this investor base and how best to engage with these investors, through either the primary market stage or secondary market activities.

### **The disappearance of the retail investor base**

First, a short history lesson. Until the 1960s, retail investors actively bought bonds. During the latter part of the 20th century, however, a combination of inflation and exchange controls gradually killed off the bond market. When it revived in the 1980s, it became dominated by wholesale investors as retail investors turned to the equity markets. The final death knell came in 2003, when the European Union effectively imposed a minimum denomination on bonds, which was brought into UK regulation – initially as €50,000 and later in 2010 at €100,000. Unlike the equity market, which has retained direct private investment, the bond market has moved towards a business-to-business environment, with large corporations issuing large bonds. These bonds are, in turn, absorbed by funds of a proportionate size, often with many billions under management. The benchmark size for an issue in the sterling bond market is taken to be £250m.

**“Unlike the equity market, the bond market has moved towards a business-to-business environment”**

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**150**

The number of bonds and gilts London Stock Exchange transferred to ORB in 2010

This has resulted in two consequences: the disappearance of the direct retail investor in the bond markets, and closing the market to medium-sized companies wishing to raise debt in amounts below the perceived benchmark size. Smaller investors who wish to put tens (or hundreds) of thousands to work have struggled to gain access to the market, both primary and secondary.

### London Stock Exchange's platform for retail investors

In answer to this problem, and with support from an increasingly frustrated wealth management sector, London Stock Exchange launched the ORB platform in 2010.

London Stock Exchange transferred about 150 corporate bonds and gilts to ORB, which created a visible market for all investors. It is now a highly visible shopping window to the bond market for the retail investor base.

Discretionary wealth managers were some of the first investors to put money to work in the newly emerging retail bonds. During the next few years, however, a variety of different types of investors became regular users of the market.

This created a platform for primary issuance (known as 'born on ORB') that could allocate retail investors' orders on a fairer basis than typically happens with wholesale issues.

### The increasingly diverse retail bond investor base

As a regulated security, a corporate bond can only be bought by a retail investor through an appropriately qualified stockbroker, wealth manager or other regulated intermediary. The strong demand for fixed-income investment from a range of issuers, not necessarily rated, maturing between five and 10 years and offering an attractive yield, has encouraged a wide range of intermediaries to become involved.

### Discretionary wealth management (DWM)

This is the default option for many investors wishing to use an adviser. The manager exercises full discretion over the client's account and typically diversifies across a number of asset classes. While many such managers have funds under management in the billions, the ease of access and greater frangibility of the retail bond market is highly appealing. Investors of this type have a similar approach to running bond portfolios as many conventional fund managers. As with institutional investors, the credit rating, or lack thereof, will form part of the decision-making process. DWMs have a notable presence on ORB with a buy-and-hold profile.

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“London Stock Exchange has created a highly visible shopping window to the bond market for retail investors”

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**£10k**

The minimum denomination for bonds on ORB cannot be above this amount

**Advisory stockbrokers**

This is the traditional form of stockbroking, although it is becoming less common as clients migrate to discretionary or execution-only models. With this model, clients interact with the broker to make decisions on investment. Many of the considerations of discretionary managers will remain. However, such investors are frequently more risk-positive and trading-oriented, responding to price moves in the secondary market.

**Execution-only stockbrokers**

Many private investors are comfortable with, and indeed enjoy, making their own investment decisions. This has been the case for many years in the equity markets and the retail bond market has followed suit. Investors using these platforms are typically focused on absolute return, rather than relative value, and favour well-known names. Tax wrappers are an important factor for such investors and ISAs are the most popular mechanism for holding bonds, followed by SIPPs. These two low-cost tax shelters have provided an important boost for retail bonds, helping to moderate the established bias against income-style investing in the UK.

**Online brokers**

Such brokers fall into an execution-only category and their emergence has been the most significant change for private investors during the past decade. Low-cost execution, combined with easily accessed web-based information has, in many ways, placed private investors on a level playing field with fund managers. Retail bonds have found a ready market among this investor base, many of whom have rotated cash out of low-paying deposit accounts into the more attractive yields available in this sector. Again, the tax shelter afforded by ISAs and SIPPs is an important factor in boosting the popularity of retail bonds among this type of investor.

**Independent Financial Advisers (IFAs)**

IFAs generally do not deal in securities and tend to make use of pooled funds. The impact of the Retail Distribution Review<sup>2</sup> is seeing many advisers consolidate into larger groups, often with access to efficient centralised dealing and custody facilities. These larger funds provide an efficient route to ORB. Direct investment in bonds currently makes up only a small proportion of this total, although the area has potential for growth.

**Institutional investors**

One feature of the retail bond market is the opportunity to offer issuers investor diversification. As a result, it may seem counterintuitive that fund managers have started to feature in bond issues. However, the sterling market lacks breadth of issuers and ORB-listed bonds provide a valuable source of variety for such investors. In the secondary market, the price action of retail bonds frequently differs from the conventional run of corporates. Relative value-driven switch trades have also brought the sector to the attention of many funds, which also value the transparency of the exchange-traded platform. As the market grows, it will become more attractive to this type of investor.

<sup>2</sup> This piece of legislation came into force in December 2012 and sets standards of conduct by which financial advisers must abide, especially relating to fees and transparency.

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**£40m****The value of trades that go through the market on a weekly basis**

### How to reach out and connect with investors

There are two phases when a firm interacts with the investor community and both involve sell-side activities. The first is during the primary phase, when marketing a new issue, and the other is in the secondary market, when executing trades on behalf of a client – either on a reactive or a proactive basis.

The primary phase is a significantly more intense period of marketing as the book runner is operating to a deadline, has a borrower who intends to raise new capital and typically needs to raise capital in excess of the value of trades that go through the market on a weekly basis (circa £40m). At the planning phase of marketing, it is essential to target suitable investors, as well as maximising coverage across the investor community. Different bond issues attract different levels of demand from various investor groups. The £150m issue by A2Dominion was the first issue to see a significant wholesale participation, while Premier Oil attracted one of the most diverse retail investor groups to date when it raised a similar amount.

Interaction with investors through the secondary market is reactive and proactive. Reactive when investors approach market makers for prices, but proactive when developing trading ideas based on research, whether purely value-driven or in expectation of a material credit event. The marketing of trading ideas provides an excellent opportunity for a sales desk to broaden the investor base and entice more investors for 'born on ORB' bonds. This is especially true of wholesale investors who have become familiar with the workings and liquidity of the ORB marketplace and have meaningful buyers across a number of issues.

### Roadshows and book-building

This is an absolutely key phase of a bond issue as the company formally starts marketing a potential transaction and needs to compete for investors' attention against other secondary market offerings and new issues. With the retail investor base, the competition also includes equity, structured products and even guaranteed bank deposits. The book runner is not only keen to see an issue successfully completed, but also ensure an orderly secondary market develops with reasonable flow and to set reference yield levels for future issues.

As a result, a book runner will want to finalise an order book with a healthy range of committed long-term investors, without any group holding an excessive percentage of the book or without clearly short-term investors. Wholesale investors, typically holding £10m to £25m in a wholesale issue, tend to be held at approximately £5m to avoid excessive concentration. There is nothing to prevent them building up a larger position through the secondary market after the issue.

Developing an appropriate roadshow and communication through conference calls is essential. The typical roadshow can take as many as four days across the UK and Channel Islands (see graphic, opposite) and combines lunch presentations with one-to-one meetings. Roadshows will typically have between 10 and 100 attendees.

Potential key roadshow destinations

**FPO**

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“Developing an appropriate roadshow and communication through conference calls is essential”

The retail distribution pyramid

**FPO**

### Securing the future of the market

The market has grown impressively in recent years. However, there is still a way to go to develop this market in order to attract more investors, market makers and borrowers.

#### **Make primary issuers more cost-competitive and lower primary yield levels**

For bonds with less than five years to maturity becoming ISA-eligible from July 2014, investors will be able to access new issues of shorter-dated bonds and the bond/ISA combination will provide meaningful competition for the multibillion-pound cash ISA and retail-deposit markets. From an investor's point of view, the risk profiles of the two types of investments are different, with deposits benefiting from the Financial Services Compensation Scheme. When short-term rates are low and the outlook for future rate rises moderate, a diversified portfolio of shorter-dated bonds will provide a good balance between risk and reward. In addition, the increasing wholesale investor involvement will assist this. The reduction of the five-year ISA hurdle will help attract retail investors to lower yield levels for shorter durations.

#### **Make risk profiles more transparent**

A number of unrated issues have distinct sub-investment grade characteristics, whether due to size, sector or structure. As more issues come to the market at different yield levels, it is helpful for investors to differentiate between different credits and structures, and price the differential appropriately. Independent credit research is therefore likely to be a helpful development for the market.

#### **Documentation/obtaining a listing**

Documentation has to comply with the requirements of the Financial Conduct Authority (FCA) Listing Rules. Wholesale bonds are straightforward to list with a relatively simple listing document. However, the FCA requires an issuer of bonds in small denominations to provide information in a different format. The retail-eligible documentation is longer and can be more expensive to complete. Issuers that wish to use both wholesale and retail markets may have to produce two sets of documents.

ORB has drawn significant attention to a thriving market in which retail investors can now participate, rather than feeling dependent on bond funds and the performance of fund managers. It has created significant publicity, which benefits both investors and issuers. It permits investors to manage their own bond portfolio and opens a capital market that helps UK companies reduce their dependence on banks.

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“ORB opens a capital market to UK corporates previously dependent on banks”

“Retail bonds involve communication with a much wider audience, reaching thousands of potential individual investors”

# Raising the company profile and widening the investor base

## Bell Pottinger

Victoria Geoghegan, Partner

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**Why an effective PR strategy is key to the success of a bond issue**

The industry has come a long way since the launch of the Order book for Retail Bonds (ORB). What started out as an experimental market has evolved into an increasingly established source of capital for businesses with a number of repeat issuers. Businesses from a range of economic sectors have all raised money for investors – from oil production to property and finance. A secondary market has also emerged with strong liquidity.

Having an effective and well-planned PR strategy can be one of the most important factors in determining the success of a bond issue. If the communication is done correctly, it can open the bond to a large new base of potential investors and also bring the issue to the attention of the markets and the media.

The retail bond market shares some obvious similarities with the institutional bond market, but the process of launching a retail bond and the communications required are very different. One of the most striking differences is the amount of work to raise awareness of the bond. Institutional bonds require a few conversations with large investors. However, retail bonds involve communication with a much wider audience, reaching thousands of potential individual investors.

This process has changed since the launch of ORB in 2010. As the market has matured, the changes in how journalists view and understand it have been marked.

Broadly speaking, this is a good thing for companies coming to the market.

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**“As the market has matured, the changes in how journalists view it have been marked”**

A number of early teething issues have been resolved. For example, the confusion between listed and unlisted retail bonds has largely been addressed, with many journalists now attuned to the difference. What had once been a threat to the sector – that investors would confuse the listed retail bond market with the comparatively unregulated mini-bond market – has become something of a strength, highlighting the transparency and tradability of retail bonds.

Likewise, heightened concerns that came in the wake of bonds that were launched, but did not raise enough capital to come to market, appear to have dissipated. While the events provided negative headlines at the time, the market recovered, which allayed fears and also indicated there was more discretion in the retail market than some had feared.

#### **Growing knowledge**

Perhaps most importantly, the successes of the market has attracted media attention and left most journalists covering the sector well informed about the basics. While initial launches required a large amount of work to educate the media about retail bonds as an asset class, current conversations are increasingly focusing on the company and the structure itself.

However, the sheer number of bonds launched to date also means standing out from the crowd has become more difficult. As a result, companies need to be able to tell their stories in a creative, interesting way if they want to raise the profile of the bond among the execution-only investor segment.

When the market launched, most bonds received widespread coverage across national newspapers, as the novelty made an inherently attractive story. The issue of how Britain can develop new and alternative sources of finance has been prominent since the credit crunch. The opening of the retail bond market provided an exciting success story – similar to the high levels of media interest in other alternative sources of finance such as crowdsourcing.

It is inevitable that later issues will no longer hold the same level of excitement as the market matures – though this does not necessarily mean that bonds will be ignored. What makes a bond stand out will differ from issue to issue, but whether it is a new sector, a different tenor or an innovative structure, it is important the business is able to highlight the elements of the bond that make the launch newsworthy.

To some companies, this may be a comparatively minor problem. However, for businesses with a limited public profile and lacking a large retail shareholding, raising awareness through media engagement is particularly important.

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**“Companies must tell their stories in a creative, interesting way if they want to raise the profile of the bond”**

**Household names versus smaller businesses**

For large household names, creating an awareness of the business is not likely to prove a significant hurdle. However, for many businesses, accessing the market (especially FTSE 250 or private firms), educating potential investors and reassuring them the bond is supported by an established business is very important.

In this instance, media coverage can play a very important role as respected independent analysis.

**The importance of structure**

Of course, the communications activity behind any issue will be incomplete if the media and investors are left confused about the bond's structure. Whereas equity investors are investing in the future success of the business and the ability of the management team to grow the value of their capital, investors in retail bonds are more likely to see themselves as putting their money into a product, where their primary concern is whether or not the company will be able to continue to support that product. Retail bonds are not uniform in their structure and outlining the exact nature of the product is an important part of the overall communications activity.

Having the ability to explain relatively complicated products is even more valuable given the sophisticated understanding of the market that many journalists now have. Increasingly, businesses are being asked to address technical questions regarding the structure and pricing of the bond.

A good example is the launch of Bruntwood's retail bond in 2013. The bond itself was launched during a difficult period with high levels of market turbulence, particularly within fixed-income markets, following Ben Bernanke's comments regarding tapering by the Federal Reserve<sup>1</sup>. In spite of this potentially challenging backdrop, the issue raised £50m, playing a role in a wider successful refinancing by the company.

During this issue, it was important to outline the function of the business and its strengths. While Bruntwood is very well known in its core markets, it was less well known outside the north west. The bond issue and its accompanying publicity were effective in helping to raise the company's profile.

**Understanding a bond's structure**

While explaining the business itself mattered, it was just as important to ensure the media understood the difference in the bond's structure. Unlike other issues in which retail bond holders were subordinate to bank debt, investors would see their money secured against particular assets within the group's portfolio. Without an understanding of how the structure affected the investment, the picture would have been incomplete.

There are a number of reasons a strong public relations component is an important element in any retail bond launch. But it is important to recognise the process is very different to the standard work conducted for businesses looking to explain their investment case.

<sup>1</sup> In May 2013, then Federal Reserve Chairman Ben Bernanke indicated a slowdown of the US asset purchase programme.

**The value of the personal finance media**

It is largely the personal finance media, not the city correspondents, who drive coverage of the sector. This clearly places the emphasis on a different set of relationships and requires an understanding of a different group of publications and journalists. For many businesses, these will not be existing contacts.

Likewise, the way of describing the business and the investment story is very different to the approach required for equity investors. The majority of businesses are, understandably, used to explaining the opportunities that they have to grow, to focus on investments and the areas where they think they can expand. Whereas equity investors are looking for a business that can grow the value of their capital, investors in retail bonds are buying into a set product.

This requires businesses to learn a different way of describing what they do and their prospects for the future. Doing so can prove trickier than it may appear, going against instincts that have been second nature for the chief executives of many listed businesses.

The complexity involved in the communication of a retail bond launch is partly due to the nature of the product, but also reflects the growing maturity of the market. As a greater range of businesses and structures come to market, this complexity is set to increase.

Retail bonds have traditionally been issued in an environment in which there were very few alternatives for savers. Yields on retail bonds were comfortably higher than anything available in savings accounts and a relatively dormant IPO market meant there was comparatively little competition for retail investors' money.

A more favourable income rate environment for savers, however, could mean making the case for investors to put their money into a retail bond will become more of a challenge. Being able to explain how the structure of the bond fits into an environment of higher rates will be increasingly important. The majority of issues have historically been fixed rate – understanding of how inflation-linked products work is low and many investors would benefit from increased education in this area. Just as a great deal of work has been required to explain the implications of listed and unlisted bonds and differing levels of security, businesses that launch bonds linked to inflation will need to work hard to explain their products.

As the market continues to mature and change, it is likely we will continue to see the communications needs of businesses launching bonds changing at the same time. This is generally a positive development and should be welcomed by the industry. As long as issuers continue to adapt and refine the way they explain bonds, we can be confident the profile and depth of understanding will also grow, contributing to the long-term prospects of the industry.

“This guide looks at the process that takes place once books have been closed, bonds have been allocated and a final pricing call has confirmed all details with the issuer”

# Settling and issuing a bond

## Lloyds Bank Commercial Banking

Marcus Coverdale, Director, Debt Capital Markets

Samantha Riley, Director, Commercial Banking Legal

### Understanding the process of settling and issuing a bond

The retail bond market and ORB provide a flexible venue for issuers to raise finance. For investors, secondary market liquidity is visible and accessible, and standards of disclosure exceed those of the institutional bond market.

For both issuers and investors, there are a number of points to consider in relation to the settlement and issue of a bond. Certain subtleties relate only to retail bonds, particularly in the areas of settlement and ongoing reporting requirements.

#### The primary issue

This guide looks at the process that takes place once books have been closed, bonds have been allocated and a final pricing call has confirmed all details with the issuer. In reality, this pricing call can be something of a formality because, for a retail bond, the coupon is set ahead of opening the books. For institutional bonds, the usual pricing process is based on a spread over gilts or swaps and the settling of a resultant coupon is based on the current yield on the chosen gilt or the swap rate.

Following the agreement of the pricing of the bond, secondary market trading can commence, but participants must wait until settlement before exchanging cash flows and the issuer receives the proceeds (net of fees). Primary settlement is usually set at three to five days after closure of the books to allow time for the billing and delivering bank, the paying agent and the lawyers to finalise documentation and payment details.

**“Following the agreement of the pricing, secondary market trading can commence”**

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**£2,000****The minimum  
primary  
subscription for  
retail bonds**

The billing and delivering bank will usually look through the calendar for the year of maturity to find a convenient maturity date – for example, not falling on a weekend or a bank holiday. This may result in the bond settlement date being set at a longer period than the normal T+3 or T+5. ('T' represents the transaction date, followed by the number of days following the transaction that settlement will occur.)

Retail bonds can vary from this timetable as books may close early due to oversubscription. A formal regulatory news service (RNS) announcement will signpost this early closure to the market. This advance notification can vary from one to 24 hours and will often depend on the momentum with which the book is growing.

Retail books are sized to meet the issuer's fundraising requirements, meaning the book is closed once the size target is met and oversubscription is managed to a low level. Early closure will not result in any change to the settlement date, which is set out in the draft final terms or the prospectus (for a standalone bond) at the launch with no room for movement. On occasion, therefore, there can be very long settlement periods of T+9 and T+10.

#### **The secondary market**

Secondary market trading commences once the bond is announced as 'free to trade' or deemed 'when issued traded' on the Order book for Retail Bonds (ORB).<sup>1</sup> The timing of the bond being free to trade is agreed by the lead managers' syndicate desks and is generally within an hour of the final pricing call. This is the formal point when market makers can post their bid and offer levels on screens and trading commences. A small amount of trading sometimes occurs during the 'grey' market that develops once investors have been advised of allocations.

When a bond is documented under a medium-term note programme, trading of the bond commences on the settlement date. When a bond is documented on a standalone basis, then trading in the bond only commences one day after settlement.

Investors may wish to top up their allocations and will be looking for bonds. While nobody has any bonds at this stage, and won't until settlement, the coupon has already been set, prices have been set and trading can occur.

In any bond's primary investor book, there are likely to be some investors who have taken a view on the relative value in the coupon and spread, expecting the bond to trade up in the secondary market – for the price to rise. These investors may want to quickly on-sell the bond and make a profit on the difference between the price at issue and the price in the secondary market. This practice is less common in the retail bond market than the institutional market, but still exists.

The lead managers and bookrunners of the primary issue will generally attempt to minimise the potential for loose bonds in the secondary market through a thoughtful primary allocation process – allocating bonds in consultation with the issuer to accounts known for being buy-and-hold investors. The secondary desks of these lead managers are likely to support the new issue in the secondary market by bidding on loose bonds. It is a good idea for issuers to check the market-making limits their lead managers can apply to the secondary market.

<sup>1</sup> For more information on 'when issued dealing' trading on ORB, visit [www.londonstockexchange.com/traders-and-brokers/security-types/retail-bonds/downloads/whenissueddealing.pdf](http://www.londonstockexchange.com/traders-and-brokers/security-types/retail-bonds/downloads/whenissueddealing.pdf)

**Ongoing coupon payments and cashflows**

During the lifetime of a bond issue, some of the notes will trade actively, while others rest quietly in investors' portfolios, with the investor happy to focus on fixed-income generation from the half-yearly coupon payments. The issuer will make coupon payments (usually every six months and on maturity) to investors. A paying agent, appointed by the issuer, can manage these payments, calculate the coupon payments and transmit funds to bond holders through the International Central Securities Depositories – Euroclear and Clearstream. Some issuers will also appoint a trustee for the bonds. The trustee will:

- Act as intermediary between the issuer and bond holders
- Monitor the receipt of ongoing information from the issuer – for example, the annual report and accounts
- Maintain the rights of bond holders in any covenants in the bond documentation.

**Market makers**

There will be a range of market makers providing two-way pricing for the bond in the secondary market, both on- and off-ORB. The ORB requirements for market makers are to enter two-way electronic executable orders (EQs) within the applicable maximum spread for the sector.

Corporate bonds are broken down into three categories – UKC1, UKC2 and UKC3 with maximum secondary market quote spreads (the difference between the bid and the offer quotes) of 3%, 5%, and 10% respectively. The majority of corporate bonds issued on ORB fall within the first two categories, with a small number in the third.

Gilts are broken down into two segments – UKG1 and UKG2. The maximum spreads allowed in ORB quotes are 1.5% and 3% respectively, and the ORB trading system rejects quotes wider than these levels. Most ORB-listed gilts are categorised as UKG1, with a small number of less liquid gilts categorised as UKG2.

These bands are technical limits set at relatively wide levels to allow maximum flexibility and ensure market makers can support the system.

Market maker EQs must be entered in at least the exchange market size (EMS) for the instrument concerned. These quotes will be available for electronic execution by any other qualifying member firm. For corporate bonds, the minimum EMS is £25,000, and for gilts it is £40,000. Some less liquid corporate bonds may require a lower EMS setting.

The trading day for all segments traded on ORB runs from 8:00 – 16:30 UTC. From 7:50 – 8:00, there is an opening auction, and from 16:30 – 16:35, there is a closing auction. These opening and closing auctions ensure the market open period of continuous trading is conducted as smoothly as possible. Market makers must submit quotes for at least 90% of continuous trading in the bonds they are registered in and this is measured daily.

## £100

### The minimum denomination for retail bonds

In addition to the lead managers' secondary desks, there are a number of independent market makers registered on ORB that will make a market in the bonds.<sup>2</sup>

Having this mix of market makers ensures secondary market liquidity can extend to all corners of the market. Small-sized holders of retail bonds across the country are also able to access secondary market liquidity in the right size.

#### Liquidity

Secondary market liquidity is of critical importance for the public markets. Both institutional and retail bond markets rely on liquidity to operate efficiently and ensure holders of bonds are able to access a bid when they want to sell.

The general perception of the largest investors in the retail bond market is that the minimum issue size required to ensure liquidity in the secondary market is £50m. (The equivalent figure for the GBP wholesale/institutional market is £250m.<sup>3</sup>) Liquidity is important to ensure efficient markets and provide an accurate reflection of the market view of the price of the bond.

#### Bond pricing

The bond's secondary market price will be affected by underlying rates, as well as the issuer's credit quality and the structure of the bond. This could include a view on any potential subordination the terms of the bond allows.

When there are more buyers than sellers, the price of the bond goes up. From an issue at par (100), the cash price may increase to 101 or 101.5, for example. This means the yield will go down – there is an inverse relationship between price and yield based on the fixed coupon.

If the price goes up, the yield will reduce as investors are paying more than par to buy a fixed-income return of a certain amount, stated as a percentage of 100 – the par value of the bond – for a fixed time period. If there are more sellers than buyers, the price can go down – to 99.5 or 99, for example. This will have the opposite effect and the yield will go up. This situation can reflect the increased risk of holding the bond – the price has gone down and the yield has gone up for any new buyers. Higher risk results in potential higher return.

From an investor perspective, some may be focused on holding fixed-income securities for this precise reason – the fixed income or coupon. These are paid half-yearly, until the maturity of the bond. However, corporate bonds do not guarantee the final repayment and are subject to changes in the status of the issuer's credit quality.

From an issuer's perspective, there will be a constant live price for their debt. Further issues will reference that price, potentially building up a 'curve' of pricing over a range of tenors. These levels are based on buyers' and sellers' appetite for the credit, and reflect the market price for the issuer's debt.

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“A mix of market makers ensures secondary market liquidity can extend to all corners of the market”

<sup>2</sup> For a full list of these market makers, visit [www.londonstockexchange.com/traders-and-brokers/security-types/retail-bonds/marketmakers.pdf](http://www.londonstockexchange.com/traders-and-brokers/security-types/retail-bonds/marketmakers.pdf)

<sup>3</sup> The figure is based on standard market practice.

### Ongoing obligations for bond issuers

Bond issuers have ongoing obligations regarding the terms and conditions set out in the prospectus. Key among these are the maintenance of coupon payments throughout the lifetime of the bond and the ongoing publication of information.

Missing a coupon payment qualifies as a default (if not remedied within a limited timescale – usually 14 days). These terms and conditions also govern certain aspects of what the issuer can do in terms of selling assets, changing its business, or maintaining certain covenants. The trustee, who is appointed by the issuer, but with a fiduciary duty of care to the bond holders, is responsible for taking action on behalf of the bond holders in order to enforce their rights in relation to these covenants.

Ongoing obligations in relation to the publication of annual and interim accounts, and the allowed timescales, differ slightly from the institutional bond market.

### Key ongoing disclosure requirements

The Transparency Directive came into effect in the UK from 20 January 2007 with the stated purpose of harmonising disclosure standards for companies across Europe. It has been refined over time following consultations.

The directive requires companies to disclose information at regular intervals through prescribed channels and in such a way as to impose similar requirements across borders.

It works alongside the Market Abuse Directive (MAD), which was implemented in the UK on 1 July 2005. While MAD addresses the handling and dissemination of inside information by companies to remove the risk of market abuse, the Transparency Directive focuses on information companies need to disclose on a periodic basis and how this information should be made public.

The former FSA implemented the directive through the Financial Conduct Authority publication of a technical note on the Disclosure and Transparency Rules (DTR).

### Retail bonds versus institutional bonds

**Retail bond market** refers to bonds sold bearing denominations below £100,000 – often £100, with a minimum primary subscription of £2,000. These bonds are subject to enhanced disclosure requirements as detailed overleaf. Retail bonds are often (but not exclusively) marketed in primary distribution through an extended book-build, and listed on ORB.

**Institutional bond market** refers to bonds sold in denominations of £100,000 or higher. These bonds are allowed some exemptions from the disclosure rules and are usually marketed on an intra-day basis to institutional investors, including fund managers and asset managers.

**What does a company need to disclose on an ongoing basis?**

A company that has applied for securities with a denomination of less than £100,000 to be listed and admitted to trading on London Stock Exchange will need to comply with certain ongoing disclosure requirements.

According to the DTRs, a company:

- DTR 4.1 – will need to publish an annual report within four months of the end of its financial year end. Annual reports must include:
  - (i) audited financial statements
  - (ii) a management report, and
  - (iii) a responsibility statement.
- DTR 4.2 – will need to publish a half-yearly report as soon as possible and, in any event, within two months of each period end. The half-yearly report must contain:
  - (i) condensed financial statements (in accordance with IAS 34 or equivalent)
  - (ii) an interim management report, and
  - (iii) responsibility statement.
- DTR 6 – will need to notify of any amendments to the issuer’s constitution/articles and make disclosure of any changes in the rights of holders, information on holder meetings etc. The information must be disseminated to a Regulatory Information Service (RIS).
- DTR 7 – an issuer must have a body responsible for performing the audit functions set out in DTR 7 and the issuer must produce a corporate governance statement.
- DTR 2: disclosure and control of inside information – issuers must notify an RIS as soon as possible of any inside information that directly concerns it, unless it is permitted to delay disclosure. There is also a requirement to keep up-to-date lists of insiders.

These disclosure requirements are part of the obligation to disclose regulated information, which is defined as:

**“All information which the issuer, or any person who has applied for the submission of securities to trading on a regulated market, without the issuer’s consent, is required to disclose under the directive, under article 6 of MAD, under the laws, regulations and administrative provisions of a member state adopted under article 3(1) of the directive or under article 3(3) of the directive, which includes foreign filings.”**

In summary, retail investors benefit from standards of disclosure that exceed the institutional bond market. This, allied with the visibility of and access to secondary market liquidity through ORB, ensures that up-to-date information on issuers and the market is available to retail investors on an ongoing basis.

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**“Retail bonds are often marketed in primary distribution through an extended book-build”**



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