

FeBAF-VOEB event on “New Financial Instruments: the Experience of Schuldscheindarlehen in Germany and the Comparison with Mini-Bonds in Italy”

Background Document on Mini-bonds

I. Definition & Introduction

“Short or long-term debt securities issued by listed and or unlisted Italian companies on the securities market and subscribed by professional and qualified investors who offer a remuneration contractually established through the payment of coupons and the reimbursement of principal at maturity.”

Mini-bonds were first enshrined into Italian law by two subsequent Development Decrees in 2012 (Law Decree of 22nd June, nr. 83, with urgent measures for the country's growth and Law Decree of 18th October, nr. 179). These measures enabled SMEs to remove the main statutory and fiscal obstacles that effectively precluded them from issuing bonds in order to raise funds, thus depriving them from any real alternative to the traditional bank funding. Moreover, in the “Destination Italy Decree” of 2013 further measures to encourage the use of Mini-bonds by Italian companies and their distribution among investors were added. Specifically, 1) the access to collateral was made less onerous, 2) the issuance of secured bonds was facilitated, and 3) the establishment of specialized funds or securitization companies with the purpose of supporting the aggregation and professional selection of Mini-bond portfolios in order to stimulate the capital markets was encouraged. As a consequence, the conditions were created in order to structurally increase investments by channeling institutional players such as insurance companies and pension funds into this new asset class. Finally, some minor and additional improvements were introduced by the “Growth and Competitiveness Decree” in 2014 (Law Decree of 24th June 2014, n. 91).

II. Issuing Companies

In 2016, 88 companies issued Mini-bonds on the Italian securities market, compared to the 67 companies who issued Mini-bonds in 2015, thereby recording a substantial increase in the use of this debt instrument. In 2016, 47 companies were SMEs which accounted for 53,4% of the total issuing enterprises, compared to only 43,3% in 2015. Particularly, in 2016 there was an increase regarding the number of companies issuing Mini-bonds in Central Italy (from 11 to 19), while Lombardy with its 29 enterprises and the Veneto region with its 14 issuing companies continue to represent the front-runners. Overall, there are 222 enterprises which issued Mini-bonds between 2012 and 2016.

Among the main reasons for companies to issue Mini-bonds are the following:

- 1. Financing internal growth;*
- 2. Financing external growth;*
- 3. Restructuring the debt;*
- 4. Financing the operating cash of the company.*

III. Issues and Volumes

The number of Mini-bonds issued in 2016 increased to 106, of which 89 were under €50 million, compared to 85 during the previous year. However, 50% of total issuances were below the €5 million threshold. The total volume of Mini-bonds issued in 2016 reached €3,57 billion. Since 2012

there have been 292 Mini-bonds issued overall, of which 245 under €50 million. Compared to other countries, the volume of loans is still quite low, but the trend is definitively increasing.

Most Mini-bonds were listed on the ExtraMOT PRO platform, although some issues (20) have also been listed abroad (Germany, Ireland, Austria and Luxemburg).

The majority of companies issuing a Mini-bond (82) require a maturity date between 4 and 5 years, followed by 44 Mini-bonds with a maturity above 7 years, and 37 with maturity of just 1 year. The mean value increased (5.7 compared to 5.2 years in 2015) suggesting that companies rely on Mini-bonds to pursue long-term financing objectives, while also benefiting from a low-interest-rates environment.

The maturity date does not always coincide with the remuneration of the par value (bullet method), but it can also be remunerated using the amortization method. The bullet method was certainly the most used one (54,4% of the cases), especially for bigger issuances and for previously listed companies. However, in 2016 the use of the amortizing method increased, and was mostly used by SMEs issuing Mini-bonds below the €50 million threshold. The average duration of portfolios containing Mini-bonds is of 4 years as of January 1st 2017.

The remuneration of Mini-bonds occurs through a coupon payment which can be at either fixed or variable rate, but most issuing companies adopt a fixed coupon payment. Only 11,3% of cases showed a preference for a variable coupon rate.

As far as the rating is concerned, 61% of Mini-bonds do not have a rating in Italy. However, 12% of Mini-bonds issued received an ‘investment grade’ rating (which is almost equal to a BBB rating in the scale of S&P 500), while 10% had a ‘speculative grade’ rating.

As is the case also with other debt instruments, Mini-bonds can be either “callable”, “puttable”, or both. In 2016, 38% of Mini-bonds issued used both options, while 15% used neither option. Those companies who decided to adopt solely a “put” option were 68 (which amounts to 23% of the total volume), while those who went for solely a “call” option were 61 (21%). In addition, in 2016 there was an increase of the “call” option, while the decrease of both options and “only put” options were also recorded.

IV. The Actors

Normally, SMEs trust and seek the help of an advisor who will help the company in the process of choosing the main strategies and will sustain the link with the other subjects involved. We can also consider the legal consultants who will verify the legislation in force, the honesty of the procedures and the fulfilment of the contracts between the parties. The arranger, on the other hand, has the role of structuring the agreement and, on behalf of the company, he will connect with the potential investors. Even though the ratings are not strictly required, rating agencies can be involved. The Italian market is dominated by two main agencies: Cerved Rating Agency (16 ratings) and Crif Rating Agency (8 unsolicited ratings). Moody’s, S&P and Fitch operate only for issuances above €70 million. Currently, the legal framework in Italy allows the placement of Mini-bonds only to professional investors who are able to value the risk they undertake. Therefore, the traditional subscribers of Mini-bonds in Italy are: banks, insurances, brokerage companies, and pension funds.

V. Future Perspectives

The first half of 2016 did not present a meaningful progress, only during the second half, the development of mini-bonds was accomplished. In December 2016, 24 companies issued mini-bonds allowing for an optimistic view in 2017. SMEs adopt this instrument and consider it a step toward a greater managerial maturity of the enterprise. There is the perception that mini-bonds can serve as a source of financing more stable than bank loans, mostly for what concerns long-term financing.