Chapter 7
"An Analytical Approach to Investments, Finance and Credit"

Debt Markets: issuing Corporate Bonds 144As Private Placements

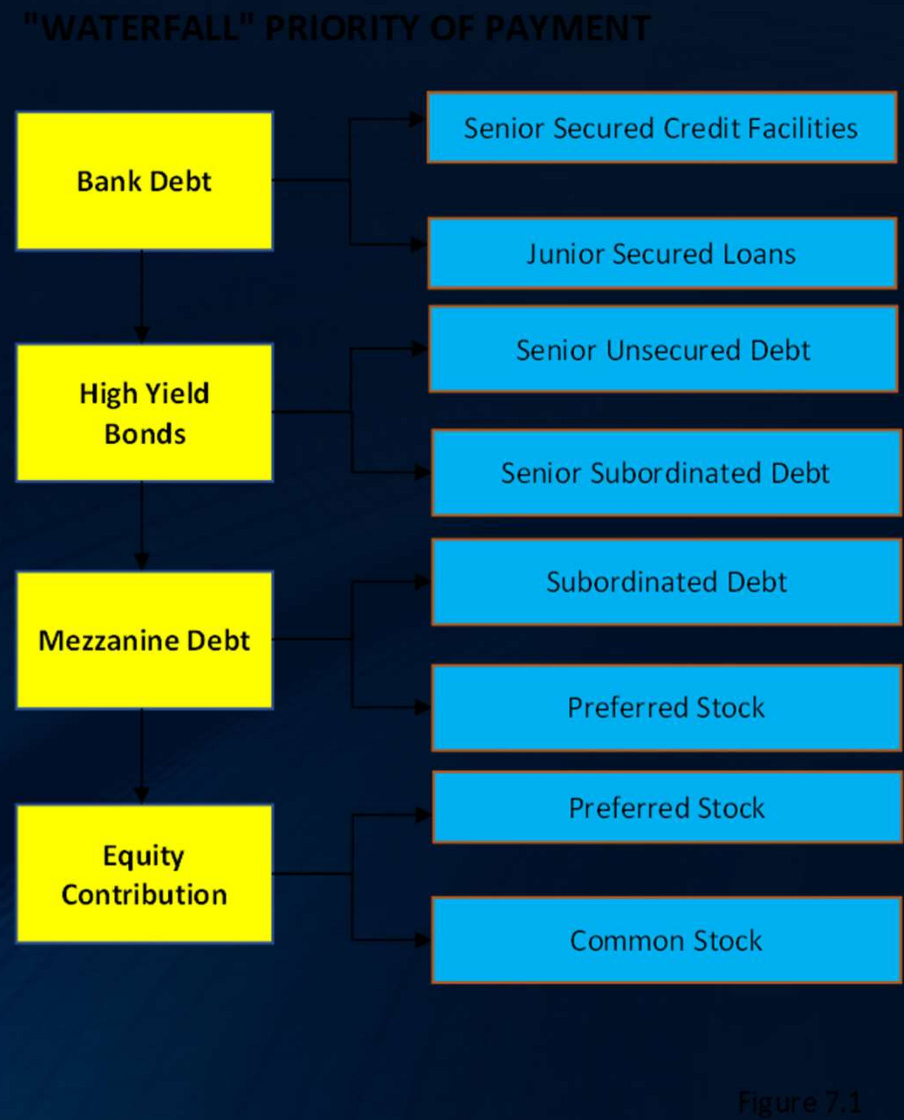
PROFESSOR C. DROUSSIOTIS

Corporate Debt: An Overview

- Corporate debt is by far one of the most prefer
- Raising debt ,in general, do not need to give up ownership and instead they signed a contract.
- The contract, called bond indenture or loan agreement, requires the company to pay back such debt in the future plus pre-determined interest payment which represents the cost of borrowing.
- Though debt is the preferred source of capital, is not always available.
- Debt holders are betting that the company has relatively strong income and cash flows to meet their debt obligations which include both interest and principal payments.
- In a bankruptcy, debt is viewed higher in the capital structure than stock

Corporate Debt: An Overview

"The Waterfall" or priority of payment, in a bankruptcy, bonds are viewed higher in the capital structure than stock.



Types of Corporate Debt

- **Unsecured Bonds**
- **Secured Bonds**
  - ***Mortgage bonds***
  - ***Collateral trust bonds***
  - ***Equipment trust obligations***
  - ***Guarantee bonds***
- **Convertible Bonds**
  - $\text{Conversion ratio} = \frac{\text{Par value}}{\text{Conversion price}},$
- **Zero Coupon Bonds**
- **Paid-In-Kind (PIK) Bonds**

Raising / Issuing Corporate Bonds

The companies issuing bonds in the public markets are required by the Securities and Exchange Commission (SEC) to be independently rated by at least two rating agencies before they are issued Secured Bonds

CORPORATE BOND RATING AGENCIES' SCALES

Description		Standard & Poor's	Moody's	Fitch
Highest Quality (Risk Free)	INVESTMENT GRADE	AAA	Aaa	AAA
High Quality		AA+ AA AA-	Aa1 Aa2 Aa3	AA+ AA AA-
Strong Payment Capacity		A+ A A-	A1 A2 A3	A+ A A-
Adequate Payment Capacity		BBB+ BBB BBB-	Baa1 Baa2 Baa3	BBB+ BBB BBB-
Likely to fullfill Obligations	NON-INVESTMENT GRADE (HIGH YEILD)	BB+ BB BB-	Ba1 Ba2 Ba3	BB+ BB BB-
High-risk Obligations		B+ B B-	B1 B2 B3	B+ B B-
Current Vulnarable to Default	DISTRESS	CCC+ CCC CCC- CC C	Caa	CCC
Default	**DEFAULT**	D	D	DDD,DD,D

Figure 7.2

Rating Agency Methodology

- **Industry Risk**
- **Company-Specific Business Risks**
- Management Factor
- **Financial Risk Analysis**
  - **Loan-to-value or debt capitalization ratio**
  - **Leverage ratio of debt to EBITDA**
  - **Coverage ratios, including EBITDA/interest and cash flow to debt service**
  - **Cash Flow Forecasting and Modeling**

Going to Market to Raise Corporate Bonds

- **Step I: Select the Investment Company/Underwriter**
  - **Firm Commitment**
  - **Best-Effort Commitment**
- **Step II: Preparing the Documents for the Bond Offering**
- Step III: SEC Registration and ApprovalThough debt is the preferred source of capital, is not always available.
- **Step IV: Marketing the Bond Offering**
- .Step V: Indication of Interest
- **Step VI: Closing, Funding, and Free to Trade**

Terms of the Bonds

- Money Terms
  - Amount
  - Interest
  - Maturity/Term
  - Principal Payment
- Non-Money
  - Financial Covenants
  - Negative Covenants
  - Afifrmative Covenants

Money Terms - Primary

- Amount Concepts
  - Face Value (Book Value) $1,000 per Bond – PAR AMOUNT 100
  - Redemption
    - Maturity 100
    - Earlier than Maturity (Call/Non-Call) at different prices
- Interest Rate / Coupon Rate
  - Fixed or Floating
  - Semi-Annual Payment (i.e. 8.0% Coupon pay $80 per year or $40 every six months)
- Maturity (anniversary of issuance)
- Principal Payments
  - Term Bond (0,0,0,0,100)
  - Serial Bond (20,20,20,20,20)
  - Balloon Bond (10,10,10,10, 60)

Pricing Bonds

- The initial pricing of bonds is guided primarily by demand and supply based on the rating. In setting up the coupon rate, which is the interest rate of cost of borrowing for the issuer, the investment advisor considers the following factors:
  - Risk Free Rate or AAA rated bonds which are used as the base
  - Inflation Price
  - Maturity Rate Price
  - Default Rate based on rating
  - Liquidity

$$Coupon\ Rate = Rfr + IP + MRP + DRP + LP$$

Term Sheet

THE OFFERING:

	Issuer	**Celerity Technology Inc.**
MONEY- TERMS	Notes Offered	$1,200,000,000 principal amount of 7.0% Senior Notes due 2029
	Coupon Rate	7.0%
	Maturity Dates	December 1, 2029
	Interest Payments	June 1 and December 1, beginning June 1, 2019 (Issuance Day)
NON-MONEY TERMS	Optional Redemption	The issuer may exercise the right to call the bonds to be redeemed all or part of the notes at any time before December 1, 2025 at a price based on the following redemption prices: Redeem on or before: December 1, 2020 105% of Principal Amount December 1, 2021 104% of Principal Amount December 1, 2022 103% of Principal Amount December 1, 2023 102% of Principal Amount December 1, 2024 101% of Principal Amount December 1, 2025 100% of Principal Amount
	Offer To Repurchase	If there is **change of control**, as defined in "Description of Notes – Definitions" the repurchase all or part of the notes will be available for purchase at price equal to 101% of their principal amount plus accrued and unpaid interest to the repurchase date. If we sell a portion, but less than all or substantially all, of our assets under certain circumstances, we will use the cash proceeds of such asset sale remaining after other permitted uses to offer to repurchase the notes at a price equal to 100% of their principal amount plus accrued and unpaid interest to the repurchase date. After a fall away event, as described below, these note repurchase obligations no longer apply.
	Permitted Spin-Off Transaction	The indenture governing the notes will permit a spin-off, split-up, split-off or other transaction involving the dividend, distribution or transfer by us of all or some portion of one or more of our business units. To make this dividend, distribution or transfer: •The company created by the spin-off must complete a registered exchange offer in which it offers holders of the notes the opportunity to exchange their notes for notes of the new company with terms substantially identical to those of the notes; •The company created by the spin-off must be able to incur at least $1.00 of additional debt pursuant to the fixed charge coverage ratio test set forth under "Description of Notes – Covenants – Incurrence of Indebtedness and Issuance of Preferred Stock" after giving pro forma effect to the spin-off transaction; •Each series of new notes issued in the exchange offer has ratings at least as high as the highest ratings given to the corresponding series of the notes in the one-year period immediately prior to the consummation of the spin-off transaction; •Immediately after such transaction, no default or event of default exists; •The company created by the spin-off assumes all obligations of the Company under the notes and the indenture pursuant to agreements reasonably satisfactory to the trustee, whereupon the company's obligation in respect to the notes exchanged for such notes of the new company shall be fully satisfied and discharged; and •We must offer to repurchase all of the notes at a price equal to 100% of the principal amount of the notes plus accrued and unpaid interest to the repurchase date.
	Covenants	Unless and until the notes receive an investment grade rating from two or more nationally recognized statistical rating organizations and other conditions are satisfied, which we refer to as a fall away event, the indenture will, among other things, limit our ability and the ability of our restricted subsidiaries to: •Pay dividends on our stock or repurchase our stock; •Make investments; •Borrow money and issue preferred stock; •Create liens; •Restrict the ability of our restricted subsidiaries to pay dividends or make other transfers to us; •Consolidate or merge with another person or sell all or substantially all of our assets and our restricted subsidiaries' assets to another person; •Engage in certain transactions with affiliates; •Enter into sale and leaseback transactions; and •Expand into unrelated businesses.
	Use of Proceeds	We intend to use the net proceeds of this offering to repay borrowings under our revolving credit agreement, to provide cash necessary for the transaction and for other general corporate purposes.

Figure 7.3