Experts Review

Experts Review: Capital Markets

Take it away, Lithuania!

This issue Experts Review focuses on Capital Markets, with articles presented in order of literacy rate in CEE according to the CIA World Factbook. Why literacy rates in a feature about Capital Markets? We have no idea!

Still, the facts behind this ordering do illustrate, once again, the high standard of education across the region. According to the CIA World Factbook, while the global literacy rate for all people aged 15 and over is 84.1%, only one of the 24 countries that make up this amazing part of the world has a literacy rate of below 95% (that's Kosovo, at 91.9%), and all the rest soar between 95.3% (Turkey) and 99.8% (Estonia and Latvia). Unfortunately, neither Estonia nor Latvia is represented in this issue – neither is Kosovo – so pride of place goes to Lithuania, at 99.7%.

As a result, following a featured interview with an expert on the status of Capital Markets in Austria, Christoph Moser, this issue's Experts Review Section will kick off with Lithuania.

Interview: Christoph Moser

Partner, Weber & Co on Austrian Capital Markets

Christopher Moser is a Partner with Weber & Co specializing in corporate finance, capital markets law, banking law, corporate law, and M&A. Prior to joining his current firm, Moser worked for Baker & McKenzie, Schoenherr, CMS, and Styria Borse Express.

The Capital Market In Austria

According to Christoph Moser, Partner at Weber & Co., when looked at from a general perspective the Austrian Capital Market tends to be weaker than that of Western European countries. In a conversation with CEE Legal Matters he pointed out out that while the Austrian Market fared considerably better in recent years than most CEE countries, a strong point of comparison for Vienna has always been the German Capital Market. The latter, Moser explained, "has registered considerable growth in recent years, a trend that, sadly, has not been followed by Vienna, especially on the ECM front where the general feeling is that we are in a weak phase these days." To illustrate, he pointed out that the one successful IPO in 2014 currently trades below its IPO price, while another planned IPO was aborted. "On the IPO front, the 2013/2014 period was weak with most potential players still waiting for the one large successful IPO to act as an icebreaker," Moser said. "Unfortunately, it never came."

In terms of prospects for the upcoming years, he said, there are "rumors circulating in the market" with regards to one potential high volume transaction in financial services and another revolving around an industrial company. Forced to speculate about which is more likely to come to fruition, he reluctantly pointed to the financial services one, but he emphasized that, at the moment, both are just rumors.

No One is Paying Premiums

When asked if he thinks that the lack of movement on the IPO front is caused more by economic conditions or by regulatory blocks, Moser suggested that the former was more to blame, but also highlighted the market structure as a potential obstacle. Specifically, he explained, many non-listed Austrian companies, including large players, are still family-owned or in the hands of private foundations. These types of agents tend only to take an IPO route if there is a prospect for good pricing. In light of a number of projects being dropped due to pricing, Moser reported, the optimism of the market simply isn't there.

This market structure also adds to the effect of new regulations. Moser explained. "Yes, there are some stricter rules in place for a few years now, and any company that is planning an IPO needs to know what this entails, including in terms of corporate governance and disclosure. With family-owned companies this requires a considerable adjustment both in terms of organizational culture and in terms of rebuilding their governance structure to match the public market's and regulators' expectations." He emphasized that this is "a minor point relative to the valuation that has been awarded in previous years, but it definitely does not help."

At the end of the day, according to the Weber & Co. Partner, the market and investors simply do not pay the premiums that they used to in the past, and without this, it is unlikely that we will see a lot of large IPOs in the near future. "The one hope is in niche players that are really ambitious and want to take their company public, but, overall, there are not many big ticket IPOs on my personal radar for 2015."

Where Are the Capital Holders?

According to Moser, the main investors in the Austrian market 4-5 years ago were from the US. Even further back, starting in 2002-2003 in particular, the market saw a lot of investors turning towards Austria as the gateway into the rest of CEE. "Many such investors felt that, because of the country's positioning, they would get CEE exposure if they invest in Austria," he said. "Unfortunately, the CEE fantasy has dried up for some years now and the market is mainly driven by continental European and some US and Asian investors."

As the Polish market did **(see page 34)**, the Austrian market enjoyed a flux of capital from pension funds a few years ago, but this too is no longer the case. Moser said that while there still is a strong pension-fund basis available in the market, it is not an overly active one – "definitely not like the ones we hear about in Norway or New Zealand for sure." Indeed, the only notable recent example of a pension fund investing in the market that he could point to was an Australian fund intending to invest in a minority stake in Flughafen Wien AG, the Viennese airport, but Moser believes that is a one-off example rather than a trend.

What's The Stopgap?

Since there are no big-ticket IPOs "just waiting to happen," what's keeping the firm and the market busy while everyone is waiting for that ice-breaker? According to Moser, while IPOs have yet to pan out in the market, "the situation with rights issues is quite different, with very large and very successful transactions taking place in the past years, primarily driven by financial institutions." He pointed to two transactions of Uniqa Insurance Group in 2012 and 2013 with high volumes, including a so-called re-IPO, and a large rights issue by Raiffeisen Bank International.

"Re-IPOs are a growing trend in the case of companies with one or two major shareholders and a low free-float. In such instances, a rights issue is combined with a notable secondary placement of shares from the major shareholders," Moser explained. According to him, they are primarily interesting if the shares of the companies are traded with low volumes and the free flow is small. In such case, a successful re-IPO may expose the stock to totally different investors. Moser was optimistic about this growing trend, stating that "if rights issues continue to come up in the next months as a growing trend, despite our relatively small size, as an experienced corporate finance law firm we're a notable market player and hopefully will play a role in them."

On top of that, the Weber & Co. Partner explained that DCM is one of their core practices, as well as securitizations – but "really, just like everyone else, we are all waiting for the next big equity deal."

Status of DCM in Vienna

According to Moser, 2012 to 2014 saw a lot of new bonds being issued, driven by low interest rates with "many companies managing their debts via bond issues as they expected interest rates to rise soon, which not yet happened." Since most bond issuers have, by now, collected the funds they needed, a slow down can be expected – but in terms of volume, Vienna is likely to register one of its strongest years as a result of Italian companies listing bonds in the market due to a regulatory loop-hole **(see Buzz Section – Austria – Issue 1.5.)**, which really is more of an anomaly than the norm. In terms of what Moser refers to as "the real market," he believes there should still be a steady deal flow with a considerable amount of bonds reaching their 4-5 year maturities and being subject to refinancing, which will likely lead to recurring transactions – at least as long as interests rates remain low.

A likely-to-increase set of transactions identified by Moser is in the secured bond market. The reason for this, he said, is that in a market where investors show almost no risk appetite, these (mortgage-) secured bonds, if sold in a conservative manner, tend to be perceived as a very safe and – as a result – popular investment, especially by pension funds and insurance companies. Moser explained that this was especially true for the latter in light of increasingly stricter rules on insurance companies in terms of their investments.

But Moser warned that "secured bonds might not always be as secured as they are advertised." He explained that some issuers try to market secured bonds with coupons of 7-8% (compared to other secured bonds' interest rates of 2.5-3.5%). The reason for the discrepancy is that many of these higher interest bonds are not directly secured or relate to real estate project developments, a situation which presents certain risks. According to Moser, it comes down to a "marketing question," and it is up to the intermediaries to ensure full disclosure, rather than simply "portraying it as a safe harbor investment."

Gazing Through the Regulatory Chrystal Ball

In terms of legislation, according to Moser, the market will continue following EU developments, especially in the banking and financial sector, where Austrian banks will of course face stricter capital requirements. Recently, Austria implemented the Alternative Investment Fund Managers Directive, which "has closed a lot of gaps in the unregulated funds scene but, as always, there are still problems related to implementing a European directive across various member states, which can become a problem in cross-border transactions." For example, one country – like Austria – may qualify an entity as an alternative investments fund, while the same entity may be expressly exempted from the AIFMD regime by another. It then becomes difficult to market such offers across different jurisdictions.

At the same time, the new Market Abuse regime will come into force in 2015. According to Moser, penal provisions in cases of market abuses will be introduced. This will likely affect the manner in which people act in a market where "it sometimes used to be treated as a gentleman's game of 'if I am caught' – pretty much like tax evasion."

All of the above considered, Moser's outlook on his firm's position in the market is optimistic. He concluded, "We have built up a small but strong team and our unique selling point – our strong track record as well as in particular our involvement in 70-80% of the transactions on the underwriters' side – will likely keep us busy in the upcoming period."

Radu Cotarcea