

Minimizing the Cost of Capital by “Going Public”

Any businessman will tell you that for a business to get off the ground and survive it requires capital. Capital is the foundation and the life line for business. Here in Fiji, like other parts of the world, many businesses are established with capital contributed by a small number of investors who become part owners or shareholders. As a business grows, additional capital is needed. Raising capital to fund growth is one of the biggest challenges facing any business, particularly for emerging enterprises.

Very often businessmen turn to bank borrowings when they require additional capital if they cannot fund it internally from their own profits. However some may not be aware that there are other cost effective options available in the capital markets. For example, when a company takes a loan from a bank, it will be required to repay the principal borrowed, interest and associated fees for the term of the loan. This can be a significant sum, compared to the capital raising costs in the capital markets. However if a company raises capital by selling its shares to the public, the business essentially has interest free capital, as there is no loan repayments, and funds raised can

be fully committed for the purpose which it was raised.

Alternatively an established company or business that is listed has an option of selling down part of its shareholding at an attractive premium, raising interest free capital. They can trade equity for cash and they can use that cash to further grow their business, retire or diversify into new ventures.

A company can also raise capital by issuing a bond or debenture. In such cases the company would be required to make regular interest repayments to investors or bond holders for a fixed term. Some companies may find this option more attractive because they may be able to obtain more competitive terms like a lower interest rate at a fixed term which a bank may not be willing to provide.

Any company can make a public offering if its Memorandum and Articles of Association permit it. Most companies formed under Fiji's Companies Act are private companies. These companies cannot make public offerings without changing their constitutions to allow public offerings and (if necessary) to meet the requirements of a stock exchange listing.

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MEET A BROKER REP

Elenoa Kaloumaira
 (Kontiki Stockbroking Ltd.)

Getting Started

Prior to joining KSB, I gained my Bachelor of Business Degree majoring in Finance and Operations Management from UNITEC New Zealand in April, 2008.

I wanted to join KSB because while studying Finance, I became interested in financial services, in particular, stock markets. Also, when working for Guardian Trust New Zealand Company Ltd in 2007 as part of a student job placement programme, I learnt the importance of building a strong relationship with clients, a quality which I also found at KSB. I began working for KSB in May 2008.

The Clients

We have a wide range of clients with an equally wide range of needs. For example, there are clients who want regular income and therefore prefer investments that have a high dividend yield. Other clients are focused more on capital gains and so prefer higher growth investments, while others want a mix. The key is to first understand these client objectives before making recommendations.

The Job

Currently, at KSB I have to assist the Manager Broking in the following:

- Building and maintaining relationships with clients
- Trading on the South Pacific Stock Exchange
- Liaising with clients
- Carrying out back-office functions
- Coordinating the weekly market analysis newsletter

Biggest Challenge

The biggest challenge for me is building strong client relationships. When I say 'challenge', I mean this in a positive way. Relationship building is a very important area in our business as broker-client interaction relies a lot on trust, and this is a very fulfilling experience.

Best Investor

A good investor for me is someone who has already taken the time to understand investments at a basic level and who is clear about his/her investment objectives. With this foundation, we can work well together to build an appropriate investment portfolio.

Best Thing about the Job

Getting to meet new people and helping to create wealth for clients.

Kontiki Stockbroking Limited.

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Did you know?

Companies are eligible to claim as tax deductible expense, one and a half times (150%) of the costs associated with the preparations for listing on the South Pacific Stock Exchange.

What are the benefits of 'going public'?

The desire to maximize wealth is what drives companies to go public and list on a stock exchange. By careful planning, founding business owners can maximize the value of their company and can enhance their retirement earnings if they allow their business to go public and list. There are many advantages that accrue to companies that attain a public listing of their shares. Some of the key considerations and benefits are:

- Creating a market for the company's shares – listing the company on the Stock Exchange, creates greater liquidity for shareholders
- Companies can also enjoy the flexibility of making public offerings several times during its business life, and with such flexibility companies can go into joint ventures and choose partners beyond its present membership;
- Enhancing the status and financial standing of the company;
- Accessing to additional fund raising in the future by means of new issues of shares or other securities;
- Facilitating acquisition opportunities by use of the company's shares;
- Offering existing shareholders a ready means of realising their investments - the founding shareholders can sell part of the company to new investors, thereby sharing the business with the public and

thereby potential for increases in the share price;

- A company's image can be enhanced as a result of the prestige and public exposure of listing. The listed company will enjoy a higher profile due to the reporting requirements of the stock exchange and public interest in listed companies; and,
- Providing the company with an opportunity to implement share option schemes for their employees, this can act as a powerful motivator for management and staff.

It generally takes 6 months to publicly list a company on the stock exchange although the time period can range from 3 months to 2 years. A range of professional advisors are needed to assist with the legal, financial, accounting and valuation aspects of public listing plus prospectus preparation, underwriting of shares and assistance with IPO Plans.

If you intend to raise capital or list your company on the SPSE, talk to a licensed investment adviser or call our office or visit our website www.cmda.com.fj for more information.

References:

- CMDA Guide: "How to List your Company on the Local Stock Exchange"
- UNITAR: "Advantages to the Company and Owners in Going Public"

"The Relationship between Bond Prices & Interest Rates"

...investors who hold the bonds to maturity are guaranteed that they will be repaid the par value of the bonds at maturity

[Last quarter, we looked at the basics of investing in bonds. In this quarter's article, we will examine the relationship between bond prices and interest rates.]

Investors who buy bonds do not have to hold on to them for the full term but may trade them in the secondary market e.g. through a broker on the stock exchange.

The price at which an investor can trade the bond in the secondary market will be determined by the current level of interest rates in the market compared to the coupon rate of the bond. Other things being equal, generally when interest rates fall, bond prices rise and vice versa. Thus interest rates and bond prices move in opposite directions. The extent to which bond prices move, in one direction or another, will depend on the magnitude of the interest rate movements. Bond price volatility will also vary because of its coupon and the maturity.

Let us look at an example of how interest rates affect bond prices. Suppose an investor buys \$5,000 worth of Fiji Government bonds when it is first issued in the primary market by government. The bond has a fixed coupon rate of 10% and a life of 10 years i.e. it is a ten-year bond. Each year, for the next ten years, the investor will receive an annual coupon (interest) payment of \$500. At the end of 10 years, Government (the issuer) will repay the investor the \$5,000 it borrowed. The return or yield to maturity on the bond is 10%.

To see how interest rates affect the price of bonds, we will look at the example used above and assume the investor wishes to sell the bonds in the secondary market after four years, rather than hold it for the full term. We will look at two scenarios, one where interest rates have fallen and one where interest rates have risen.

Assume that after four years, interest rates have risen and investors are now looking for a 12% coupon rate on similar newly issued bonds. This means that the market value of the bond will have to be such that investors earn at least the current market rate of 12%. The bond will continue to pay periodic payments of \$500, however, the new investor (purchaser) requires a yield or return of 12% so they will pay the original bondholder less than the initial par value of \$5000. Using a bond price formula, the price of the bond will be calculated such that the annual coupon payments of \$500, plus the difference between what the new investor pays the bondholder and the face value of \$5000 to be received in 6 years, will result in a yield to maturity or return of 12% for the new investor over the remaining 6 years of the bond. The new investor will therefore buy the bond from the initial investor for \$4,581 and receive a \$500 coupon each year plus a principal repayment of \$5000 in

the sixth year when the bond matures. The \$500 per year plus the gain of \$419 (\$5000 face value received less purchase price of \$4581) will equate to a 12% per annum yield on the initial \$4,581 invested by the new investor. The original bondholder therefore incurs a capital loss on his/her investment.

Now assume that the opposite happens and interest rates had fallen and investors were now seeking a coupon rate of 8% on similar bonds. The bondholder would require the new investor to pay a price that yielded a return equal to the current market rates of 8%. Because the bond pays an annual coupon of 10% which is

higher than the current market rate of 8%, the price to be paid will be higher than the original price paid by the bondholder. The new investor would be required to pay \$5,469 for the bond, which would yield him/her an annual return of 8%, equivalent to the current market rate. The original bondholder therefore makes a capital gain on his/her investment of \$469.

The prices of bonds with longer terms to maturity are likely to fluctuate more with rising interest rates than ones with shorter terms to maturity and vice versa.

The example above illustrates that during

the life of a bond, its capital value can change at any time in line with changes in the overall level of market interest rates. However, investors who hold the bonds to maturity are guaranteed that they will be repaid the par value of the bonds at maturity.

You can also calculate bond prices or returns by using the bond price and bond returns calculator now available on www.cmda.com.fj or buy a CMDA Personal Wealth Calculator. ©

[Next quarter, we will examine the risks of investing in bonds.]

“CMDA Adopts Corporate Governance Principles for the Industry”

Good corporate governance is not an abstract goal – it is an essential element in developing a viable capital market. Investors place their funds into the hands of management and unless they have full trust and faith in the objective and careful decisions of management, investors will stay away.

The Capital Markets Development Authority (CMDA) believes that sound corporate governance practices are essential for attracting investments. In that regard, improving corporate governance has been one of CMDA’s top priorities and in 2007 started work on a project funded by AusAID to develop a set of Corporate Governance principles for the capital markets industry.

Following a thorough consultation process in 2007, stakeholders met in June 2008 to review and agree on a set of principles that will set a benchmark for good corporate governance

practices in the industry. The document, Corporate Governance Code for the Capital Markets articulates on 10 Principles (as summarized in Box 1) that intermediaries, listed companies, and key market players could consider essential for the development of good governance practices.

The underlying objective of developing these principles are to guide companies and stakeholders in adopting appropriate structures that will enhance investor confidence, efficiency and growth in the capital markets. These structures are designed for the board and management to pursue objectives that are in the interests of the company and its shareholders.

The Principles will be effective from 1st January 2009. An electronic copy can be obtained via request email on info@cmda.com.fj

| Box 1 | Corporate Governance Code for Capital Markets |
|--------------|--|
| Principle 1 | Establish clear Responsibilities for Board oversight |
| Principle 2 | Constitute an effective Board |
| Principle 3 | Appointment of a Chief Executive Officer |
| Principle 4 | Board and Company Secretary |
| Principle 5 | Timely and balanced disclosures |
| Principle 6 | Promote ethical and responsible decision-making |
| Principle 7 | Register of interests |
| Principle 8 | Respect the rights of share holders |
| Principle 9 | Accountability and Audit |
| Principle 10 | Recognise and manage risk |

Regulatory Matters

On regulatory matters, during the quarter, the CMDA received no complaints and no inquiries into potential breaches of the CMDA Act, Regulation and Rules.

The CMDA granted approvals to:

- Kontiki Stockbroking Limited (KSB) to conduct the business of broker/dealer from 1 February 2008 to 31 January 2009.
- Mr Jack Lowenstein to act as a broker representative for KSB from 1 February 2008 to 31 January 2009.
- Mr John Courtney to act as a broker representative for KSB from 1 February 2008 to 31 January 2009.
- Ms Raghni Khatri to act as a broker representative for KSB from 7 March 2008 to 6 March 2009.
- Mr Sanjay Dewan to act as a broker representative for KSB from 16 May 2008 to 15 May 2009.
- Mr Meli Verebalavu to act as a broker representative for FHL Securities Limited from 25 April 2008 to 31 December 2008.

- Mr Jaoji Koroji to act as an investment adviser representative for FHL Securities Limited from 27 March 2008 to 31 December 2008.
- Kontiki Capital Limited to conduct the business of investment adviser from 30 June 2008 to 31 December 2008.
- Mr John Courtney to act as an investment adviser representative for KCL from 30 June 2008 to 31 December 2008.
- Mr Gilbert Veisamasama to conduct the business of investment adviser from 26 April 2008 to 31 December 2008.
- Mr Rick Croker to conduct the business of investment adviser from 17 May 2008 to 31 December 2008.
- Mr Sunil Dutt Tiwari to act as a unit trust representative for Colonial First State Investments Limited from 11 June 2008 to 31 December 2008.

- Mr Bipin Patel to act as a unit trust representative for Colonial First State Investments Limited from 13 June 2008 to 31 December 2008.

New Licenses:

- Mr Rajnesh Chand to act as a broker representative for FijiStock Brokers Limited from 13 May 2008 to 12 May 2009.
- Ms Elenoa Lalabalavu to act as a unit trust representative for Fijian Holdings Trust Management Limited (FHTML) from 13 May 2008 to 12 May 2009.

License cancelled:

- Ms Nijeshni Wati to act as broker representative for KSB.
- Mr Trevor Labati to act as a unit trust representative for UTOF.

News in Brief

- The Flour Mills of Fiji Ltd announced plans to invest a total of \$7m to increase the capacity and product range for the Biscuit manufacturing. FMF is planning to purchase a modern high speed creaming and packaging machine which will allow for greater production efficiency to compete in the international market. This investment is expected to commence in 2009 and FMF is looking at recruiting an additional 200 employees.
- Yasana Holdings Ltd (YHL), which has 51% ownership interest in Fiji Television Limited has put on hold its plans to offer shares to the districts and villages within the 14 provinces to raise \$3m. An internal financial assessment undertaken by YHL shows that some provincial companies might not be ready and have thus postponed the offer to a later date. The Company had earlier allocated 150,000 shares to be sold to each district.
- The Fiji Sugar Corporation (FSC) received a \$25m guarantee from the Interim Government to pay for cane supplied by growers before the Company receives proceeds from its sales. The move by the Interim Government will greatly assist FSC to better manage its working capital. The Company is exempted from paying a guarantee fee.
- Fiji Care Insurance Ltd had quoted an additional 269,742 shares on the South Pacific Stock Exchange (SPSE). The additional shares were a result of reinvestment under the Dividend Reinvestment Scheme (DRS) and increased outstanding shares to 6,030,516. FIL recently paid a dividend of \$0.04 per share for the financial year ended 2007 amounting to \$230,430.96 The Company offers accident, health, medical and life insurance policies.
- Fiji Sugar Corporation has entered into a \$1 billion deal with the European Union (EU) based Tate and Lyle (TL) for the preferential supply of 300,000 tonnes of raw sugar annually, for the next seven years. The Interim Finance and Sugar Minister also expressed his appreciation for the long-term contract which will operate until September 2015 and rake in more than \$425m. From October 2009 sugar exports to the EU will be governed by the provision of the Economic Partnership Agreement (EPA) between Fiji and the EU. The EPA will be effective as soon as the Sugar Protocol ends in September 2009.
- Supermarket chain, RB Patel Group Ltd had released its audited financial report for its financial year ending 31 March 2008. The group reported a net profit after tax (NPAT) of \$4.28m, an increase of 15.4% on FY2007. The RB Patel Group has also announced a second interim dividend of 10 cents per share for the financial year ending 31 March 2008. This totals the dividend payment to \$0.14 per share for the FY2008.
- Fiji's prime telecommunications company, Amalgamated Telecom Holdings Ltd has acquired 51% ownership into Fiji's largest mobile service provider Vodafone Fiji Ltd (VFL), effective 31st March 2008. ATH took over the majority ownership from its subsidiary, Telecom Fiji Ltd (TFL).

The change in ownership was undertaken to accommodate the introduction of the new telecommunications regulatory framework.
- The Fiji Sugar Corporation Ltd has entered into a Memorandum of Understanding with Japan-based Sojitz Corporation to investigate the feasibility of ethanol production in Fiji. The project is expected to be completed by the end of 2009, employing approximately 100 workers and is estimated to cost around \$36m. It is expected to earn around \$20m annually and production capacity at around 33,000 kilolitres per year.
- Fijian Holdings Ltd has announced an unchanged interim dividend of ten cents and five cents per share for the company's A class and B class shareholders respectively for the six months ending 31st December 2007. The aggregate payout of over \$2.0m will be sourced from NPAT of \$3.9m.
- Cabinet approved the Electronic Commerce Promulgation 2008, based on the submission made by the Minister for Industry, Tourism, Trade and Communications.

As a result, the on-line trading environment will now be regulated under an efficient electronic commerce infrastructure, which concentrates specifically on Business to Consumer transactions, Business to Business transactions and Business to Government transactions. The Minister outlined that the objective of the Promulgation is to recognize the validity of and promote the development of electronic communications in commercial and non-commercial dealings and in dealings with government entities and to remove uncertainty about using electronic methods to satisfy various legal requirements about documents and record keeping.

Quarter 2 2008 Trading on the South Pacific Stock Exchange

| Company | Total No. of Shares Traded | Total Value of Sharea Traded (\$) | No. of Trades | Last Price Traded this Qtr (\$) | Qtr 2-Qtr 1 (% Change) | Earnings Per Share Traded (cents) | Price/Earning Ratio (times) | Divided Yield (%) | Market Capitalisation (\$m) | |
|------------------------------|----------------------------|-----------------------------------|---------------|---|------------------------|-----------------------------------|-----------------------------|-------------------|-----------------------------|-----------------|
| Atlantic & Pacific Packaging | 10,000 | 7,000 | 1 | 0.70 | - | 3.60 | 19.47 | 3.57 | 5.60 | |
| Amalgamated Telecom Holdings | 132,687 | 134,616 | 28 | 1.04 | 14.29 | 9.84 | 10.57 | 6.73 | 438.99 | |
| Communications (Fiji) | 22,400 | 33,199 | 8 | 1.50 | 2.74 | 12.39 | 12.11 | 4.00 | 5.34 | |
| Fosters Group Pacific | 6,125 | 79,625 | 7 | 13.00 | (1.52) | 77.19 | 16.84 | 3.46 | 135.31 | |
| FijiCare Insurance | 1,225 | 796 | 1 | 0.65 | - | 9.49 | 6.85 | 6.15 | 3.92 | |
| Flour Mills of Fiji | 114,400 | 81,446 | 5 | 0.73 | (2.67) | n/a | n/a | 2.74 | 109.50 | |
| Fiji Sugar Corporation | 13,066 | 4,531 | 6 | 0.35 | 2.94 | 14.06 | 2.49 | - | 15.54 | |
| Fiji Television | 49,155 | 160,867 | 16 | 3.36 | 0.30 | 8.32 | 40.39 | 5.36 | 34.61 | |
| Kontiki Growth Fund | - | - | - | 0.87 | - | n/a | n/a | - | 3.08 | |
| Pacific Green Industries | 114,830 | 241,060 | 5 | 2.10 | (2.33) | 5.43 | 38.70 | - | 16.00 | |
| R B Patel Group | 15,137,654 | 21,203,750 | 22 | 1.67 | 5.03 | 14.26 | 11.71 | 8.38 | 50.10 | |
| The Rice Company of Fiji | - | - | - | 2.45 | - | 24.66 | 9.93 | 6.94 | 14.70 | |
| Toyota Tsusho | 858 | 1,682 | 1 | 1.96 | - | 8.82 | 22.23 | 2.55 | 27.50 | |
| VB Holdings | 1,000 | 3,000 | 1 | 3.00 | 2.39 | 16.48 | 18.20 | 4.00 | 4.59 | |
| Yaqara Group | - | - | - | 1.18 | - | n/a | n/a | - | 17.99 | |
| Fijian Holdings | 210,077 | 461,453 | 142 | 2.16 | (11.48) | 73.52 | 2.94 | 9.26 | 22.60 | |
| TOTAL | 15,813,477 | 22,413,025 | 243 | Market Capitalisation as at 30 June 2008 | | | | | | \$905.36 |