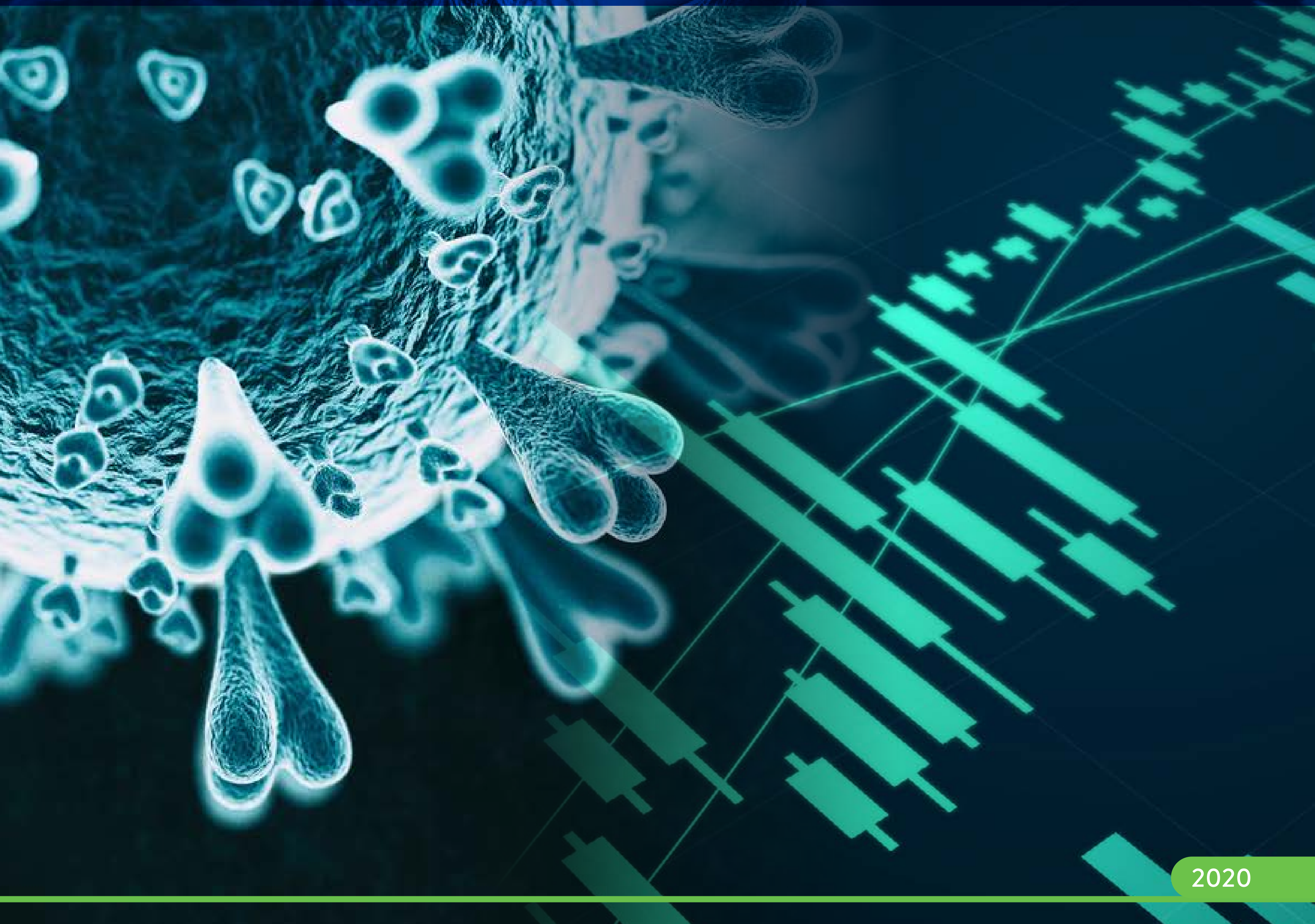
GILBERT
+TOBIN

RAISING CAPITAL IN THE AGE OF CORONAVIRUS

Key considerations for issuers and underwriters and lessons from the GFC



2020

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INTRODUCTION

For some, the share market plunges, earnings downgrades and requests for government bailouts of the past few weeks are reminiscent of the uncertainty of the 2007-2009 global financial crisis (**GFC**).

However, as governments around the world continue to adopt unprecedented mitigation measures, such as closing borders, implementing travel bans and ordering the closure of businesses and workplaces, concerns that the economic cost of coronavirus (**COVID-19**) will exceed that of the GFC are becoming more widespread. This is particularly the case for Australia, which managed to avoid a recession during the GFC and kept unemployment levels below 6% during that period.

The impact of COVID-19 on Australia's economy means that many entities will need to assess all available means of accessing funding to alleviate the brunt of a cash flow squeeze resulting from declining sales and operational closures. We expect it will drive many entities to need cash injections – in some cases, urgently.

The most immediate question now is whether Australia's public equity markets will respond to bridge this period of halted revenues like they did to repair balance sheets during the GFC. As this paper shows, comparisons to the GFC are not perfect and the circumstances here are very different. The ongoing uncertainty about the duration of COVID-19 and therefore the extent of its impact on revenues is the big question boards everywhere are facing.

This paper is intended to assist listed entities, and their directors, as well as all participants in equity capital markets (**ECM**) transactions from lead managers / underwriters, fund managers, securityholders and other investors navigate the many legal considerations that arise in the context of capital raisings undertaken during periods of prolonged market and economic uncertainty.

We hope that you find this paper useful. G+T has one of Australia's leading ECM teams, having advised on more ECM transactions in the past 5 years than any other law firm, and we have extensive experience assisting both issuers (and their boards) and lead managers / underwriters on complex and challenging capital markets transactions.

A NOTE ABOUT OUR METHODOLOGY

We have based on our analysis on publicly available data for all equity or equity-like capital raisings which were announced between 1 August 2007 and 31 December 2009 and which were to raise amounts of A$100 million or greater. This covers institutional and other placements, rights offers, security purchase plans (**SPPs**), distribution reinvestment plans (**DRPs**) as well as issues of convertible securities and bonds.

2 KEY TAKEAWAYS

AN INCREASE IN EQUITY CAPITAL MARKETS DEALS – BUT WILL THE MARKET BE ABLE TO RESPOND?

As more businesses are forced to temporarily close or reduce operations in response to governmental and voluntary controls imposed to manage COVID-19, many will face a cash flow squeeze in the short to medium term. What we are currently seeing is a number of entities drawing down their headroom under existing debt facilities and reducing discretionary capital expenditure and any other non-fixed costs. Within the next few months, and depending on the levels of cash burnout, we expect that some will be required to undertake equity capital raisings (and some even sooner than that – as is already occurring – whether due to an immediate cash flow shortfall or prudent capital management). This will result in a substantial increase in equity capital markets activity and the key immediate question is whether the market will facilitate this like it did during the GFC.

GOVERNMENT SUPPORT MAY MEAN EQUITY MARKETS AREN'T DOING THIS ALONE – BUT WILL PROVIDE A BASIS FOR FURTHER EQUITY RAISINGS DOWN THE TRACK AS WELL:

There are some significant differences between COVID-19 and the circumstances which led to the GFC which may affect the role the public equity capital markets have to play. For example, we are seeing more targeted financial responses from Australian governments than we saw during the GFC and "bailouts" or other forms of financial support will also do some of the heavy lifting in the short term for entities most severely affected. For support provided in the form of debt, recipients may need to raise equity in the future to repay that debt.

EXPECT TO SEE A LOT MORE INSTITUTIONAL PLACEMENTS:

In the short term, raising structures with short risk periods for underwriters will be preferred: institutional placements (with non-underwritten SPPs to manage dilution of retail holders). Entities that have experienced a massive reduction in their share price, or who have limited headroom in their placement capacity or who will rely on major shareholders to backstop capital raisings will need to turn to rights offers instead – as with the case in the GFC, in times of uncertainty, non-renounceable structures will offer the greatest chance of success as underwriting in this market will be challenging for the immediate future.

CHALLENGING DISCLOSURE ISSUES WILL NEED TO BE MANAGED:

The unique nature of COVID-19 and the difficulties in forecasting its impact (both on individual entities and the economy as a whole), present difficult disclosure issues that need to be managed carefully – what can be said about future prospects or even whether the cash that is being raised will be enough when there remains uncertainty about not only the impact of COVID-19 on an entity's customers, suppliers or in many cases, both but also the duration of that impact?

MANY ENTITIES MAY NEED TO BE TAKEN PRIVATE, OR ELSE CEDE CONTROL TO A SUPPORTIVE INVESTOR TO SURVIVE:

Too much uncertainty around the impact of COVID-19 on a particular entity may make raising equity practically impossible and where such entities are not able to hold until there is more clarity of when the virus has peaked may need to look at more unconventional means of survival – in some cases, recapitalisations that result in a change in control or the acquiring of a substantial stake in the entity. That being said, we expect that where the underlying businesses remains fundamentally sound underwriting will be available.

LOTS FOR BOARDS TO CONSIDER:

Liquidity is key and ensuring balance sheet stability for the next 12-18 months is prudent, given the uncertainty about how long the measures to manage COVID-19 will last. Key issues when raising equity capital include quantum, speed and certainty, pricing, identification of issues and appropriate disclosure of those to investors (and implementation of appropriate due diligence processes to identify and manage those issues) as well as allocations (and maintaining register quality) and control implications.

ISSUES FOR UNDERWRITERS TOO:

leaving aside the commercial complexity of underwriting in this market, we expect underwriters will be looking closely at the balance of risk between themselves and issuers in their underwriting agreements, working out how to effectively use bookbuild messaging to manage investors in choppy markets in the new "norm" of heavy regulatory scrutiny of those practices and thinking hard about how to satisfy internal risk committees about the adequacy of diligence processes adopted by issuers (and the underwriters themselves) and offering disclosure. Reputational risks will also be important.

We live in interesting times. Companies, directors, underwriters, investors and regulators will need to improve and adapt in order to overcome the financial uncertainty ahead. In the age of COVID-19, listed entities should be prepared to raise capital and be able to move swiftly and decisively when required to do so.

3 SOME CONTEXT: BE CAREFUL WITH COMPARISONS TO 2009 AS IT'S NOT THE GFC ALL OVER AGAIN

Comparisons to the period of extreme market dislocation which we saw in the GFC are superficially attractive: March 2020 has seen 3 of the 10 largest single day share market falls since the 1987 share market collapse (including the second largest single day fall ever) and from its peak of 7,237.4 points on 20 February 2020, the ASX All Ordinaries Index had fallen by approximately one-third to 4,854.3 points by 20 March 2020. Although not as large as the percentage declines seen during the GFC (~54% from late 2007 to early 2009) or the 1987 "Black Monday" share market crash (~50%), the velocity of the fall has been astounding (see Figure 3) and Australian and global equity markets remain highly volatile (the volatility index, VIX, jumped 43% on 16 March to close at 82.69 points - its highest level ever) and very few, if any, people are confident of how much further the correction may have to run.

Figure 1: Ten largest single-day falls in the All Ords since 1987.

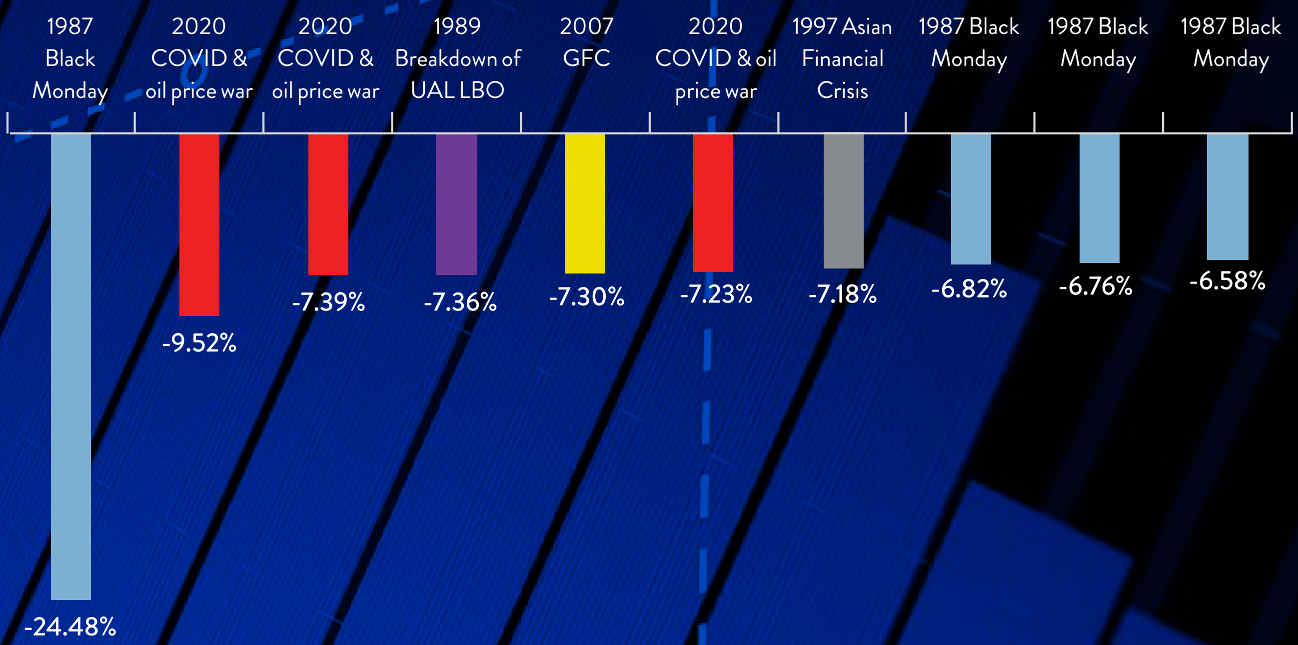


Figure 2: Historical falls in ASX All Ords Index

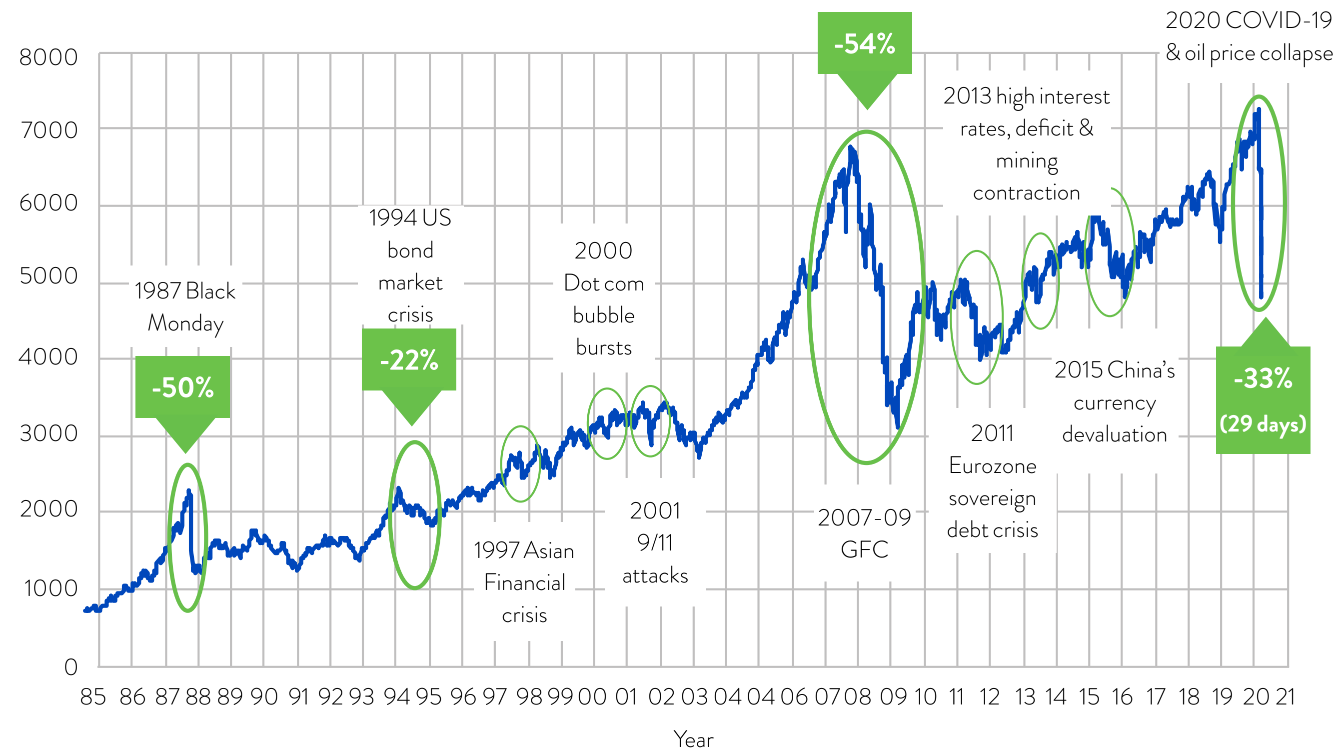
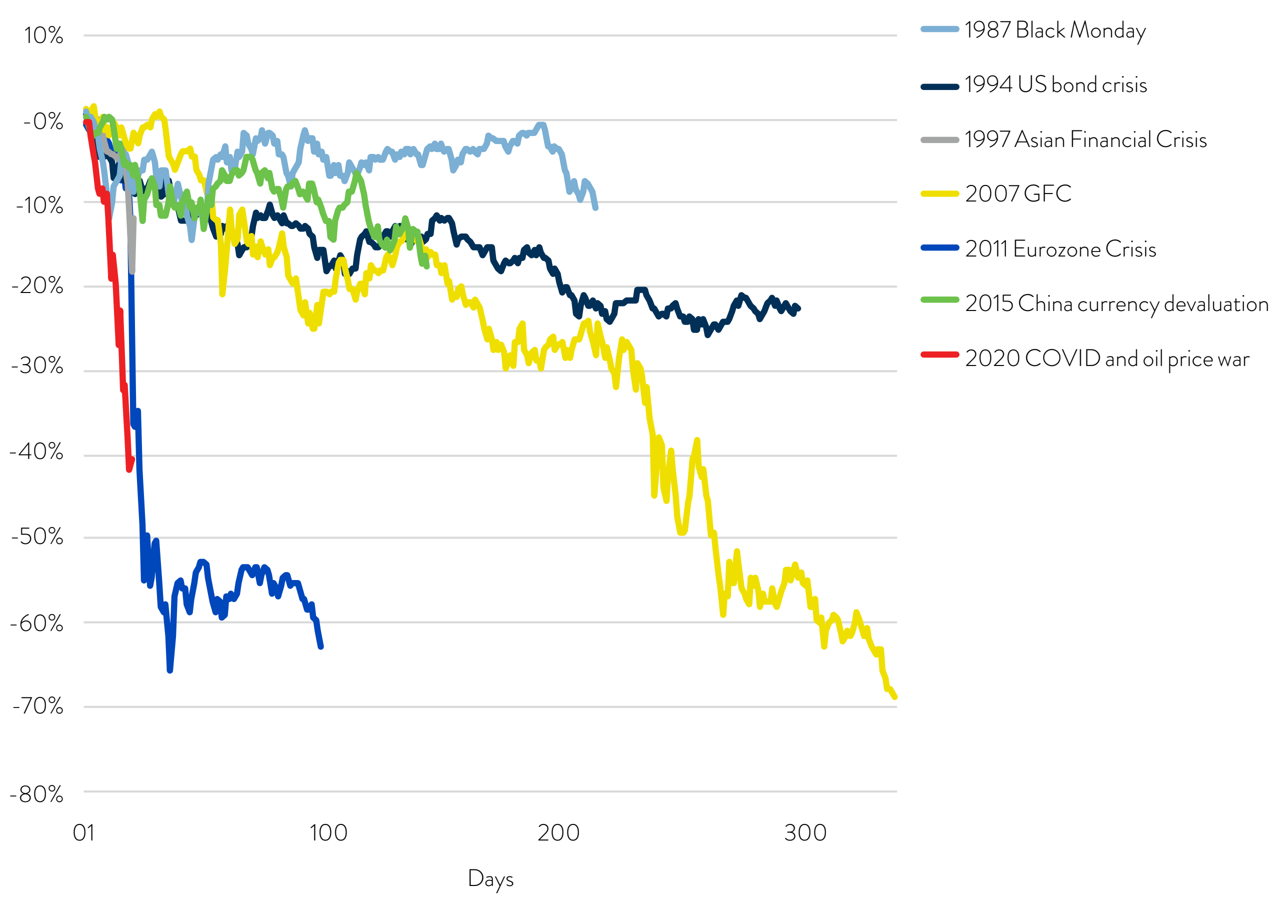


Figure 3: ASX crashes – speed of the fall compared – cumulative % decline in All Ords relative to peak



Recent weeks have seen central banks around the globe unleash a fusillade of stimulatory monetary policy measures, including RBA announcing that it would introduce quantitative easing measures for the first time, dropping Australia's overnight cash rate to its lowest level in history (0.25%) and establishing a A$90 billion 3-year funding facility at a fixed rate of 0.25 percent to facilitate lending to SMEs. These expansionary policy settings look very similar to those adopted offshore during the GFC. At an administrative level, governments around the world have already announced extensive economic stimulus packages. Large-scale bailouts for affected sectors are expected in the coming weeks and months.

However, notwithstanding these similarities, the circumstances which have caused these ructions are very different to those of the GFC and some of those differences will have a bearing on the nature (and level) of future fundraising activity and associated legal issues. In particular:

+ much of the market reaction has been caused by the high level of uncertainty about the broader impact and duration of COVID-19 which is creating particularly volatile markets – however, there is also an expectation that once that uncertainty is reduced, market recovery may be quicker too.
+ whereas in the GFC there was a crisis of confidence in financial institutions (caused by a liquidity crisis) and a deep credit crunch which required a record number of entities to recapitalise (credit markets were basically shut), there is no here systemic risk and the private banking sector is well capitalised (and less leveraged than during the GFC) – this means that it should be possible for the global economy to "bounce back" relatively quickly.
+ as we are discovering, the actual and expected government restrictions being imposed on society to suppress COVID-19 are unprecedented and quickly decimating entire sectors of the economy through both supply effects and demand effects – aviation, tourism, leisure and entertainment, education, consumer discretionary, insurance and energy entities in Australia (and elsewhere) being the most prominent of these. Many businesses are experiencing reductions in their earnings which were previously considered improbable and creating (in some cases urgent) requirements for capital for those entities with insufficient cash (or access to cash) to ride out the downturn.
+ the potential for "social distancing" policies to prevent certain sections of the workforce from being able to operate has also resulted in massive reductions in manufacturing and other industrial activity, which has negatively impacted a number of commodity markets (and in particular oil, which is simultaneously affected by brinksmanship between the largest oil-producing nations over production levels and pricing). Australian producers of oil, gas and other commodities experiencing pricing shocks may come under pressure to raise.

COVID-19 has also promoted more targeted responses from Australian governments than we saw during the GFC. The Federal Government has so far announced a $130 billion JobKeeper wage subsidy and various industry-specific relief packages, including A$1 billion for tourism, agriculture and education; A$715 million for aviation and A$101.2 million for aged care. This is on top of measures for small and medium businesses more generally and the welfare system.

With further federal stimulus expected, it is expected that Australia's governments will spend big to support critically affected sectors in coming weeks. This may reduce the need for private funding solutions to be found (or reduce the size of such solutions). However, there is a high degree of uncertainty about what these additional measures might look like, the timing and process for putting these measures into practical effect and there is no shortage of precedents for similar government measures taking longer than originally hoped or expected (such as in relation to the recent bushfire crisis). However, to the extent we see the government lending to ASX-listed entities (or even taking equity positions – albeit this is not something that has been flagged to date) we expect that this will present opportunities for future equity capital raising activity once the immediate crisis has passed as entities look to get out from under their government support where it takes that form.

Considering the above factors, we expect the "first wave" of entities seeking to raise capital will be those whose revenue models have come under immediate and sustained pressure from the responses adopted to constrain COVID-19 and either need urgent support or want to augment their balance sheet to "ride out" the virus. Unlike the GFC where companies were in urgent need to repay debt or put themselves into a position to do so, these affected entities will likely be facing a cash flow drought and require the cash raised to fund working capital. This will present unique disclosure issues that need to be managed carefully – we discuss this further below.

4 CHOOSING THE RIGHT OFFER STRUCTURE

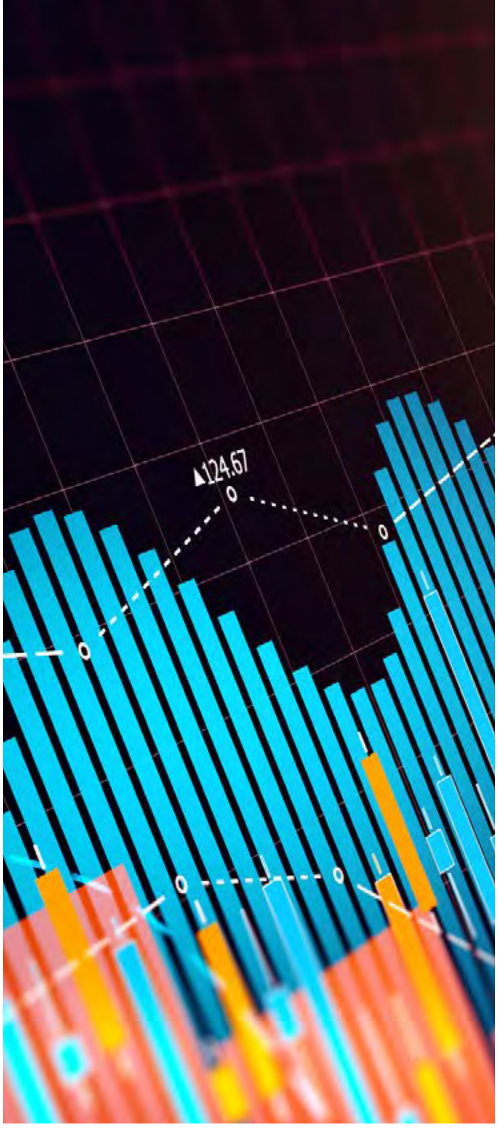
Once a listed entity has decided to proceed with a capital raising, a key consideration will be the most appropriate structure to adopt. As with any corporate transaction, it is important for boards to carefully consider the form that a capital raising takes as it will have a direct impact upon timing, funding certainty and dilution of existing securityholders.

1 Types of structures

Broadly speaking, there are two main types of equity capital raising structures: an institutional placement which involves the offer of securities to existing and new institutional investors during a 1 or in some cases 2-day period; and a rights (or entitlement) offer, which is a pro rata offer made to eligible existing securityholders on the same terms. There are various different structures for rights offers and factors specific to the entity (such as its register composition) and the market more generally will influence the structure chosen. Given these two structures are best capable of delivering large quantities of capital, those are the focus of our report and data analysis.

The other main methods of raising capital (leaving aside corporate debt financing) include:

+ security purchase plans (SPPs) which are commonly conducted following a placement to facilitate retail securityholder participation, particularly, retail shareholder participation. The Australian Securities and Investments Commission (ASIC) last year increased the SPP limit for individual shareholders from A$15,000 to A$30,000 and as such it is expected that, in most cases, retail shareholders will be able to subscribe for an amount of securities equal to or more than their pro rata amount, thereby offsetting any dilution risk.
+ underwritten distribution reinvestment plans (DRPs); and
+ much more rarely, convertible securities and bonds (either convertible or non-convertible).



2 Capital raising structures used during the GFC

Figure 4: Types of capital raisings during the GFC

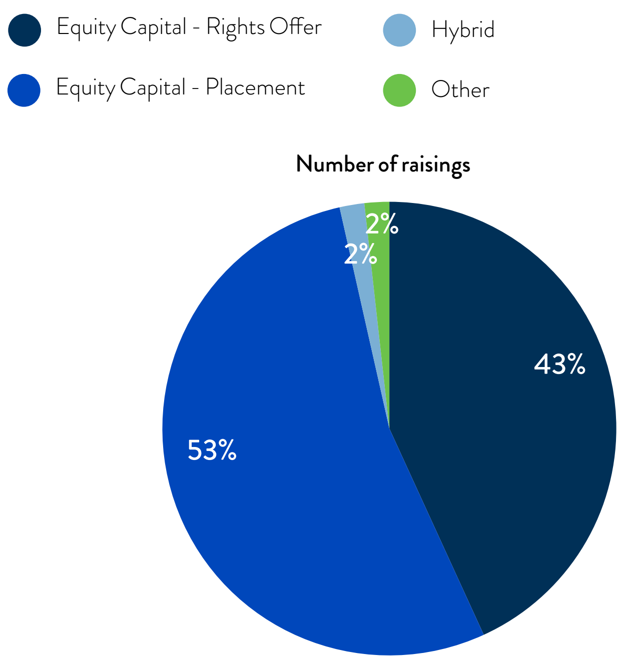


Table A: Secondary capital raisings during the GFC[1]

Issue type	Number of raisings	Proportion of raisings	Average offer size	Median offer size	Average discount[2]
Equity Capital[3]	219	96.48%	$586,856,344.40	$300,193,020.00	17.17%
Placement	98	44.75%	$467,246,154.91	$220,569,000.00	9.12%
Rights offer	121	55.25%	$683,730,712.74	$410,809,313.00	22.05%
Hybrid[4]	4	1.76%	$1,025,406,666.75	$908,106,200.00	Not applicable
Other[5]	4	1.76%	$986,148,700.00	$972,297,400.00	Not applicable
Total	**227**	**100.00%**	**$601,620,092.03**	**$304,058,871.00**	**17.04%**

[1] Capital raisings greater than A$100m from the period 1 August 2007 to 31 December 2009.

[2] Includes various discount measures depending on the fundraising structure. For rights offers, this is the discount to TERP; for Placements this is the discount to previous close, or, if not disclosed, the discount based on the shortest VWAP that was disclosed.

[3] Includes placements, rights offers, share purchase plans and dividend reinvestment plans that are not underwritten.

[4] Includes offers of convertible note and preference shares.

[5] Includes offers of subordinated notes, options, bonds and stapled securities.

3 Institutional placements

During the GFC, institutional placements accounted for 43% of all capital raisings of A$100 million or more. This compares to institutional placements accounting for only 25% of capital raisings in the past 3 years (seeking to raise more than A$100 million). Institutional placements, combined with SPPs, have become increasingly popular in the past 12 months (in part due to ASIC's increase in the cap on SPP size and the fact that it is generally easier and less dilutive to get a placement underwritten).

In the next few months, we expect to see an even greater increase in the preference for institutional placements as the preferred capital raising structure for the following reasons:

+ In the current climate of extreme market volatility, placements will be the fastest means of raising capital and are generally far easier to procure underwriting for since the risk period is much shorter. During the GFC, the use of placements was highest for raisings in the immediate aftermath of large share market falls when it was harder to have confidence about transaction pricing holding up for more than a short period of time.
+ Given the shorter risk period, it is possible to set an offer price at a smaller discount than might otherwise be required to achieve a successful rights offer, which may assist in reducing dilution overall (at least compared to non-renounceable entitlement offer structures, which based on our analysis were much more common than renounceable offer structures in the GFC – the average discount for rights offers during the GFC was approximately 22% to the "theoretical ex rights price" (TERP) compared to 9% for placements, while 72% of rights offers were non-renounceable.
+ The higher threshold for SPPs will make placements more palatable from a "fairness" perspective, given that for many registers it will be possible to ensure that a very high proportion of securityholders will be able to subscribe for an amount of securities equal to or more than their "pro rata" amount, thereby offsetting any dilution risk.
+ placements also involve a less intensive due diligence process (at least from a documentary perspective) and more streamlined offer documentation.

The use of institutional placements is, however, not without its drawbacks. Structurally, as placements are only available to select institutional investors, non-participating securityholders (including retail shareholders) are subject to dilution – whilst the SPP structure can assist with retail investors, there will inevitably be high net worth or smaller institutional investors who miss out.

The biggest drawback of institutional placements is that there is a regulatory limit on their size imposed by the ASX Listing Rules. Typically, this limit is no more than 15% of the shares on issue under Listing Rule 7.1 or 25% where prior shareholder approval has been obtained under LR 7.1A (for small cap companies). However, ASX has recently increased the 15% limit to 25% under its temporary COVID relief (for further detail, see "How have the regulators responded" below). Although it is possible to issue a higher proportion than 25%, doing so requires prior shareholder approval which removes certainty and creates delay. A 28-day notice period applies for all shareholder meetings, which may be problematic if funds are urgently needed.

Entities considering raising capital via an institutional placement should be aware of their current placement capacity. Companies should be aware that shareholder approval will also be required for some complex restructures (for example where a single person is to take up and would increase their holding above 20%) or for issues of securities involving a related party or other "closely connected parties".

4 Entitlement offers

While placements entail a shorter risk period, entitlement offers are particularly valuable in times of market decline where the entity's share price has fallen so much that a placement is incapable of delivering the required capital without securityholder approval.

In the past decade, companies have increasingly taken advantage of the "low doc" entitlement issue regime which allows issuers to raise capital without the need for a prospectus or disclosure document. In particular, there has been a preference for accelerated offer structures – most notably, accelerated non-renounceable retail entitlement offers (**ANREOs**) and accelerated renounceable entitlement offers (**AREOs**), which together accounted for approximately 75% of all entitlement offers (seeking to raise more than A$100 million) in the past 3 years. Under accelerated structures, entities can access the lion's share of the funds within 8-10 days of launch, without diluting eligible retail shareholders who take up their entitlement.

During the GFC, the ANREO structure was dominant – representing over 70% of rights offers of over A$100 million. During times of particular volatility, many of those ANREOs were also only partially underwritten – with the institutional component underwritten but the retail component not underwritten. This was due to the difficulty of taking underwriting risk over a 3-4 week period during times of significant market uncertainty. Since there is no way to receive value for entitlements that are not exercised, ANREOs tend to maximise the incentive for securityholders to participate and so will generally be preferred over AREOs in volatile conditions like what we currently have. However, there are limits on the level of dilution possible which apply to ANREOs so recapitalisation sized ANREOs must be carefully managed.

It is also possible to include an institutional placement into an ANREO which is offered and settled on the same timetable as the institutional component of the ANREO. An entity's ability to do this is subject to the same constraints and requirements as outlined above for standalone placements.

5. Other structures

There are a range of other structures available – one that we expect may be attractive is a convertible note that delivers much needed cash without initially impacting equity ownership. There are complex structuring issues to resolve here. Whether to put a floor on the conversion price and shareholder approval requirements (both from a takeovers law and a Listing Rule 7.1 perspective).

5 DISCLOSURE MATTERS

Companies wishing to undertake a "low doc" entitlement offer should ensure that they are eligible and not precluded from doing so (there are pre-conditions).

Companies may need to go into trading halt followed by periods of suspension while they assess the impacts of COVID-19 on their business and what options may be available to solve their need for capital which may rule out a "low doc" offer and force them into needing a prospectus which will add further delay.

Regardless of the approach, low doc or prospectus, raising capital will present unique disclosure issues that need to be managed carefully.

All listed companies whether they are raising capital or not should be carefully considering any existing earnings guidance in the market and whether or not that can reasonably be updated or whether it should be withdrawn.

In connection with a capital raising, consideration needs to be given to whether the cash that is being raised will be enough or whether that can even be determined in circumstances where there remains significant uncertainty about the impact of COVID-19 on an entity's customers, suppliers or in many cases. Too much uncertainty may make raising equity practically impossible and so entities that are not able to last until we have more certainty on when the virus has peaked may need to look at more unconventional means of survival – in some cases, recapitalisations that may even result in a change in control. However, we expect that where the underlying businesses remains fundamentally sound, underwriting will be available.

We also expect to see a lot of offers launched only after confidential market soundings are successfully undertaken. Where a deal doesn't move forward, there are challenging issues concerning how to "cleanse" the wall-crossed investors.

The scope and adequacy of the due diligence review will be influenced by the market in which the entity operates and how exposed its business is to the virus.

Entities should assess the impact of COVID-19 on all aspects of their business including:

+ supply chain disruptions and other major operational issues, including delays and counterparty risk;
+ changes in consumption and demand for products and services;
+ implications for its workforce;
+ impacts to material contracts (including whether the entity or its counterparties may be able to rely on "force majeure" provisions to avoid liability for non-performance), insurance and financing arrangements; and
+ the impact of government intervention and new regulatory obligations (for example, quarantining and restrictions on public gatherings) and even changes in private behaviour (i.e. voluntary self-confinement to mitigate the risks of transmission).

6 I'M A DIRECTOR OF AN ASX LISTED ENTITY. WHAT DO I NEED TO BE THINKING ABOUT?

We anticipate that all directors of ASX-listed entities will already be well advanced in their thinking about the implications of COVID-19 for their businesses.

This requires each entity to carefully consider the impact in a dynamic way, ensuring that constantly changing circumstances are considered and the analysis (and any assumptions on which it is based) is updated. Many of our clients are undertaking "scenario analysis" to consider the potential differing effects of the situation at various levels of severity (including "worst case" scenarios).

All directors have a personal responsibility to ensure the company doesn't trade while insolvent, and solvency under Australian law is a cash-flow, rather than a balance sheet, test. As such, directors of companies which are affected by COVID-19 must ensure that cash flow analysis is being undertaken covering an appropriate future period (generally 6-12 months) to identify where capital requirements may exceed available cash. Of perhaps more immediate concern are the covenants under a company's debt facilities and the timing of any obligations to report on compliance with those covenants. It may be worth modelling the entity's ability to satisfy those covenants out beyond just the next testing period given how uncertain the duration of this crisis is.

If a capital raising need is identified, it is helpful to obtain financial and legal advice expeditiously. Although it is possible for an emergency equity capital raising to be done in a matter of days (a common occurrence during the GFC), that sort of timeframe is extremely challenging, particularly where difficult judgements are required on the nature of any risks or issues affecting the company and importantly how to disclose those. Getting organised ahead of time helps and every day counts.

Although in the context of a "low doc" offer, the issuer's directors do not have personal liability for the offering documentation in the same way that they would if a prospectus were used, we are seeing ever greater scrutiny by regulators (and other market participants) of disclosures, particularly about "known" issues or risks and it is important for each director to be comfortable with the adequacy of the due diligence process put in place to support the disclosures made.

Other matters requiring the directors' consideration are:

+ **Offer structure:** how important is it for an offering structure to be "fair" to all shareholders? To what extent can the commercial need to raise the funds take priority over fairness considerations?
+ **Offer pricing**: is there a level of discount that is too deep? From our review of GFC capital raisings above A$100m, the average discount was 22% (to TERP) for rights offers and 9% (to last close or based on a VWAP) for placements.
+ **Allocations**: ASIC has published guidance about ASIC's expectations of the level of involvement that boards have in the allocation process. We expect boards to be increasingly focused on these decisions and will be looking to discuss with underwriters/ lead managers. The level of difficulty of executing the raise will determine the extent to which boards are able to influence these decisions.
+ **Alternatives:** what are the alternative ways of meeting the capital requirement (if any)? Particularly where the offer may affect the control of the issuer, consideration of alternatives is essential.

Boards can be assisted in working through these matters by equity capital markets and relationship investment bankers, independent financial advisers who specialise in ECM and law firms with strong ECM experience as well as other professional advisers with relevant experience and transactional accounting advisors who can assist in detailed analysis of cash flows.

7 WHAT DO UNDERWRITERS NEED TO BE THINKING ABOUT?

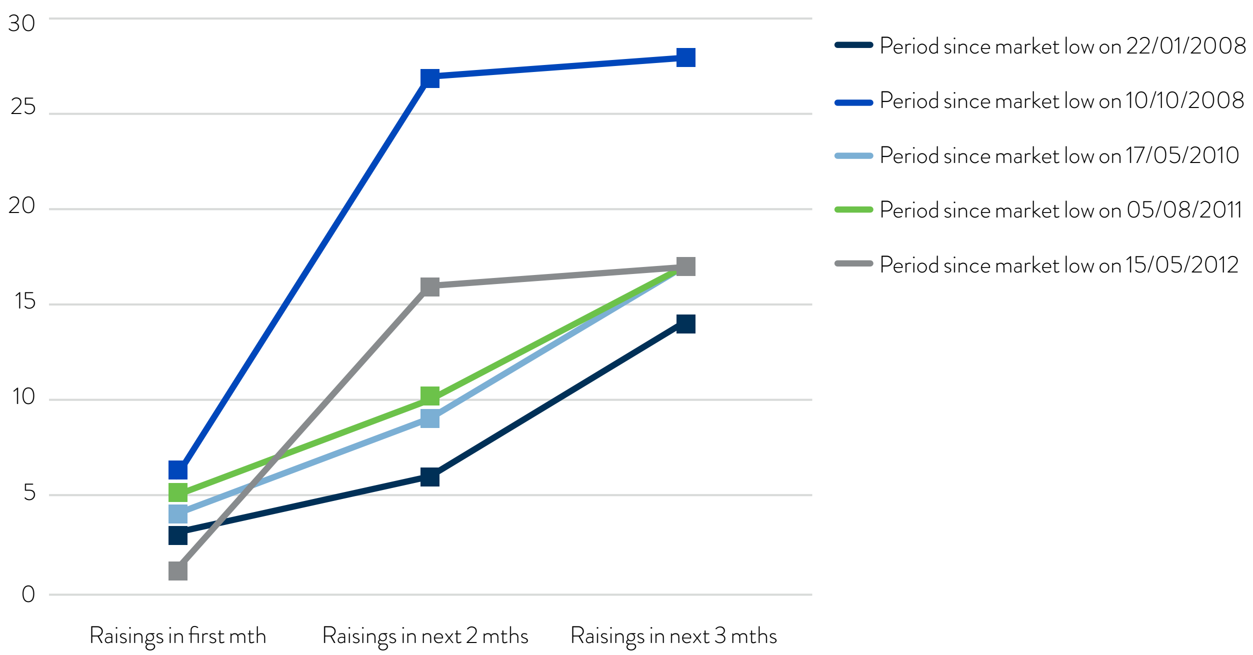
The immediate environment is presenting significant challenges to underwriting equity capital markets transactions.

With daily movements on the major U.S., European and Asian exchanges of greater than 5%, pricing transactions is extremely challenging, let alone getting comfortable to take the risk of underwriting those trades.

However, as the GFC showed, whilst difficult, it is not impossible to launch follow-on raisings even in the immediate aftermath of substantial declines.

"As the chart below shows, following the five major share market declines in the period between January 2008 and May 2012, the number of capital raisings markedly increased within 3 months of the drop. This suggests that while there may be a dearth in capital raisings in the immediate period following extreme market declines, this is necessarily short-lived (it also shows that it was not impossible during the GFC and the period immediately following, still to do capital raisings close to the time of major share price falls). Approximately 40% of placements and 93% of rights offers of A$100 million or more during the GFC were wholly or partially underwritten.

Figure 5: Capital raisings following major ASX falls during the GFC (and the period immediately following)



In the current climate, and as we are already seeing, those entities who have an urgent need for capital or expect to have such a need in the next several months, will seek to raise capital quickly (possibly by taking advantage of a day when markets trade up) but we would expect it to be more common to see a larger number of raisings within around 3 months from now. This will depend on a number of factors, including the extent to which cash flow difficulties persist, the amount of headroom under corporate debt facilities that is available for draw down (and other alternative cash sources) and the degree of uncertainty that any debt-funded entities have about whether they can meet any debt covenant tests slated for June 30 balance dates and assessment of the continued outlook and uncertainty created by COVID 19 and when the crisis may be over.

There are several key issues that lead managers / underwriters should consider in connection with capital raisings undertaken in periods of high market volatility and economic uncertainty:

+ **Reading investors:** Unlike in the GFC, when a big whack of capital could cure a balance sheet of its over-leverage in a macro-environment which was, at least in Australia, more benign than we are seeing under COVID-19, now underwriters and investors are dealing with assessing whether capital injections will be enough in circumstances where the various shutdown measures may suppress activity for an indefinite period of time (with difficult to predict outcomes).
+ **Bookbuild messaging:** there has been a notable level of regulatory focus on bookbuild messaging and ensuring such messages are delivered fairly and accurately. It is fair to assume that the importance of such messaging will increase in such choppy market conditions and this will need to be managed carefully.
+ **Due diligence:** underwriters will need to ensure that issuers are putting in place appropriate due diligence processes to ensure that, so far as is practicable, they can be informed about how and to what extent the entity seeking to raise capital will be impacted by COVID-19 – a hard task when the entity is unsure itself. This goes not only to pricing and exposure to liability but also reputational risk.
+ **Underwriting agreements:** it has become increasingly difficult to predict weeks or even days in advance and unexpected developments will continue to arise as the "COVID-19 curve" changes. Managing and planning for future risks, for example as a result of sudden changes in government policy, economic declines or a sharp increase in the severity of the impact of the virus on the issuer is crucial. To a large extent the standard forms of underwriting agreements provide for the allocation of these risks, however specific consideration of this will be a must on any transaction and underwriters will need to consider what types of unexpected events or risks are "deal breakers" and ensure contracts reflect this (such as market and business performance related termination events).
+ **Extent of underwriting:** during the GFC, underwriters would only take on underwriting risk for a short period of time or underwrite a portion of the offer (eg, many accelerated entitlement offers had only the institutional component underwritten). When considering whether to underwrite an offer, we expect underwriters will be thinking about whether offer pricing discounts can be minimised by reducing the component of the offer that is underwritten. This will always depend on whether it will deliver the funding outcome that an issuer requires.
+ **Moratoriums on further equity issues:** underwriters will need to consider the appropriateness of seeking lengthy moratoria on further capital raisings by the entity. In an environment with so much uncertainty, it is conceivable that entities may be required to undertake several capital raisings within a short period of time (as was demonstrated in the GFC where a number of entities, including very large ones such as the big 4 banks, Wesfarmers and Westfield (as it was then called) to name a few all undertook consecutive raisings).
+ **Logistics and practicalities:** it remains to be seen whether underwriting firms are themselves required to implement even more stringent "social distancing" measures than they currently have and whether that may affect the way raisings are done – for eg, sales desk briefings and investor engagement (eg investor lunches and presentations). No doubt underwriters have been working through their compliance requirements and their ability to operate outside their office environment.

8 CAN'T GET A PROFESSIONAL UNDERWRITER? WHAT ARE MY OTHER OPTIONS?

Entities seeking greater certainty in their funding arrangements are not restricted to utilising a professional underwriter.

There are likely to be occasions where the underwriting risk cannot be accepted on commercially acceptable terms (or at all) and it will fall to the major shareholder of an entity to provide support for an urgent capital raising either in the form of a pre-commitment to take up entitlements or directly as an underwriter of the entire capital raising.

When relying on existing shareholders to underwrite a capital raising, companies need to consider a range of factors – in particular, control (the 20% rule) and related party issues and in some circumstances whether Foreign Investment Review Board (FIRB) approval will be required. The Takeovers Panel may intervene if the circumstances and terms of a capital raising suggest that control of the company may be affected in an unacceptable manner and the general rule is that the control implications of an offer cannot go beyond those reasonably necessary to achieve the fundraising purpose (and financial distress is not a safe harbour, although it is a very relevant consideration). Many of the risks associated with these issues can be addressed through structuring the capital raising and underwriting arrangements appropriately.

9 HOW HAVE THE REGULATORS RESPONDED?

In response to COVID-19, the priority of regulatory authorities has been to facilitate the effective operation of Australia's financial markets and prioritise continued access to credit for businesses.

The regulatory responses to the crisis are changing more or less constantly and are difficult to predict. For certain it can be said that more will be asked of the regulators as entities and other market participants identify measures that may help in these challenging times.

Putting to one side the RBA's historic measures, APRA and ASIC have indicated that they will consider providing relief or waivers from regulatory requirements where warranted. In fact, ASIC has recently announced relief for listed companies in connection with secondary capital raisings to allow entities who have become ineligible to utilise the "low doc" regime after 19 March 2020 as a result of entering into more than 5 days of trading suspensions to be able to access that regime without needing to apply to ASIC for specific relief.

ASX will also temporarily allow entities to request back-to-back trading halts (i.e. a total of 4 days in halt). This is only available where entities are considering and preparing for capital raisings. This will help entities who would otherwise be required to expend part of their 5-trading day limit on suspensions under the current "low doc" regime.

In line with NZX's recent move, ASX has also announced a temporary lift in the placement capacity from 15% to 25%, which will be accessible where any entity includes a follow on accelerated pro rata entitlement offer or SPP. This is an overall 25% cap – entities cannot utilise both this new 10% capacity and their remaining Listing Rule 7.1A capacity. Where an entity is contemplating a placement followed by a pro rata entitlement offer, it will still qualify for the normal "supersize" waiver ASX grants and entities will not need to apply separately to ASX to get the benefit of this waiver. This will allow for large accelerated non-renounceable offers with an upsized institutional placement. Entities electing to do a placement with a follow-on SPP must conduct the SPP offer at a price equal to or lower than the placement price. If there is a limit on the amount to be raised under the SPP offer, scale-back arrangements must be pro rata to all participants and disclosed to the market. This will require some careful management for entities with large registers.

ASX has also removed the ratio limit of 1:1 for non-renounceable entitlement offers. This goes beyond what the NZX recently did in New Zealand – which was to put in place a 2:1 cap.

We expect to see institutional placements and follow-on SPPs take the lead as a result of these temporary measures (and early evidence suggests that this has been the case). The measures should also enable listed entities to raise more capital – faster. Amid the rush, directors need to continue to focus on the best interests of the company when structuring a capital raising. In particular, ASX has commented that "this requires directors to balance a range of considerations, such as the need for quick and certain capital, and the cost to and possible dilution of existing security holders. ASX shares these [i.e. ASIC's] expectations and may withdraw the benefit of [the temporary relief] in any particular case if ASX considers it is being abused by a listed entity or that a listed entity is otherwise acting unfairly or unreasonably in the circumstances."

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