

COMMENTARY: INFRASTRUCTURE IN THE US PRIVATE PLACEMENT MARKET



Geoffrey Schmidt
General Manager, National Australia Bank, New York

Ports and airports, toll roads and tunnels. These are just some examples of infrastructure sold into the US Private Placement (USPP) market over the last several years. Assets that were once unpopular and highly priced in this market are now commanding better credit spreads than many other sectors. This article will discuss the evolution of infrastructure into the USPP market over the last five years.

INFRASTRUCTURE BOOM IN THE USPP

According to National Australia Bank data, there were a total of 72 (non-power related) infrastructure US Private Placements sold into the market from 1 January 2013 through 31 December 2017. Although the size, scope and makeup of these assets varied over the period, each of these would have been deemed “critical assets” to the countries and populations they served.

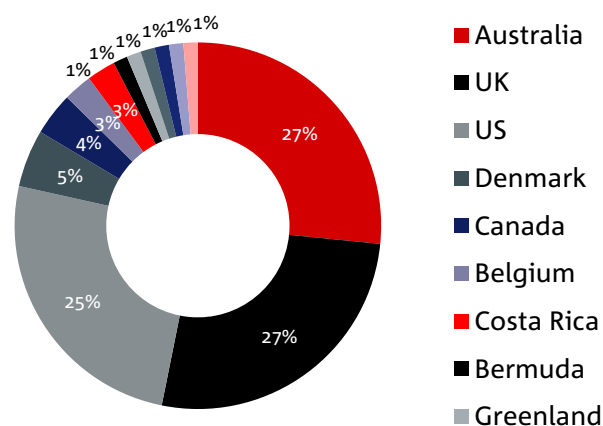
Most were massive undertakings, costing billions of dollars to build, yet are nearly invisible to day-to-day users. They travel the bridges, tunnels, and rail without much thought to the cost involved to build and maintain the asset; they drink the water from the tap that was created at the desalination plant 84 kilometers away without knowing the technology that went into each glass, and they drive the car imported from Japan without knowing that it first had to come into a port built in a strategically critical location.

UNDERSTANDING INFRA-ASSETS

There is a specific demographic makeup of infra-assets that do well in the US Private Placement market. These center around country of origin, alternative funding options, and most importantly the nature of the debt investors themselves. Each is discussed below.

Australia and the UK are tied for total number of issuances into this market over a five-year period – each providing 21 transactions. This is followed closely by the United States with 20 and the next closest, Denmark, providing four.

Percentage of USPP Infrastructure Transactions by Country - 2013 to 2017



Source: National Australia Bank and Thomson Reuters Data

WHY AUSTRALIA, THE UNITED KINGDOM AND THE UNITED STATES?

The reason is the geographic and political make-up of the countries themselves – each is a little different than the other, but all have favourable conditions for infra-USPP issuance. Australia has the smallest population of the three but is tied for first in total issuance. Why is this? Because Australia is undergoing significant privatisation and modernisation. With both of these attributes comes private funding – bank loans first and then the bond markets shortly thereafter. Some of the earlier assets are coming up for refinancing and, as a consequence,

are issuing more and more into the markets, rebalancing bank debt and bond market debt.

The United Kingdom is further along the privatisation path, so we are seeing more refinancing of existing infrastructure and less first-time privatisation funding.

Most of the infrastructure in the United States is still funded at the state level, with subsequent bond issuance into the municipal bond market. Issuance into the US Private Placement market is a result of the sheer size and scope of the country itself, because per capita issuance is small (especially when compared to Australia and the UK) but growing. The US has the most room of the three countries to “modernise” its ageing infrastructure, so despite state level financing, there should continue to be a growing pipeline in the future.

WHY US PRIVATE PLACEMENT MARKET?

If a US mutual fund was to invest in a municipal bond, it would normally be investing in the credit risk of the state itself. It's less about the asset and more about the state's ability to pay. This does not mean that there are not municipal bonds whose risk is tied to the performance of the asset, but this is less likely in the United States (in the US these are often called Private Activity Bonds, or PABs) than many other areas of the world. (I'll note that this may change as the Trump agenda takes hold.)

PRIVATE PLACEMENT INVESTORS ARE “BANK LIKE”

Most municipal bonds have straightforward “state based” credit risk and are well suited for investors and the funds that participate in high volume, frequent issuances by states and municipalities across the USA. On the other end are transactions that are bespoke. Structural protection is designed for the asset under consideration. Revenue is derived from a variety of different “non-state” sources and operating history is often significantly shorter. These assets are perfect for the US Private Placement investor –

because US Private Placement investors are some of the most sophisticated in the world, and will take the time to deeply understand credit risk.

US Private Placement investors are often referred to as “bank-like,” because of their long term buy and hold nature, the amount of credit work they do and the amount of capital they deploy. This week, for example, NAB completed a US\$1 billion+ transaction for a well-known, highly regarded Australian company. The largest USPP investor bid in excess of US\$300 million-dollars. The second largest bidder was over US\$150 million and numbers three, four, and five were US\$100 million or more. Some major banks won't commit that much capital to a single client, so how can players in the US Private Placement market do it, particularly if it's long term (10+ years) capital? They do the same level of credit work as many banks.

HOW TO TELL IF AN INFRASTRUCTURE ASSET IS RIGHT FOR US PRIVATE PLACEMENTS?

If the asset has investment grade characteristics, is mission critical, is privately owned (or is part of a public/private partnership) and has long dated funding needs, then it's probably a good candidate.

For more information please contact our US Private Placement Team at National Australia Bank in New York: 212-916-9678.

CONTACT THE AUTHOR

Geoffrey Schmidt
General Manager
Corporate Finance, Corporate & Institutional Banking
National Australia Bank, New York Branch
gschmidt@nabny.com

Sources

- 1 www.cnbc.com/2017/05/23/moodys-downgrades-china-rating-to-a1-from-aa3-with-stable-outlook.html
- 2 www.cnbc.com/2017/09/21/sp-cuts-chinas-credit-rating-citing-increasing-economic-financial-risks.html
- 3 www.reuters.com/article/china-economy-state-firms/update-1-china-to-further-cut-debt-ratios-at-big-state-owned-firms-as-profit-growth-surges-idUSL3N1PC1NT
- 4 <https://www.ft.com/content/d6cebf7e-e449-11e7-97e2-916d4fbac0da>
- 5 <https://www.bloomberg.com/news/articles/2018-01-22/trump-makes-first-big-trade-move-with-tariffs-aimed-at-asia>
- 6 <https://www.bloomberg.com/news/articles/2018-01-24/mnuchin-says-weaker-dollar-is-good-for-u-s-due-to-trade>

Important Notice

Disclaimer: This document has been prepared by National Australia Bank Limited ABN 12 004 044 937 AFSL 230686 (“**NAB**”). Any advice contained in this document has been prepared without taking into account your objectives, financial situation or needs. Before acting on any advice in this document, NAB recommends that you consider whether the advice is appropriate for your circumstances. NAB recommends that you obtain and consider the relevant Product Disclosure Statement or other disclosure document, before making any decision about a product including whether to acquire or to continue to hold it. Products are issued by NAB unless otherwise specified.

So far as laws and regulatory requirements permit, NAB, its related companies, associated entities and any officer, employee, agent, adviser or contractor thereof (the “**NAB Group**”) does not warrant or represent that the information, recommendations, opinions or conclusions contained in this document (“**Information**”) is accurate, reliable, complete or current. The Information is indicative and prepared for information purposes only and does not purport to contain all matters relevant to any particular investment or financial instrument. The Information is not intended to be relied upon and in all cases anyone proposing to use the Information should independently verify and check its accuracy, completeness, reliability and suitability obtain appropriate professional advice. The Information is not intended to create any legal or fiduciary relationship and nothing contained in this document will be considered an invitation to engage in business, a recommendation, guidance, invitation, inducement, proposal, advice or solicitation to provide investment, financial or banking services or an invitation to engage in business or invest, buy, sell or deal in any securities or other financial instruments.

The Information is subject to change without notice, but the NAB Group shall not be under any duty to update or correct it. All statements as to future matters are not guaranteed to be accurate and any statements as to past performance do not represent future performance. The NAB Group takes various positions and/or roles in relation to financial products and services, and (subject to NAB policies) may hold a position or act as a price-maker in the financial instruments of any company or issuer discussed within this document, or act and receive fees as an underwriter, placement agent, adviser, broker or lender to such company or issuer. The NAB Group may transact, for its own account or for the account of any client(s), the securities of or other financial instruments relating to any company or issuer described in the Information, including in a manner that is inconsistent with or contrary to the Information. Subject to any terms implied by law and which cannot be excluded, the NAB Group shall not be liable for any errors, omissions, defects or misrepresentations in the Information (including by reasons of negligence, negligent misstatement or otherwise) or for any loss or damage (whether direct or indirect) suffered by persons who use or rely on the Information. If any law prohibits the exclusion of such liability, the NAB Group limits its liability to the re-supply of the Information, provided that such limitation is permitted by law and is fair and reasonable. This document is intended for clients of the NAB Group only and may not be reproduced or distributed without the consent of NAB. The Information is governed by, and is to be construed in accordance with, the laws in force in the State of Victoria, Australia.

Analyst Disclaimer: The Information accurately reflects the personal views of the author(s) about the securities, issuers and other subject matters discussed, and is based upon sources reasonably believed to be reliable and accurate. The views of the author(s) do not necessarily reflect the views of the NAB Group. No part of the compensation of the author(s) was, is, or will be, directly or indirectly, related to any specific recommendations or views expressed. Research analysts responsible for this report receive compensation based upon, among other factors, the overall profitability of the Global Markets Division of NAB.

United Kingdom: If this document is distributed in the United Kingdom, such distribution is by National Australia Bank Limited, 88 Wood Street, London EC2V 7QQ. Registered in England BR1924. Head Office: 800 Bourke Street, Docklands, Victoria, 3008. Incorporated with limited liability in the State of Victoria, Australia. Authorised and regulated by the Australian Prudential Regulation Authority. Authorised in the UK by the Prudential Regulation Authority. Subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. Details about the extent of our regulation by the Prudential Regulation Authority are available from us on request.

USA: If this document is distributed in the United States, such distribution is by nabSecurities, LLC. This document is not intended as an offer or solicitation for the purchase or sale of any securities, financial instrument or product or to provide financial services. It is not the intention of nabSecurities to create legal relations on the basis of information provided herein.

Hong Kong: By accepting this document, you represent and warrant that you are a “**professional investor**” within the meaning of the definition of that term in Part 1 of Schedule 1 to the Securities and Futures Ordinance (Cap. 571 of the Laws of Hong Kong). If you think you have received this document in error, please contact NAB at Level 27, One Pacific Place, 88 Queensway, Hong Kong Ph: +852 2826 8111

If this document is distributed in Hong Kong, such distribution is by National Australia Bank Limited, Hong Kong Branch, which is licensed by the Hong Kong Monetary Authority and registered (CE Number AAO169) under the Securities and Futures Ordinance (Cap. 571 of the Laws of Hong Kong) for Type 1 (dealing in securities) and Type 4 (advising on securities) regulated activities. Its main business address is Level 27, One Pacific Place, 88 Queensway, Hong Kong.

The contents of this document have not been reviewed by any regulatory authority in Hong Kong. If you are in any doubt about any of the contents of this document, you should obtain independent professional advice.

New Zealand: This publication has been provided for general information only. Although every effort has been made to ensure this publication is accurate the contents should not be relied upon or used as a basis for entering into any products described in this publication. To the extent that any information or recommendations in this publication constitute financial advice, they do not take into account any person’s particular financial situation or goals. Bank of New Zealand strongly recommends readers seek independent legal/financial advice prior to acting in relation to any of the matters discussed in this publication. Neither Bank of New Zealand nor any person involved in this publication accepts any liability for any loss or damage whatsoever may directly or indirectly result from any advice, opinion, information, representation or omission, whether negligent or otherwise, contained in this publication. National Australia Bank Limited is not a registered bank in New Zealand.

Japan: National Australia Bank Ltd. has no licence of securities-related business in Japan. Therefore, this document is only for your information purpose and is not intended as an offer or solicitation for the purchase or sale of the securities described herein or for any other action.

Singapore: This document is distributed in Singapore to institutional investors (as defined under the Financial Advisers Regulations) only.

People’s Republic of China: In the PRC, the Materials are directed solely at persons who would be constituted as (i) Qualified Domestic Institutional Investors in accordance with the applicable PRC laws and regulations promulgated by China Banking Regulatory Commission, China Securities Regulatory Commission or China Insurance Regulatory Commission or (ii) other eligible investors in accordance with the applicable PRC laws and regulations.

Further, the information on the Materials does not constitute “marketing or production and business activities in the PRC” as defined in the Administrative Measures on the Registration of Production and Operation Activities of Foreign Enterprises in the PRC promulgated by the State Administration of Industry and Commerce.

This publication has been provided for general information only. NAB has no licence for securities-related, derivative or other capital market products in China.