

Bankers hurt as deals dry up; 'Disorderly Market'

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Byline: Jonathan Ratner
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Investors aren't the only ones on a roller-coaster ride through volatile markets these days. With the delay of a number of initial public offerings, sharp declines for shares of newly public companies and a lack of liquidity in the credit market, investment bankers looking to raise money for companies have also been whipsawed by the turmoil.

"It's a disorderly market with forced sellers and no liquidity," said Christine Horoyski, head of fixed income at Aurion Capital Management. "It's been incredible how quickly this has hit."

While this is being felt most in the high-yield bond market, Ms. Horoyski thinks the majority of retail investors who were buying investment grade corporate bonds last year have also turned into sellers.

Despite the success of Tim Hortons Inc.'s first Canadian bond issue on Thursday, an oversubscribed private placement of seven-year notes yielding 4.20%, the deal was relatively small at just \$200-million.

It also came as Viterro Inc. was forced to delay the sale of as much as \$500-million in bonds "pending stabilization in global credit markets" due to unattractive yields. This, despite a well-received investor roadshow and a recent upgrade of the company's debt to investment grade by Standard & Poor's Inc.

Ms. Horoyski also noted that spreads on Canada mortgage bonds and provincial bonds widened after recent deals came to the market. "Bid-ask spreads have widened significantly -- another indicator of lower risk tolerance," she said. "People are very nervous."

Yields on U.S. junk bonds continue to rise sharply on concerns that efforts by European leaders to curb deficits will hamper the economic recovery-- putting them on pace for their first loss in 15 months.

Bank of America Merrill Lynch's global high-yield index showed that the percentage of corporate bonds yielding 10% or more jumped to 17% last week. Financing concerns stemming from the European debt crisis pushed the "distress ratio" up from 9.2% in April -- the biggest increase since November 2008.

"The risk contagion trade is global," Ms. Horoyski said.

"The back-up in credit spreads in high-yield really led the risk aversion trade throughout the credit

markets," she said.

As prices for junk bonds continue to fall and investors pull their money out of fixed income funds, Bloomberg data shows that at least 22 companies have postponed or withdrawn about US\$5-billion worth of debt sales in the past two weeks. Junk bond sales have also plunged in May to their lowest level since March 2009.

However, once the equity market stops selling off, Ms. Horoyski expects credit spreads to narrow. "If we stop seeing redemptions in high-yield funds and we see people buying them now that yields have backed up, the forced selling should stop," she said. "You have to look to the credit markets because they are probably an early indicator of stress and probably a good indicator of when risk is coming back. We feel risk is coming back to the marketplace in credits."

While Athabasca Oil Sands Corp.'s \$1.35-billion IPO was North America's largest such deal so far in 2010 and Canada's biggest since 1999, the Calgary-based oil-sands developer saw its shares fall to about \$10 from \$18 in early April.

Technology firms Lulu Ltd. and NetMotion Wireless Inc. pulled their equity offerings, ScotiaMocatta withdrew its physical copper fund IPO, and Porter Aviation Holdings Inc. had to delay and cut the price of its \$120-million IPO late last week.

Meanwhile, newly issued shares of Colombian oil developer C&C Energia Ltd. and Homburg Real Estate Investment Trust fell sharply when they first came to market last week, before quickly recovering.

"The fact that we're seeing a slew of IPOs coming to market is a positive sign," said Roman Dubczak, head of Canadian equity capital markets at CIBC World Markets

"When you've got market volatility like we've had in the last month or two, investors tend to become a little more discriminating."

While the income trust era saw IPOs move to the forefront, he noted that the majority of deals have been secondary offerings in the past three or four years. Since companies making secondary offerings already have a public track record, it's easier for the market to make a relative value assessment.

"Last year was remarkable from an equity-issuance perspective because of all the deleveraging of corporate balance sheets," Mr. Dubczak said,

referring to the shoring up of balance sheets in the face of a high degree of uncertainty.

As a result, there is less of a supply of new issuance this year. This was reflected in the most recent quarterly results from Canada's biggest banks, which cited a lull in underwriting revenue.

Yet Mr. Dubczak said this must be put into context: Canada saw about \$19-billion worth of new issuance in the fourth quarter of 2009 -- the biggest three-month period in several years. At \$11.2-billion, the second quarter of 2010 may have been one of the slowest in recent history, but he noted that things started to pick up for the banks in May, so their fiscal third quarter should turn out to be much stronger. At the same time, Mr. Dubczak pointed out that there remains a very deep pool of investable cash to potentially absorb new equity issues.

"It's a pretty healthy market," he said. "You get doses of volatility, which we've been experiencing, that kind of gets in the way. But I'm not telling anyone to hold back, you just have to watch the market for periods of time."

Mr. Dubczak said he has seen no slowdown in equity issuance and highlighted several large financings in recent weeks. Crescent Point Energy Corp. raised \$375-million in a bought deal; Just Energy Income Fund closed a \$330-million convertible debenture offering; Sun Life Financial Inc. completed a \$280-million preferred share sale; and Central Fund of Canada Ltd. increased its equity offering to US\$376-million.

"These are big deals, It's been quite choppy of late so deals may be pushed back a day or two just given extreme volatility, but they still do come to market and they still clear," Mr. Dubczak said. "Deals still get done, but obviously it's tougher execution."

jrattner@nationalpost.com
Uncertain markets prompted Porter Aviation Holdings

to delay and reprice its \$120-million initial public offering.