

# [Non-government bond issues essay](https://assignbuster.com/non-government-bond-issues-essay/)

[Finance](https://assignbuster.com/essay-subjects/finance/)

Non-government bond issues have increased over the past five years, both in importance and value of issuance. Bank lending is now addressed to households in the first place, than to businesses. However, businesses have shown an increasing tendency to accessing debt directly through capital markets. It seems that in 2004 non-intermediated debt accounted for 21 per cent of Australian businesses’ total debt, compared to 13 per cent accounted in 1999. the annual reports show that over the past five years the share of non-intermediated debt in the total debt of 350 largest listed Australian businesses, reaching around 40 per cent,[1] as shown in the table below: Table 1: Australian Businesses’ Sources of Debt Finances[2]June 1999June 2004Higher ratedLower ratedUnratedTotalHigher ratedLower ratedUnratedTotalNon-intermediated debt11. 411.

91. 024. 327. 522. 48. 958. 8Domestic bonds1. 50.

90. 32. 76. 13. 52. 512. 1- Unwrapped1. 50.

90. 32. 76.

12. 20. 08.

3- Credit wrapped0. 00. 00. 00. 00. 01.

42. 53. 9Offshore bonds9. 910. 20. 020. 119. 713.

42. 635. 8- Private placements1. 32. 50. 011. 52.

49. 32. 614.

3- Other8. 77. 70. 08. 717. 34.

10. 021. 4Hybrids0.

00. 80. 71. 51. 75. 53. 811. 0- Domestic0.

00. 30. 71. 11.

73. 13. 88. 6- Offshore0. 00. 40.

00. 40. 02. 40. 02. 4Intermediated debt34. 830.

446. 2111. 419. 533. 735.

388. 5Total46. 342. 247.

2135. 747. 056. 244. 2147. 4The table reveals the increased use of non-intermediated debt: domestic bonds’ share increased from 2 per cent to 8 per cent, offshore bonds’ share increased from 15 per cent to 24 per cent, hybrid securities’ share increased from 1 per cent to 7 per cent.

The decrease of intermediated debts’ level is more evident among higher-rated businesses. Over the past five years, 82 per cent of non-intermediated debt raised by lower-rated and unrated businesses was either credit wrapped, hybrids or issued in the US private placement market. In the Reserve Bank of Australia’s view the non-government bond market is divided in four categories: bonds issued by financial institutions, bonds issued by Australian corporations, asset-backed bonds and Australian dollar bonds issued in Australia by non-residents. As Mr. R. Battellino, the Assistant Governor (Financial Markets), shows in the RBA Bulletin in August 2004, the asset-backed bonds have rapidly grown over the past five years, reaching the value of over $60 billion (issued only in Australia), twice the size of the other categories of bonds that reach around $30 billion each.

The $60 billion value reached by the asset-backed securities issued in Australia is similar to the amount issued in offshore markets. It seems that domestic issues have been outgrown by offshore issues.[3]The Australian mortgage-backed marked has now reached international standards, according to Mr. R.

Battellino.[4] Even more, the Australian market is ranked fifth largest in the world, being outranked by the US, the UK, Spain and Italy markets. The greater part of these bonds is backed by residential mortgages. “ If we focus only on this segment, Australia ranks third, after the US and the UK”, also stated Battellino.[5] This is due to the increasing demand for residential mortgage finance in the recent years. Finance provided through mortgage-backed securities has increased twice as fast as mortgage finance provided through the balance sheet of financial intermediaries.

The main issuers of mortgage-backed securities are: mortgage originators (around $70 billion in 2004), NBFIs (around $30 billion in 2004), regional banks (around $25 billion in 2004), major banks (around $10 billion in 2004).[6]The most important issuers are mortgage originators. They have issued the largest amount of mortgage-backed securities.

In the mid 1990’s the competitive advantage banks had at the time reduced, due to the decrease of the general level of interest rates. This caused gaining a foothold in the market by mortgage originators by increasing low-cost retail deposits through their branch networks.[7]Regional banks are the second largest source of mortgage-backed securities. Their issuance is twice as large as the major banks’, although regional banks are smaller in size than major banks, but more active in this market segment. This is due to facing higher cost in funding their balance sheets. Also, as opposed to the major banks, for regional banks the relative costs favour securisation. However, major banks are more active in the offshore segment. Mortgage originators and regional banks face both the offshore and the domestic demand.

Credit unions and building societies are more active on the domestic market, as the value issued offshore is seven times higher than the value issued domestically. As concerns the buyers of mortgage-backed securities, more than half of the bonds  have been sold to foreigners, represented mostly by US dollar investors. Recently, the demand increased in Europe as well.[8]Securisations are used by banks and other deposit-taking financial institutions in order to manage their credit risk while continuing to maintain a relationship with the borrower, free up regulatory capital in order to use it more efficiently. In addition to this, securisations are also used in order to diversify their funding sources which leads to raising funds used for financing new lending.

[9]The credit-wrapped bonds are especially addressed to “ domestically focused, highly geared businesses with relatively stable cash flows”.[10] It seems that the increased use of credit-wrapped bonds conducted to an important concentration of credit risk in a small number of monocline insurers, AAA-rated. All the bonds issued by unrated businesses have been credit-wrapped. Domestic issuers of credit-wrapped bonds have also issued unwrapped bonds. Credit-wrapped securities have been issued by utilities, airports and infrastructure businesses. These businesses are more attractive than others to credit wrappers because they are likely to offer a high recovery rate in case a default should happen. In conclusion, Australian non-government bond issuance has significantly increased over the past five years, Australian businesses have raised debt from capital markets rather than from financial intermediaries, as to achieve non-intermediated finance. This growth supports financial stability.

References: 1. How Do Australian Businesses Raise Debt? Online version of the Financial Stability Review, March 2005, pp. 53-62http://www. rba. gov. au/PublicationsAndResearch/FinancialStabilityReview/Mar2005/Pdf/financial\_stability\_review\_0305. pdf2.

Asset Securisation in AustraliaOnline version of Financial Stability Review, September2004, pp. 48-56http://www. rba.

gov. au/PublicationsAndResearch/FinancialStabilityReview/Sep2004/Pdf/financial\_stability\_review\_0904. pdf3. Some Comments on SecurisationOnline version of Reserve Bank of Australia Bulletin, Aug. 2004, pp.

62-67http://www. rba. gov. au/PublicationsAndResearch/Bulletin/bu\_aug04/bu\_0804\_3. pdf[1] How Do Australian Businesses Raise Debt? Online version of the Financial Stability Review, March 2005, pg. 53http://www. rba. gov.

au/PublicationsAndResearch/FinancialStabilityReview/Mar2005/Pdf/financial\_stability\_review\_0305. pdf[2] How Do Australian Businesses Raise Debt? Online version of the Financial Stability Review, March 2005, pg. 54http://www. rba. gov.

au/PublicationsAndResearch/FinancialStabilityReview/Mar2005/Pdf/financial\_stability\_review\_0305. pdf[3] Some Comments on SecurisationOnline version of Reserve Bank of Australia Bulletin, Aug. 2004, pg. 62-63http://www. rba. gov. au/PublicationsAndResearch/Bulletin/bu\_aug04/bu\_0804\_3.

pdf[4]Some Comments on SecurisationOnline version of Reserve Bank of Australia Bulletin, Aug. 2004, pg. 64http://www. rba. gov.

au/PublicationsAndResearch/Bulletin/bu\_aug04/bu\_0804\_3. pdf[5] Some Comments on SecurisationOnline version of Reserve Bank of Australia Bulletin, Aug. 2004, pg. 65http://www.

rba. gov. au/PublicationsAndResearch/Bulletin/bu\_aug04/bu\_0804\_3. pdf[6] Some Comments on SecurisationOnline version of Reserve Bank of Australia Bulletin, Aug. 2004, pg. 63http://www. rba. gov.

au/PublicationsAndResearch/Bulletin/bu\_aug04/bu\_0804\_3. pdf[7] Some Comments on SecurisationOnline version of Reserve Bank of Australia Bulletin, Aug. 2004, pg. 64http://www. rba. gov.

au/PublicationsAndResearch/Bulletin/bu\_aug04/bu\_0804\_3. pdf[8] Asset Securisation in AustraliaOnline version of Financial Stability Review, September2004, pg. 49http://www. rba. gov. au/PublicationsAndResearch/FinancialStabilityReview/Sep2004/Pdf/financial\_stability\_review\_0904.

pdf[9] Asset Securisation in AustraliaOnline version of Financial Stability Review, September2004, pg. 49http://www. rba. gov. au/PublicationsAndResearch/FinancialStabilityReview/Sep2004/Pdf/financial\_stability\_review\_0904. pdf[10] How Do Australian Businesses Raise Debt? Online version of the Financial Stability Review, March 2005, pg. 56http://www. rba. gov. au/PublicationsAndResearch/FinancialStabilityReview/Mar2005/Pdf/financial\_stability\_review\_0305. pdf