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Earlier this month, two new bond issues were announced and it may have come as a surprise to many that, for the first time, the wording 'unsecured' was included in the title of the new bond on offer.

On previous occasions, the terms 'secured', 'subordinated' or 'guaranteed' were sometimes used since these were distinct features of the bond on offer. However, the wording 'unsecured' which represents all bond issues that do not have some form of 'security' in place has never been included in the title.

Following the press release issued by Mariner Finance plc on June 4, a number of comments were posted online on *Times of Malta*, some of which clearly indicated the confusion among readers on what the 'unsecured' term implies. This prompted me to provide some clarification in this respect. I had already tackled this topic in 2008 and 2009. However, given the recent spate of new bond issues, which is expected to carry on throughout the second half of 2014, it is worth raising the topic again to assist investors in their decision-making.

What does the security aspect entail? The security normally takes the form of a hypothec in favour of bondholders on property held by the issuer or one of its subsidiaries. Few bond issues are secured. Normally, it is property development companies that are dependent on the sale of properties to finance the repayment of the bond that provide secured bonds to investors. Last month two bond issues by Pendergardens Developments plc were structured in this manner. Other companies that offer security in the form of a hypothec over a building or a piece of land they own, normally include those firms with a short track record or an erratic profitability record. Companies of this nature require such a feature to be included in the offering as an added assurance to prospective investors.

Apart from the two Pendergardens bonds, there are another three secured bond issues currently listed on the Malta Stock Exchange: Izola Bank plc, Medserv plc and Pavi Shopping Complex plc. In the past there were other issuers with secured bonds, but these have since all been redeemed. All other bonds currently listed and traded on the MSE are unsecured. Therefore, the majority of bonds are unsecured similar to the trend seen in overseas bond markets.

As such, the unsecured feature of some recent bond offers should not come as a surprise to potential investors, many of whom would have been invariably investing in unsecured bonds for several years.

While the 'security' hypothecated in favour of bondholders gives a certain degree of added comfort to investors, in my view, it is certainly not right to conclude that all unsecured bonds are riskier than secured ones. Although a hypothec is beneficial since it provides some additional reassurance to investors, the security will only come into play in case of the issuer defaulting on its obligations to bondholders. Irrespective of whether a bond on offer is secured or unsecured, investors should stay away from issuers whose business model and financial situation indicate a weak company as this may imply that it has a greater chance of defaulting.

The security feature will become relevant should the company find itself in a position where it is unable to honour its financial commitments including the interest and capital repayment to bondholders. If a company defaults, it will inevitably lead to a series of regulatory and legal procedures causing a lot of anxiety to investors. In such circumstances,

the release and subsequent sale of the security (normally property) in favour of bondholders will be marred by lengthy legal issues and other procedures which invariably take a long time to conclude.

As such, the security aspect should not be the most important attribute one must look into when analysing the attractiveness of a bond. The financial robustness of the company issuing the bonds and its ability to meet regular interest payments and final capital redemption is more important. The most common ratios for prospective bond investors to look into are the interest cover (showing the number of times a company's earnings before interest, tax, depreciation and amortisation exceeds its financial obligations) and the gearing ratio (the leverage of the company, i.e. the extent of borrowings compared to shareholders' funds).

Also, the historic track record of the issuer over an extended period of time is another very important consideration since it depicts the ability of the company to withstand changes in business sentiment and different economic cycles, amongst others. The recent prospectus of Mariner Finance plc provided the 10-year historical financial performance of their container terminal in Riga. The information provided in the financial analysis summary gives ample evidence that the company has a very strong track record in the management of the port facility and container terminal generating substantial profits and cash flows during the past 10 years even in the midst of the international financial crisis. In fact, the company achieved a net profit margin of over 40 per cent per annum in most of its 10-year track record and it is projected to register an interest cover of 4.2 times in 2015 - a very comfortable ratio by any standards.

Another term which often creates confusion among the community is the guarantee offered by some issuers. Since many bond issuers do not have any major assets within the company issuing the bonds, as their only purpose is to act as the financing arm of a group of companies (as is the case with Tumas Investments, Corinthia Finance, AX Investments and others), a guarantee is provided by the parent company to assume the issuer's obligations in case of default. As an example, in the recent bond issue by AX Investments plc which was guaranteed by AX Holdings Ltd, it is incorrect to assume that these bonds are safer than those of issuers which do not provide a guarantee. The AX Group could have also issued its bonds directly by the parent company AX Holdings, rather than using the finance vehicle. In such a case, the end result for bondholders would have been the same.

Apart from the differentiating characteristics of each bond, the pricing of a bond issue (i.e. the interest rate offered by the company issuing the bonds), naturally ranks highly among the important factors that impact an investor's decision on whether to participate in a bond issue. Pricing is a very subjective topic and could be debated at length. Investors should question whether the company/issuer is offering an adequate return to compensate them for the risks being undertaken. There are risks in all investments, even in those bonds issued by any government - whether the Malta government or other sovereign issuers which many Maltese investors may have gained exposure to in the past. As such, investors should review the issuer's financial situation or a country's economic fundamentals to gauge whether the rate offered is sufficient.

Some investors also seem to have been confused with the historical financial information available in the recent prospectus issued by Mariner Finance plc. The key figures were published as stipulated by Listing Rule 3.18 and Section 10 of the Registration Document published by Mariner Finance plc indicates that the full set of financial statements is available upon request. However, these do not provide any meaningful

information due to the recent change in the business operations of Mariner Finance. Some readers may have also failed to understand the reason for the publication of the 'pro forma consolidated financial statements'. This is explained by Deloitte Services as financial advisors to Mariner Finance plc. The report by Deloitte is available on the issuer's website [www.mfplc.com.mt](http://www.mfplc.com.mt).

Basically, pro-forma financial statements are drawn up to provide an indication on how a company or a group would have performed for the whole year following significant changes in its form or structure. In the case of Mariner Finance plc, the 2013 pro-forma financials were provided since the Mariner Group was restructured in the first few months of **2014**. Mariner Finance plc's role was changed from a special purpose vehicle entrusted solely with the raising of funds, to a holding company of two operating entities whilst still retaining the financing role. As such, this rendered the historical financial performance of Mariner Finance plc irrelevant as they do not reflect its current structure.

Furthermore, the Financial Analysis Summary appended to the Prospectus provides the 10-year historical performance of BCT. This is the main operating asset of the new Mariner Finance Group since it generates the large part of revenue. These are the figures that need to be analysed by prospective investors and the sponsor to this bond issue should be commended for the fact that although the Listing Rules do not require that financials for such a long period of time are published, a full 10 years of financials were provided. This very useful information indicates the strong profit and cash flow generation achieved by the terminal even in the midst of the international financial crisis.

Furthermore, although historical financial statements should play a large part in analysing an investment opportunity, prospective investors should also look into the projections of the future performance of a company since this will determine the ability of a company to honour its commitments.

The Financial Analysis Summary includes the estimates of Mariner Finance for 2014 and the projections for 2015. Moreover, the company's management informed financial intermediaries that by 2024, there should be excess cash of €28 million after the repayment of the bond issue. Admittedly, achieving one's financial projections over a 10-year period is no mean task, however, the projected cash buffer of €28 million is almost equivalent to the amount of bonds to be issued and as such provides ample cushion in the event of any potential business setbacks.

Financial journalism is still very much in its infancy. It is an area that needs particular attention given the sensitive nature of the topic and the increased participation by retail investors in the local financial market.

A growing and active bond market is a positive development for Malta's economy especially in the light of the Investment Registration Scheme launched last week and the indication by the Minister of Finance also last Sunday that two private pension schemes will be launched imminently.