

# Weekly Market Insight

## Kyle Lambert

Head of Trading

## Matt Macreadie

Credit Strategist

## James Shillington

Executive Director,  
Fixed Income NSW

## Scott Whitecross

Director,  
Fixed Income

Chart of the Week: High Yield Returns (USD) Over Last Five Years

Name	2021	2020	2019	2018	2017
<b>Actuals</b>					
Global High Yield	1,560.0	1,514.0	1,414.6	1,256.7	1,309.8
US Corporate High Yield	2,448.9	2,338.1	2,182.8	1,909.4	1,950.0
US B High Yield	1,960.8	1,884.6	1,801.9	1,569.6	1,590.5
US Ba High Yield	3,028.1	2,903.2	2,635.2	2,281.3	2,337.7
Pan-European High Yield	438.9	420.2	412.9	367.7	381.4
<b>YTD Return (%)</b>					
Global High Yield	3.0	7.0	12.6	-4.1	10.4
US Corporate High Yield	4.7	7.1	14.3	-2.1	7.5
US B High Yield	4.0	4.6	14.8	-1.3	6.5
US Ba High Yield	4.3	10.2	15.5	-2.4	7.3
Pan-European High Yield	4.5	1.8	12.3	-3.6	6.2
<b>Yield to Worst</b>					
Global High Yield	4.3	4.5	5.7	7.7	5.2
US Corporate High Yield	3.8	4.2	5.2	8.0	5.7
US B High Yield	4.2	4.4	5.1	8.0	5.7
US Ba High Yield	2.9	3.2	3.6	6.2	4.4
Pan-European High Yield	2.5	3.1	2.7	5.2	2.9

Source: Bloomberg

## Weekly Insights

- RBA Meeting: Bonds and Credit Yields Anchored Lower for Longer
- Suncorp (SUNPI), Macquarie (MBLPD), and WBC (WBCPK) AT1 Hybrids
- ElectraNet New Issue
- Reporting Season - Finale: What Caught Our Attention
- Weekly "Most" Traded

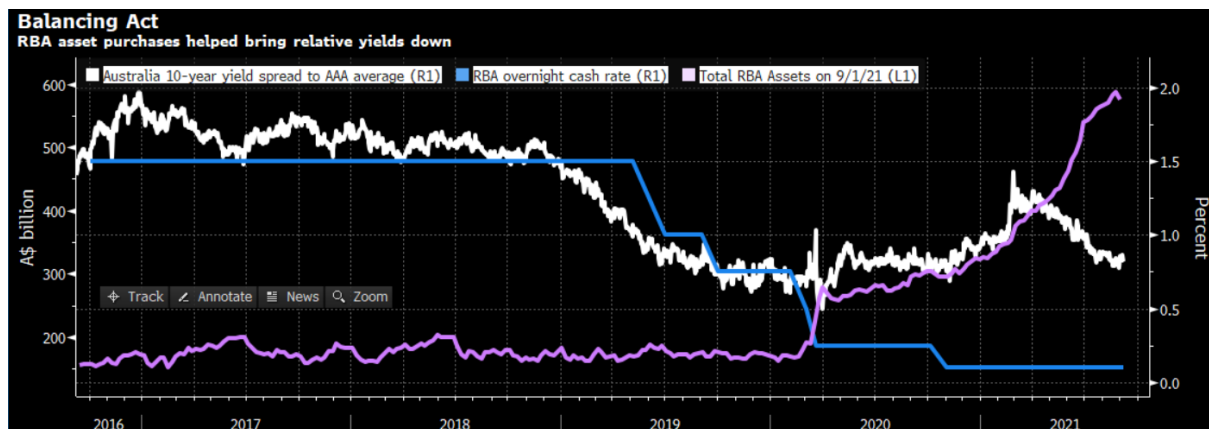
## Week in Review

- The Australian economy grew faster than expected last quarter, with GDP increasing by 0.7% QoQ vs economist estimates of 0.4%. The jump in output reflects Australia's strong recovery throughout the first half of the year as households boosted spending on the back of pent-up demand.
- Pacific National Finance returned to market last week, raising AUD400m via a 10-year fixed rate note paying 3.80% semi-annually. The deal was well received, as evidenced by a bookbuild more than two-times oversubscribed. The bond has traded actively since issue, reflecting the market's appetite for investment grade credit offering decent returns.

## RBA Meeting: Bonds and Credit Yields Anchored Lower for Longer

The RBA extended its AUD4bn weekly government bond buying program from November 2021 till mid-February 2022. The RBA had planned to review bond purchases in mid-November 2021, however an extension was required given a delay in the economic recovery and increasing uncertainty from the Delta variant of COVID-19. As expected, the RBA also maintained its key overnight cash interest rate at 0.1%.

Chart 1. RBA Asset Purchases Over 2020 and 2021



Source: Bloomberg

Governor Philip Lowe's actions to extend tapering indicate an ability to want to have flexibility if the economic impact from the Delta Variant is larger than expected. The RBA is not the only central bank taking a gradual and flexible approach.

*"The Board is committed to maintaining highly supportive monetary conditions to achieve a return to full employment in Australia and inflation consistent with the target. It will not increase the cash rate until actual inflation is sustainably within the 2 to 3 per cent target range. The central scenario for the economy is that this condition will not be met before 2024. Meeting this condition will require the labour market to be tight enough to generate wages growth that is materially higher than it is currently."*

– Reserve Bank of Australia (2021) [Statement by Philip Lowe, Governor: Monetary Policy Decision](#)

### IAM Capital Markets View

The extension of tapering from the RBA will help Australian bonds and credit yields remain anchored lower for longer. **For this reason, credit securities (both investment-grade and high-yield) could be an attractive income source in the near term.**

A government bond buying program of AUD5bn weekly with an expiry date of mid-November 2021 will see the RBA add around AUD60bn to its balance sheet. However, an AUD4bn weekly government bond buying program through till mid-February 2022 will see the RBA add around AUD70bn to its balance sheet. Governor Philip Lowe has pointed towards the stock of bonds accumulated as the key, so more overall purchases should mean lower Australian bond and credit yields.

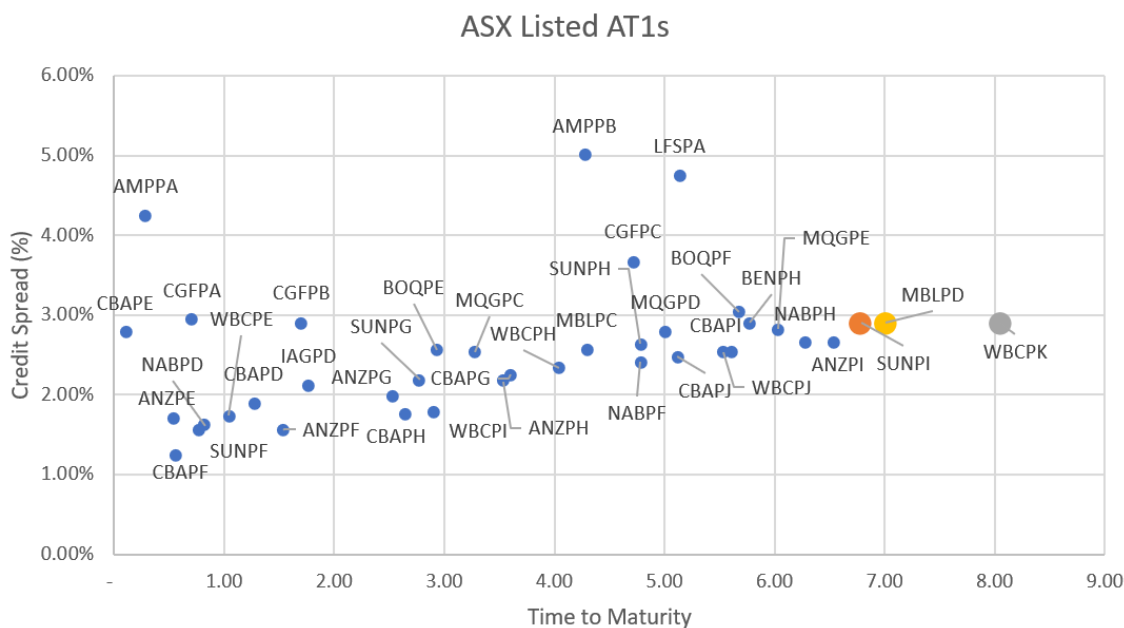
## Suncorp (SUNPI), Macquarie (MBLPD), and WBC (WBCPK) AT1 Hybrids

Suncorp (SUNPI), Macquarie (MBLPD), and WBC (WBCPK) all issued AT1 Hybrids over August 2021. The margin over 3m BBSW was set at 290bps (low end of price guidance) for all three issues. We classify Suncorp (SUNPI) and Macquarie (MBLPD) as both regional ASX-listed AT1s; however, the risk is very similar to the major banks at the lower end of the capital structure.

### The Investment Strategy

- Regional ASX-listed AT1s generally offer diversification outside the major bank AT1s, especially Suncorp (SUNPI), which has a general insurance and banking arm
- Regional banks have improved their common equity tier 1 (CET1) ratios, which is a positive for AT1 securities - as it increases the buffer above the 5.125% capital trigger
- Regional banks are not subject to total loss absorbing capital (TLAC) requirements, meaning their AT1 and T2 issuance will centre around upcoming maturities and will be less sporadic
- Point of non-viability (PONV) is unlikely to occur in practice as a regional bank would likely get swallowed up by a major bank prior to any conversion/write-down

Chart 2. ASX Listed AT1 Relative Value



Source: BondAdviser August 2021

## ElectraNet New Issue

ElectraNet (Baa2/Stable by Moody's) has hosted a deal roadshow for a 7.25-year AUD senior unsecured bond. Indicative price guidance is 140-145bps over semi-quarterly swap, which translates to a yield of around 2.55-2.60%.

### IAM Capital Markets View

ElectraNet owns and operates the sole electricity transmission network in South Australia. ElectraNet derives the bulk of its revenue (~80%) from activities regulated by the Australian Energy Regulator (AER). ElectraNet is also involved in unregulated activities (~20%), primarily the connection work of renewable projects to the main grid.

ElectraNet is owned by State Grid International Development Limited (~47%, A1/A/A+ [Moody's, S&P, Fitch]), YLT Power Investments Limited (~33%, unrated), and Australian Utilities Trust (~20%, unrated).

ElectraNet does have a large capex plan to support carbon transition in South Australia and the National Electricity Market more broadly. Such capex will be partially debt-funded. This capex, alongside Moody's expectations for lower regulatory returns in ElectraNet's next regulatory period from July 2023 (from prevailing low interest rate environment) will result in weakening financial leverage metrics.

In essence, Moody's expects funds from operations (FFO) to net debt to temporarily fall below 7%, but not for too long. The positive factor counterbalancing this is that shareholders have a strong commitment to a Baa2 rating and will likely exert their control to protect the credit profile if it were to be downgraded.

Chart 3. Financials and Credit Metrics

	ElectraNet Baa2 Stable	Ausgrid Baa1 Stable	Endeavour Energy Baa1 Stable	TransGrid [1] Baa2 Stable
(in AUD millions)	FYE Jun-21-22 (F)	FYE Jun-21-22 (F)	FYE Jun-21-22 (F)	FYE Jun-21-22 (F)
Revenue	\$390 - \$440	\$2,200 - \$2,300	\$1,380 - \$1,450	\$940 - \$990
EBITDA	\$270 - \$320	\$1,200 - \$1,300	\$710 - \$780	\$680 - \$720
Total Debt	\$2,400 - \$2,700	\$12,400 - \$12,600	\$6,100 - \$6,300	\$6,050 - \$6,210
FFO Interest Coverage	3.0x - 3.5x	2.8x - 3x	2.7x - 3.0x	2.5x-3.0x
RCF / Net Debt	4% - 6%	6% - 7.5%	5.7% - 6.3%	2.8% - 3.5%
FFO / Net Debt	7% - 8%	6% - 7.5%	7.0% - 7.5%	7% - 8%
Net Debt / RAB	85% - 90%	75% - 78%	80% - 83%	85% - 90%

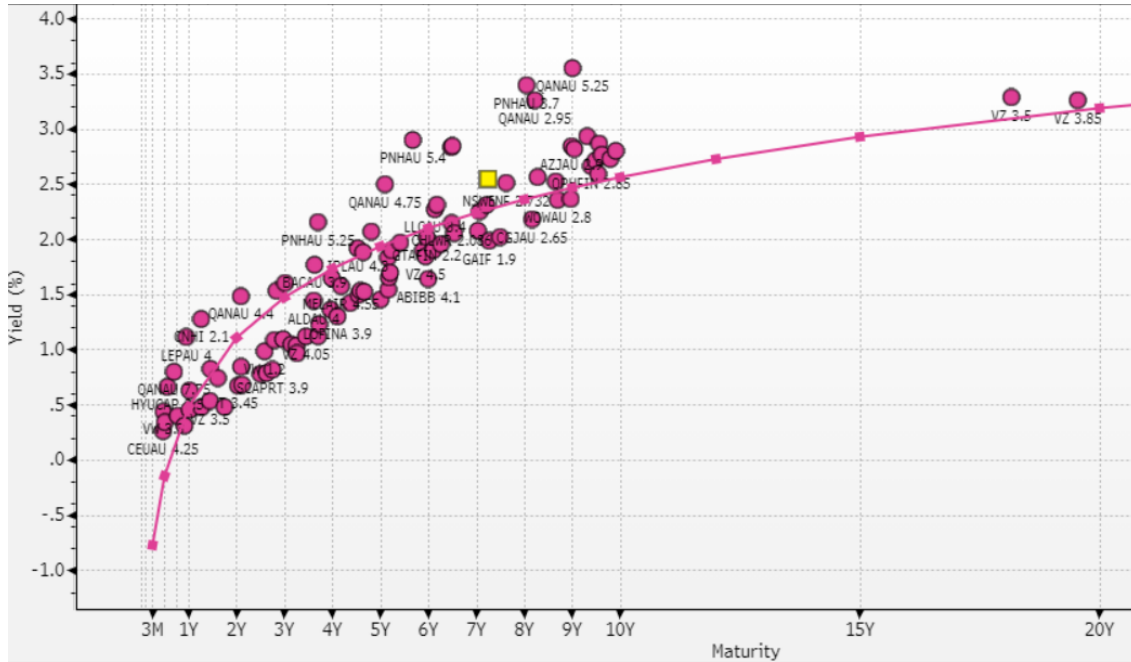
Source: Moody's

**Note:** TransGrid is rated as NSW Electricity Networks Finance Pty Ltd.

In our view, the best comparable is NSW Electricity Networks Finance Pty Ltd (TransGrid), which owns and operates similar electricity transmission networks in New South Wales, is rated Baa2 by Moody's, and has similar credit metrics (as seen above). ElectraNet does have a smaller scale (~AUD390m vs ~AUD940m) and a higher exposure to unregulated activities (~20% vs <10%) relative to NSW Electricity Networks - which may make it a marginally weaker credit.

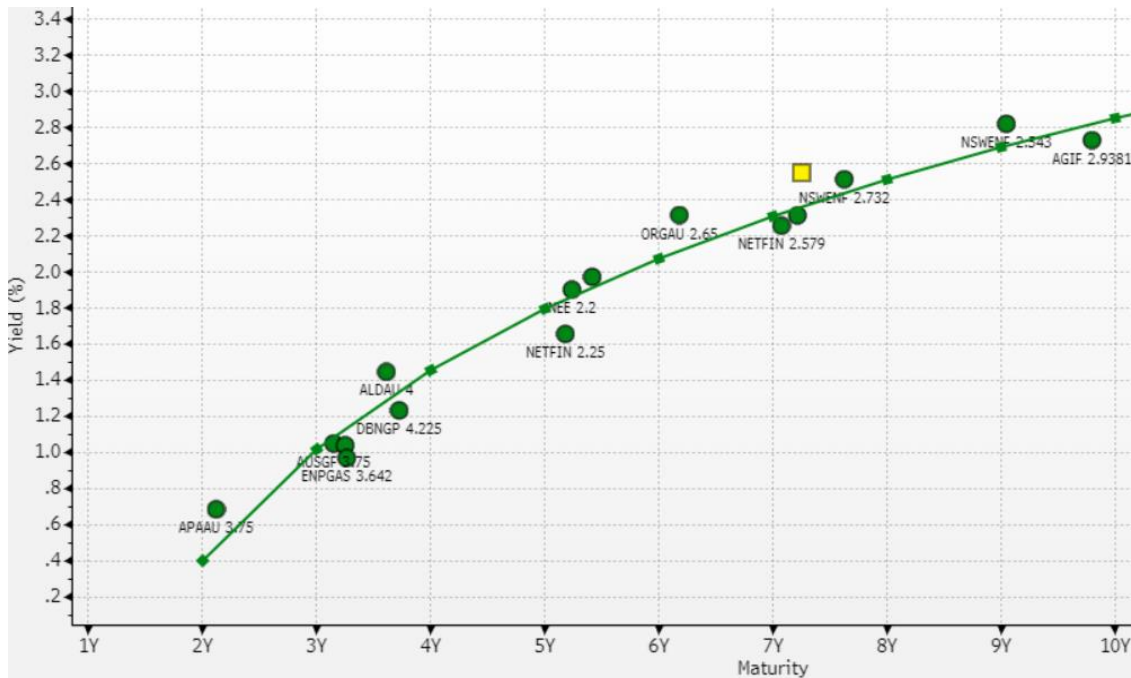
As a result, we believe ElectraNet should trade flat or slightly wider than the NSWENF 2.732 2029s. Thus, fair value for the new ElectraNet 7.25-year AUD senior unsecured bond should sit around 2.45%.

Chart 4. ElectraNet Relative Value vs BBB Corporate Curve



Source: Bloomberg

Chart 5. ElectraNet Relative Value vs BBB Utilities Curve



Source: Bloomberg

## Reporting Season – Finale: What Caught Our Attention

**Note:** Moody’s, S&P issuer ratings. In AUD unless otherwise stated.

Australian companies have finished reporting their FY21 earnings. Financial conditions remain accommodative with companies increasing M&A activities and shareholder returns. With interest rates at record lows, pressure will only start to build once we see a gradual increase in funding ratings. Most capital expenditure has been delayed or cancelled due to COVID-19, which has helped liquidity and cash buffers.

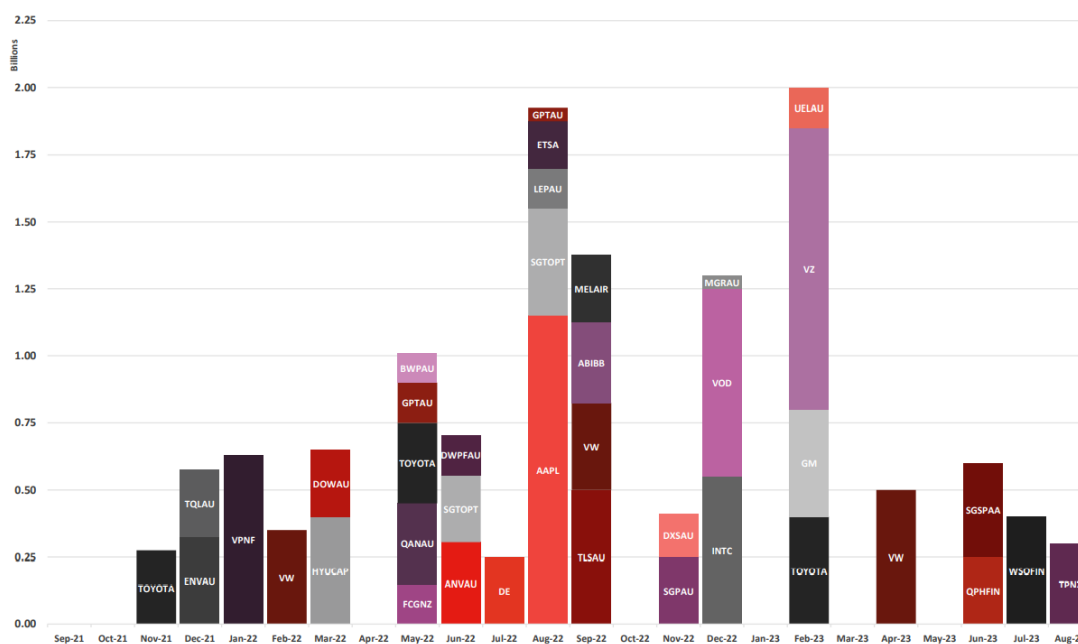
The FY22 outlook was relatively subdued from most companies. It is still unclear whether businesses and consumer confidence will rebound as quickly over FY22 – equivalent to a W-shaped recovery that many are expecting. The Delta variant remains infectious even among vaccinated people, so a reopening may not provide the growth impulse the market is seeking.

While not a new issue, the reporting season was highlighted by companies taking steps to manage their carbon exposure. Bondholders can play a big part in funding a cleaner Australia and an orderly transition into renewable energy. **For example, the new ElectraNet 7.25-year AUD senior unsecured bond.** ElectraNet has a large capex plan (partially debt-funded) which will support carbon transition in South Australia and the National Electricity Market more broadly.

We expect issuance to increase over the next couple of months as companies exit the blackout period. **Ampol, Telstra, GPT, Lendlease, and Wesfarmers** are some of the companies who have explicitly stated they will consider a capital market deal in the near term for refinancing or acquisition purposes.

Chart 6. AUD Upcoming Maturities

### A\$ Upcoming Maturities



Source: Bloomberg, Westpac

## Weekly “Most” Traded

The table below outlines our most frequently traded issues over the past week.

CCY	Issuer	Structure	Rating (Fitch, S&P, Moody's)	Cpn Type	Cpn	Call/Maturity	Yield
AUD	Pacific National Finance	Sr Unsecured	BBB-, BBB-, N/A	Fixed	3.800%	10-Jun-31	3.677%
AUD	Suncorp Group Ltd	Jr Subordinated	N/A, N/A, N/A	Floating	3m BBSW +2.900%	17-Jun-28	3.697%
GBP	Virgin Money UK Plc	Jr Subordinated	B, BB, N/A	Fixed	8.000%	08-Dec-22	2.459%
USD	Coburn Resources Pty Ltd	Secured	N/A, N/A, N/A	Fixed	12.000%	20-Dec-23	10.318%
USD	Westpac Banking Corp	Jr Subordinated	N/A, N/A, Baa1	Floating	6m USLIBOR +0.150%	30-Sep-21	11.457%
AUD	Liberty Financial Pty	Sr Unsecured	BBB-, N/A, N/A	Floating	3m BBSW +2.550%	25-May-26	2.918%
AUD	Dwpf Finance Pty Ltd	Sr Unsecured	A, N/A, N/A	Fixed	2.600%	04-May-32	2.573%
AUD	Members Equity Bank	Jr Subordinated	N/A, N/A, N/A	Floating	3m BBSW +5.000%	05-Dec-23	3.449%
AUD	BNK Banking	Subordinated	N/A, N/A, N/A	Floating	3m BBSW +5.400%	01-Feb-26	5.158%
USD	Citigroup Capital XIII	Jr Subordinated	BB+, BBB-, Baa3	Floating	3m USLIBOR +6.370%	07-Oct-21	5.400%

\*Priced to the IAM Capital Markets assumption of repayment.

## CONTACT US

If you need assistance or would like to speak with one of our IAM Capital Market specialists, don't hesitate to contact us. Our operating hours are 9:00am to 5:00pm weekdays (AEDT).

P: 1300 784 132

E: [clientservices@incomeam.com](mailto:clientservices@incomeam.com)

W: [www.incomeam.com](http://www.incomeam.com)

Sydney Office  
Level 5,  
66 Clarence Street,  
Sydney NSW 2000

**incomeam.com**

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