BondIncome.

June 2021

Weekly Market Insights

Markets	Today	Weekly Change
Australian Dollar	0.7566	0.16%
ASX 200	7307	0.18%
Dow Jones	34238	1.08%
3-month AUD Bank Bill Swap Rate	0.03%	-
3 Year AUD Govt Bond	0.42%	-0.06%
10 Year AUD Govt Bond	1.53%	-0.05%
Aus iTraxx S35	57.50	-1.5

This week's insights

- Treasury Management Service – Three expert businesses. One complete solution.
- BondIncome (ANZ) Cash Management Account.
- BondIncome High-Yield Review (FY 2020-21).
- BondIncome Investment-Grade Review (FY 2020-21).
- GBP: Shawbrook Group AT1.
- EOFY Reporting Update.

Week in review

- Economists predict the RBA may have to lift interest rates sooner than it expects. CBA expects a15bps rise in November 2022, while WBC predicts the central bank will likely raise the cash rate by 15 basis points in the first quarter of 2023.
- The AUD High Yield (HY) market warmly welcomed the Emeco senior secured $250mm transaction with secondary buying swiftly driving the price up $101.50. The total demand in primary was greater than $380mm, representing one of the largest AUD HY book builds since the now redeemed NEXTDC 2022 FRN. The notes priced with a fixed coupon of 6.25%, payable semi-annually, have a maturity date of July 10, 2026. The proceeds of the offer will be used to fully repay the outstanding 9.25% March 2024 U.S. notes and related hedges.
- MoneyMe equity continues to outperform. The stock has risen a mammoth 56.72% from its early May low of $1.34, to Friday's high of $2.10. The Company market cap is now $360mm. The MMEAU debt pieces, the 8.25% 2025 corporate secured bond, and the MMEAU +675bps Dec-21 (call) warehouse notes, continue to show very attractive risk/reward metrics.

Treasury Management Service – Three expert businesses. One complete solution.

Treasury Management Service (TMS) is a comprehensive solution for managing and optimising your cash management, liquidity and income investment strategy. A partnership of three specialist businesses, Cashwerkz, Fortlake Asset Management and Tactical Global Management, TMS combines a suite of innovative services to help plan, implement and manage cash, income investments and currency exposures.

Key highlights of the service include:

- Cross product functionality.
- Relationship management.
- Funding management.
- Real-time portfolio management.
- Compliance and risk management.
- Operations and finance support.

For investors in the Aged Care, Religious Charitable Fund, Council and Family Office sector, we believe TMS is a compelling alternative to in-house treasury management.

For more information on TMS please contact your BondIncome representative.

BondIncome (ANZ) Cash Management Account

As per last week's note, we have partnered with ANZ to launch the BondIncome CMA. This is an at-call account held at ANZ and operated by BondIncome. Early customer feedback is positive with several accounts established last week: the service is available now and accepting funds. More information can be found at https://bondincome.com.au/cma/

BondIncome High-Yield Review (FY 2020-21)

As BondIncome's inaugural financial year ends, it provides an opportunity to reflect on the number and performance of the debt transactions the desk solely arranged or supported strongly via cornerstone interest, or as a significant volume investor. Supported by the team at Acacia Partners, BI was the sole lead and distributor across five transactions. Of most significance and proudly innovative was the MoneyMe corporate secured 8.25% April-2025. This deal was a landmark transaction for both the Australian Fixed Income Market and the MME business. The arrangement, a secured holding company lend, was the first for the fintech/nonbank sector and corresponding market capitalisation. Moreover, establishing the bond program has firmly signalled MME's transition from a small-cap to a mid-cap, operationally mature business. The team was proud to play a small part in facilitating MME's pivot into the innovative Autopay product, a venture well supported by equity investors, reflected in the 71% share price increase from $1.34 in early May-2021 to $2.29 today.

The desk also firmly backed four private debt or high yield transactions as a lead investor or investor of a large scale compared to the overall deal size. Of the transactions supported, the Bennelong Funds Management holding company secured note was a highlight and the best performing asset in our high-yield bond watch list. Current holders have benefited from an approximate 18% annualised IRR (on a mark-to-market basis).

BI lead transactions:

- November 2020, $7mm APMF Blacktown 7.25% 13/11/2021 (mortgage secured land bank).
- December 2020, $15mm APMF Bonnie Brook 7% 15/07/2022 (mortgage secured land bank).
- March 2021, $15mm MoneyMe 2018 Horizon Warehouse increase.
- April 2021, $15mm 4yr MoneyMe 8.25% Secured (HOLD-CO) – a market first for the sector.
- May 2021, BNK Bank BBSW+5.40% 1/05/2031 subordinated note.

BI cornerstone and/or significant investor:

- October 2020, Bennelong Funds Management senior secured 10% 22/10/2023.
- April 2021, NAOS, NCCGA 4.50% 30/09/2028 convertible.
- May 2021, Mercantile Investment Company 4.80% 26/06/2026 unsecured note.
- June 2021, Emeco Pty Limited, senior secured 6.25% 10/07/2026.

The team at BondIncome are looking forward to offering investors several exclusive primary market opportunities in the 2021-22 financial year.

BondIncome Investment-Grade Review (FY 2020-21)

The investment-grade market has been buoyant over financial year 2020-21 led by a resurgence in corporate issuance. The economic recovery took place and companies wanting to issue in financial year 2019-2020 took advantage of better funding and execution conditions. In June 2021, Wesfarmers issued their inaugural Sustainability-Linked bond with the aim to increase the use of renewable energy in its retail divisions. This was hot off the heels of Lendlease's Green bond in March 2021. It was also the return of corporate hybrids to the fixed income suite, with deals from Ausnet, Ampol and Scentre to name a few. Hybrids reflect an important part of a company's long-term capital stack and these securities offered attractive yields for BBB-equivalent rated names.

Westpac was the first major Australian bank to issue a senior unsecured deal post-COVID raising USD2.75bn from the US market. The major Australian banks have sourced regular funding from the Term Funding Facility (TFF) so have been relatively dormant from the AUD market since financial year 2019-2020.

The desk also firmly backed four investment-grade transactions as a lead investor or investor of a large scale compared to the overall deal size. Of the transactions supported, the Ampol 60NC5.25 corporate hybrid was a highlight and the best performing asset in our investment-grade bond watch list. Current holders have benefited from an approximate 9% annualised IRR (on a mark-to-market basis).

BI cornerstone and/or significant investor:

- November 2020, Ampol 60NC5.25 corporate hybrid BBSW+360bps.
- March 2021, Westconnex senior secured 3.15% 31/03/2031.
- June 2021, NBN Co, senior unsecured 2.15% 02/06/2028.
- June 2021, Lendlease Trust, senior unsecured 2.85% 28/06/2030.

The team at BondIncome are looking forward to offering investors several exclusive primary market opportunities in the 2021-22 financial year.

GBP: Shawbrook Group AT1 – Matthew Macreadie

Shawbrook is a UK lending and savings challenger bank focused on business finance, property finance, consumer lending and savings. The bank is authorised by the PRA and regulated by the FCA, and the PRA is a member of the Financial Services Compensation Scheme. It's a Basel III AT1 instrument (GBP125mn). The trigger for permanent write down is when CET1 ratio drops below 7%. Coupons can be mandatorily deferred and are non-cumulative. Current fixed coupon of 7.875% resets to BPSW5 +6.752% from first call in 2022 (equates to around 7.5% based on current BPSW5).

The current CET1 ratio is 12.6% as at 31 Dec 2020, so the bank is a fair way off reaching a stage where write down would come into play. COVID-19 has impacted results as indicated by the cost of risk rising to 80bps – but in comparison, this is still well below other UK challenger banks where cost of risk rose 150-200bps. Cost of risk is just impairment losses as a % of average principal outstanding – and this level indicates that the credit underwriting standards have held up well and have been consistently applied across the loan book. The outlook for the UK economy has improved following the extension of the furlough scheme and the news on the approval and roll-out of the vaccine – should all-else-equal – cause a reduction in the cost of risk over 2021 and 2022.

Looking at 1Q 2021 trading results, there has been a positive movement in arrears, trending towards pre-pandemic levels following the wind-down of the payment holiday exercise. Capital and liquidity ratios remain significantly above regulatory requirements. Loan book growth of 5.4% to GBP7.5bn has retraced, driven by improving origination levels and demand from new-to-bank property finance and business customers. Stock cost of retail deposits has been managed down to 0.98% as of 1Q 2021. Return on tangible equity has been returned to 20% with IFRS 9 modelled macro-economic outlooks and weightings held consistent with those used at FY2020.

Key performance indicators

Definitions of all metrics set out in the table below are provided on page 246.

	2020	2019	Change
Assets and liabilities			
Loan book (£m)	**7,102.8**	6,781.7	4.7%
Average principal employed (£m)	**6,825.7**	6,372.6	7.1%
Customer deposits (£m)	**6,894.1**	6,109.4	12.8%
Wholesale funding (£m)	**1,020.3**	1,122.3	(9.1%)
Profitability			
Gross asset yield	**5.8%**	6.4%	(0.6%)
Liability yield	**(1.7%)**	(1.8%)	0.1%
Net interest margin	**4.1%**	4.6%	(0.5%)
Management expenses ratio	**(2.2%)**	(2.2%)	–
Stock cost of retail deposits	**1.2%**	1.7%	0.5%
Cost to income ratio	**53.6%**	48.5%	(5.1%)
Cost of risk	**(0.80%)**	(0.47%)	(0.33%)
Return on lending assets before tax	**1.1%**	1.9%	(0.8%)
Return on tangible equity	**8.0%**	15.7%	(7.7%)
Liquidity			
Liquidity coverage ratio	**229.7%**	274.5%	(44.8%)
Liquidity ratio	**21.0%**	19.1%	1.9%
Capital and leverage [3]			
Common Equity Tier 1 capital ratio	**12.6%**	12.0%	0.6%
Total Tier 1 capital ratio	**15.0%**	14.5%	0.5%
Total capital ratio	**16.8%**	16.4%	0.4%
Leverage ratio	**8.7%**	8.6%	0.1%
Risk-weighted assets (£m)	**5,271.7**	4,974.5	6.0%

Changes in ownership – IPO and Marlin takeover:

In April 2015, the Group completed a successful IPO with admission to the London Stock Exchange, raising £90 million of gross primary proceeds (£82 million net of costs) to support the Group's capital position and future growth.

On 31 March 2017, Marlin Bidco Limited ("Marlin"), a company owned jointly by funds managed and/or advised by Pollen Street Capital Limited and funds advised by BC Partners LLP, announced an offer to acquire the entire issued and to be issued ordinary share capital of the Issuer not already directly or indirectly owned by Marlin or its concert parties (as subsequently revised on 5 June 2017, the "Offer"). The Offer was declared unconditional in all respects on 7 July 2017 and, on 24 August 2017, the listing of the Issuer's ordinary shares on the London Stock Exchange was cancelled.

Marlin takeover

Marlin Bidco is a PE firm jointly owned by those 2 funds. After the final takeover offer was declared unconditional in 2017, Shawbrook was delisted and registered as a private company.

Contrary to the normal nature of PE (i.e., highly leveraged growth, bringing in a new management team, altering strategy), the setup by Marlin Bidco was a conservative one and bondholder friendly in many respects.

The strategy was built around Shawbrook benefitting from the support of new, long-term investors, and a return to private ownership.

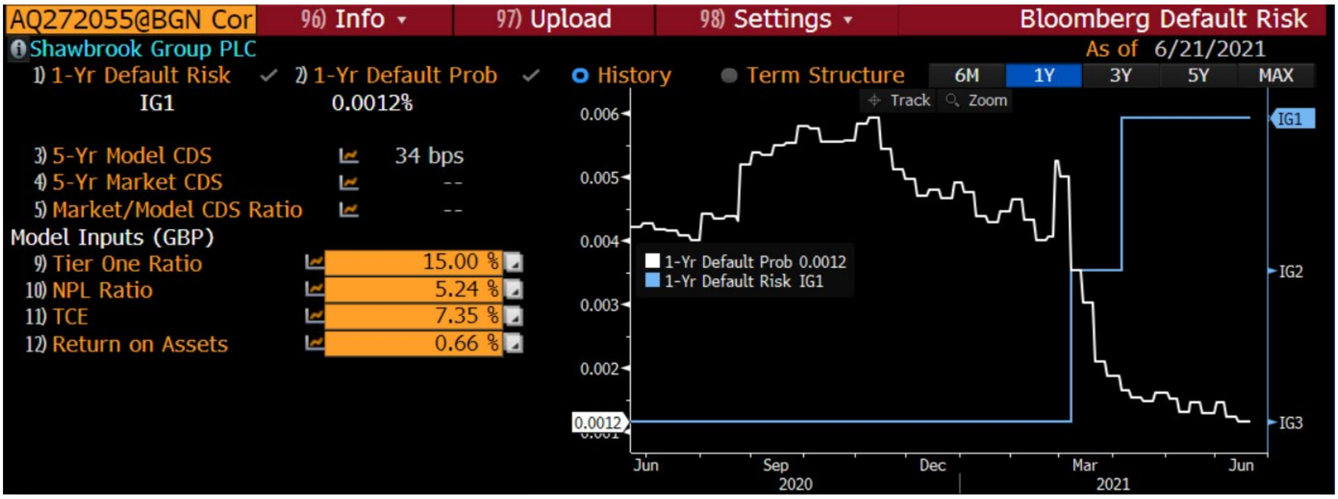
The creation of a more positive and supportive ownership structure would allow Shawbrook to adopt a more flexible approach to adapt to an uncertain economic environment with more conservative growth targets, and without the pressure to pay dividends, allowing the business to retain capital to enable it to grow safely.

Marlin Bidco kept existing management team and its strategy, focused on organic growth across its core segments of Property, Business Finance and Consumer lending.

The Group's strategy:

The Group's core strategy is primarily focused on providing specialist solutions to UK SME markets where the Issuer believes its deep expertise and established reputation for providing innovative products and services offers a truly differentiated proposition. Adopting traditional values with a modern delivery through the deployment of thoughtful funding solutions, the Group distinguishes itself by concentrating on those sectors where its expert knowledge, speed and flexibility offer a competitive advantage. The Group continues to invest for the future, increasing focus on digitalisation and automation to evolve its customer propositions and enhance operational efficiencies.

The Issuer believes that the maintenance of this strategy and business model will encourage continued growth in earnings and the provision of attractive risk-adjusted returns, while staying true to its risk management principles and creating long-term sustainable value for its stakeholders.



Issuer and security summary:

Shawbrook Perps would be equivalent to B rated banking risk. The 1Q 2021 trading results indicate strong financial and operating performance after what was a difficult 2020 with COVID-19 and UK lockdowns. However, with an improving UK economic backdrop, the bank should do well over 2021 and 2022 given their solid capital/liquidity ratios and specialised lending proposition. The bank is competing with the likes of Lloyds and Barclays but have been investing heavily in their digitisation agenda and significantly scaling up automation tools to ease customer journey, in-life management and portfolio analytics.

The Shawbrook 7.875% Perps have had a good run over 2020/2021 so a lot of the upside in the name is capped with the bonds now trading close to par. With the exception of another COVID-19 outbreak in the UK and widescale lockdown, I don't see this bank defaulting and should remain fairly steady all-else-equal.

Current offer:

Issuer	Shawbrook Group
Rating (S&P)	Unrated
Rank	AT1
Call Date	8/12/2022
Maturity Date	Nil
Issue Size	£125mm
Coupon	7.88%
If not called	5yr UK Swap + 6.752%
YTC	**8.42%**
YTM	
Running Yield	7.93%

The issue is available in a minimum face value investment of £200,000.00.

EOFY Reporting Update

As we head towards the end of another busy financial year the BondIncome client services team are busy preparing, in conjunction with Mainstream, EOFY reports for all investing clients. We expect to have reports distributed to investors by the 9th of July and will include:

- Holdings and valuations.
- Purchases/Sales and any Transfer's into/from your BondIncome custodial account.
- Income statements for coupon and maturity payments (per security).

As foreshadowed in our previous weekly notes, our development team are working to improve the delivery of our reporting to investors. We expect, over the coming months, to make these reports available via the client portal along with a host of portal enhancements.

CONTACT US

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

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