Lastly, when considering the regulatory elements in play in each of the geographies we find that these elements play a substantial part of companies’ decision making when considering where to raise capital and where to raise equity, in particular. 3

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Executive Summary

Within this report we examine the capital market structures and regulatory elements of the Australian, Canadian and South Korean capital markets focusing on financing methods available, uptake of these financing methods and capital flows into corporate bonds and equity.

Finding that Australia, Korea and Canada have large, highly functional debt and equity markets offering similar methods, or forms of capital in all the three geographies.

In addition, analysis of the uptake of these financing methods and capital flows finds that;

- The Australian equity market is the smaller of the three but all three sit with the top ten exchanges in the world in market capitalisation terms,
- The Australian bond market is immature and smaller than that of Canada and Korea,
- Australian listed companies are funded mainly from internal sources to sustain operations and undertake new investments,
- Banks in Korea provide attractive rates for companies (compared to Australian and Canadian markets), but this in turn results in higher default rates,
- Canadian and Korean non-financial companies use the bond market as a source of funding to a greater degree than Australia, with Australian non-financial companies using bank loans as their main source of funding,
- Debt to equity ratios of non-financial companies in Australia are the highest of the three geographies, at 80%, whereas ratios in Australia and Canada are on par when comparing Top listed companies,
- Korean debt to equity ratios in both non-financial and top listed companies are below 50% due to Government policy requirements to reduce debt to equity ratios post the Global Financial Crisis, and
- In Korea 90% of the bond market is domestic with only a 10% foreign bonds. However, Canada and Australia both have a higher adoption rates of foreign bonds.

Lastly, when considering the regulatory elements in play in each of the geographies we find that these elements play a substantial part of companies’ decision making when considering where to raise capital and where to raise equity, in particular.
Financing methods available - Australia, South Korea (Korea) and Canada

Common to Australia, Canada and Korea are the opportunities for businesses to raise capital via debt or equity through private or public markets. Before looking for additional capital, businesses take advantage of tax incentives to internally fund growth through retention of earnings. At any time, additional capital is required for growth, a business must decide first between the benefits of borrowing money or selling equity. This decision is affected by the business owners’ strategic intention, its current makeup of debt and equity and market conditions.

There are many theories which explain the behaviour of the firm in making financial leverage decisions. Each theory presents a different explanation of corporate financing. For example, Myers and Majluf\(^1\) presented Pecking Order Theory which states that the firms prefer to use their internal financing sources to equity financing. External financing is only used if the internal financing does not meet the needs. First firms apply for bank loan, then for public debts, and as a last resort, equity financing is used. Thus, the profitable firms are less likely to opt for debt for new projects because they have the available funds in the form of retained earnings.

Companies with debt financing are able to deduct interest repayments in offsetting their tax bill in all 3 geographies. Therefore, companies are encouraged to hold higher debt-to-equity ratios. The form of debt financing used for acquisitions is predominantly commercial loans that can include term loan and revolving credit facilities (at times put in place to pay the interest under the term loan when cash flow from the portfolio of companies is expected to fall short to meet the interest coverage). The characteristics of enterprises in Canada and Australia are similar to South Korea, with domestic banks and credit unions providing the majority of debt financing to Small to Medium Enterprises (SME’s).\(^2\)

<table>
<thead>
<tr>
<th>Benefits of alternative financing methods</th>
<th></th>
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<tbody>
<tr>
<td>Debt Financing</td>
<td>Equity Financing</td>
</tr>
<tr>
<td>Retention of business ownership</td>
<td>No requirement to meet repayment schedule</td>
</tr>
<tr>
<td>Debtors have no input to management</td>
<td>In case of bankruptcy, no repayment obligation</td>
</tr>
<tr>
<td>Interest repayments are tax deductible</td>
<td>Profit can be reinvested rather than loan repayment</td>
</tr>
<tr>
<td>More certainty in returns schedule</td>
<td>May be easier to secure where assets/cash flow are more uncertain</td>
</tr>
</tbody>
</table>

Conventionally, debt and equity decisions are between those that exist in the private market and those which are provided on the local exchange.


\(^2\) Lepone, A & Wright, D: “Capital Market Structure Comparisons”, Financial Services Council (FSC), 2014
Whether businesses favour public or private sources is also a factor decided by markets and regulations, proportions and characteristics of the economy sectors in each country. Each of Australia, Canada and Korea has a different taxation and regulatory regime which includes locally unique provisions. The effect of government initiatives in tax and regulation is intended to stimulate the economy through each respective capital-oriented activity. Variations in each economy’s debt and equity markets also influence the decisions of companies seeking capital, in turn affecting the capital structure of businesses as they grow. In other words, a business of a given size that faces a similar decision in each economy will be also influenced by a combination of local benefits and costs of financing.

**Debt**

Australia, Korea and Canada have large, highly functional debt markets serving public and private companies. These include bank loans, financial leases, term loans and mortgage loans and issuance of bonds ‘over the counter’. Listing on exchanges adds the option of issuing exchange-traded bonds. An articulation of the differences of bonds available in each of the 3 geographies is included further in this report.

**Equity**

Private and public companies in each economy have the option of raising equity finance through expansion of their respective share structures. The choice to move to exchange based equity sales (or repurchases) is a balance of the costs, scale and the depth of capital available through those means. Exchanges provide the chance to raise equity capital through IPOs, rights issues, share purchase plans and placements. Hybrid forms of debt/equity capital typically are convertible bonds, reset preference shares and setup preference shares.

**Secondary offerings**

A Secondary offering is where a company seeks further equity capital raising post its IPO;

- Korean companies who have already listed and offered shares through an IPO can issue new shares by offering them pro-rata to existing shareholders. Offering new shares to new investors is allowed in limited circumstances e.g. innovation partners, so as not to impact the rights of existing shareholders.
- Australian Companies offer through a rights issue, a similar process to Korea; Placements, new shares offered to selected investors; a Dividend reinvestment scheme, where shareholders may reinvest their dividends; Share purchase plans, new shares offered however they may not be pro-rata.
- Canada favours Placements to issue new shares with rights issues also an available method however used less frequently than in Australia.

Bank lending is the most common source of external finance for many SMEs and entrepreneurs, which are often heavily reliant on traditional debt to fulfil their start-up, cash flow and investment needs. While it is commonly used by small businesses, however, traditional bank finance poses challenges to SMEs, in particular to newer, innovative and fast growing companies, with a higher risk-return profile. Capital gaps also exist for
companies undertaking important transitions in their activities, such as ownership and control changes, as well as for SMEs seeking to de-leverage and improve their capital structures (New Approaches to SME and Entrepreneurship Financing: Broadening the Range of Instruments - OECD).

Australia

In Australia, banks have been tightening lending standards and in certain industries increasing collateral requirements for some time. Increased requirements are intended to make a more resilient and shock proof banking sector and the consequences have affected the amount of funds available to resources and property/construction services. Australian banks have in recent times reduced their exposure to international investments and that is thought to make them safer from foreign economic shocks. Meanwhile Australian businesses have access to debt finance from a wide range of international lenders who are increasing their participation in the economy, if somewhat more seasonally.

As a result of ongoing tightening of lending standards; “Businesses generally remain in good financial health, with aggregate levels of gearing around their historical averages and the earnings of listed corporations broadly in line with prior periods. Most businesses appear well placed to meet their debt obligations. An exception is companies in the resource-related sector, which continue to face much lower commodity prices than a few years ago, weighing on earnings.” (www.RBA.gov.au)

To raise capital on the Australian Stock Exchange (ASX), the minimum size requirement is small enough (\$10m Market Cap) for Australian businesses to transition from private to public equity issuance while still using debt issued by local banks. The effect is to simplify the capital structure throughout growth of Australian businesses and giving earlier access between public investors and listing companies. The availability of bank debt to exchange listed-sized businesses means that bond issuance is less desirable for its complicated processes except by large companies. Regulation is provided by the Australian Securities and Investments Commission (ASIC).

Canada

Canada’s Banking sector is considered one of the safest in the world. The five big banks provide quality services with a high level of market penetration of digital instruments such as online and telephone banking. They are also involved in insurance and operate mutual funds, so that banking customers have few other places needed to go to for financial services. Canadian banks are also moving with the development of FinTech;
“Banks recognise that they have much to gain from FinTechs’ innovations: soon, many FinTech driven offerings may become pivotal elements in banks’ operating models, enabling banks to reduce costs, reach underserved markets and open up new products and revenue streams.”

Including second tier banks there are a total of 31 banks in Canada. Big banks, being not allowed to merge any further, have expanded into USA markets with additional services on offer such as brokerage. Borrowers receive integrated services along with their debt provision from big banks.

To raise capital on the Toronto Stock Exchange (TSX), the minimum market a capitalisation requirement is $4-$10m depending on the industry the company is associated with. Companies looking for private equity and venture capital can look for information at the Canadian Venture Capital and Private Equity Association (CVCA). The CVCA works with members to improve the industry and drive growth.

The TSX offers Canadian businesses the opportunity to raise public debt and equity capital. The minimum requirements to list here are not categorically different from the ASX as to create a different market outcome but there are many more types of listing options to decipher at first. Canada’s capital markets regulators are organised by the Canadian Securities Administrators.

Korea

There are seven major banks in Korea but it has a large number of additional lenders including government-run banks, nation-wide, local and foreign banks. Korea will bring new online-only lenders into the market in late 2016, increasing competition with newcomers (and their associated services) to the market for the first time in 24 years and compelling incumbent providers to improve their digital service offerings.

The Korea Exchange (KOPSI) was created from a merger of three previous exchanges and provides for equities, bonds, exchange traded funds (ETFs), exchange-linked warrants (ELWs), Real Estate Investment Trusts (REITs), futures and a derivatives market. Coordination of regulation is supplemented by the Korea Financial Investment Association. Korea’s economy has been built with strong use of foreign investment, companies located here receive assistance in attracting foreign capital from various organisations. However, as we will see in the following sections, the Korean government has some unique influences on the equity and bond markets which have the effect of altering their composition in comparison to Canada and Australia. The differences in the Korean debt and equity markets complement the characteristics and main drivers of the economy.


Uptake of the alternative financing methods - Australia, Korea and Canada

Sources of Funding - Companies

We distinguish between financial companies and non-financial companies when analysing sources of funds. Financial companies will naturally have significant higher debt compared to non-financial companies due to borrowings originating from their activities in the form of deposits from the public and a significant proportion of funding. Non-financial companies can be both public and private, due to the limited information available for private companies the following analysis considers a macroeconomic point of view. Data used is from various sources and assesses debt levels from an absolute and Gross Domestic Product (GDP) level.

Total Credit Advanced to Non-Financial Companies

Of note in the above is that Australian non-financial companies appear to be less levered compared to their Korean and Canadian counterparts based on % credit to GDP. In addition, the Canadian non-financial company credit market is the largest of the three markets based on absolute US$ basis.
Corporate Australia

Australian non-financial companies (listed and unlisted) have de-levered since the global financial crisis. External funding compared to GDP reduced in the period immediately after the global financial crisis (GFC). Business credit slowed significantly (negative immediately after 2008) due to the financial crisis with limited liquidity in the system at the time. In contrast, listed equity funding increased due to some listed companies raising equity during uncertain times to bolster capital. Business credit has increased post 2014 as the economy continued a very slow recovery. This is also evidenced in debt/equity ratios of non-financial companies reducing from a peak of 100% in 2008 to now stabilising just below 80% and in line with levels pre-2002. We further note that corporate Australia has less debt than their European counterparts but more than US corporations when compared on a GDP basis. This may evidence that the global financial crisis has made companies more risk-averse and banks more selective in advancing credit.
Sources of Funds – Internal vs External

From the total sources of funding chart above, the business activities of Australian listed companies are funded mainly from internal sources to sustain operations and undertake new investments. On a sector level, it is noted that significant differences in funding of operations and expansionary activities exist. Investment in the non-resources sectors (other than infrastructure) post 2008 has been weak and largely limited to maintaining the asset base rather than expansion. The post-crisis phase has been characterised by the modest use of external funding across all sectors.

Resources companies earned significant profits prior to 2008 due to elevated commodity prices and generated sufficient cash to fund expansions and operations. Some external funding was used to complete Merger & Acquisition (M&A) activities during this period. The spike in the resources sector was due to Rio Tinto’s acquisition of Alcan in a $44bn transaction. Post 2008 commodity prices declined and resource companies’ profitability reduced significantly. External funding was required to complete projects that commenced prior to the crisis. We believe external funding will remain low and projects scaled down if low commodity prices persist.

In contrast, infrastructure and real estate companies utilise significant external funding due to the nature of their operations. These sectors are capital intensive and require significant capital to develop their projects. The time to realise cash is also longer due to construction periods involved. Post 2008 we note that the real
estate sector hardly used any external funding and that the infrastructure sector started to raise external funding since 2013.

Included in other sectors are Retail, Telecommunications, Information Technology, Health Care and Services. These industries (apart from Telecommunications and to a degree Health Care) are not capital intensive and their cash conversion cycles are relatively short. These industries therefore do not require significant external funding. At and around the peak before the GFC external funding was used mainly for M&A activity.

**External Funding Debt vs Equity**

Most corporate debt (listed and unlisted) in Australia takes the form of banks loans which comprise approximately 75% of economy-wide debt financing for non-financial companies. This reflects the dominance of the major Australian banks as suppliers of funding. The corporate bond market is small and underdeveloped. Debt was the preferred source of external financing for the wave of M&A activity prior to 2008 with listed companies’ net debt cash flows peaking at 15%.

The average capital structures of Australian listed companies have varied significantly over time. This is mainly due to investment cycles and economic conditions. The average gearing of Australian listed companies is around 60%, however differences exist between sectors. It is noted from the debt composition chart that bank loans have much shorter maturities compared to bonds. This is consistent in both the resources and non-resources sectors.

The net gearing of the resources sector is below 40% and lower post the GFC. The resources sector is cyclical with companies experiencing significant variation in earnings. The decrease in gearing since the GFC follows
lower commodity prices and asset sales to reduce debt. Resources companies prefer lower gearing levels as evidence by their debt to equity levels, this is to avoid unnecessary liquidity and refinancing risks. The Infrastructure sector (including utilities) is the sector with the highest gearing after the financial sector (more than 100%). Infrastructure companies are capital intensive and large projects require significant investments.

Other sectors have low debt levels by comparison. This is mainly in conjunction with shorter cash conversion cycles and the use of operating leases to gain access to premises and equipment.

**Australia compared to corporate Canada and Korea**

**Canada**

**Asia (noting Korea)**

(Source: Statistics Canada) (IMF Asia Regional Outlook)

Canadian non-financial companies have lower debt levels compared to Australia with debt-to-equity ratios of below 60% compared to Australian of just below 80% at the same time. Whilst Korea on a debt-weighted average is slightly more geared than Australian non-financial companies.
Canadian and Korean non-financial companies use the bond market as a source of funding to a greater degree than their Australian counterparts. In contrast, Australian non-financial companies use bank loans as their main source of funding. Post GFC it is noted that Australian companies have de-levered to a greater degree than their Korean counterparts.
Comparing the Major Listed Companies

<table>
<thead>
<tr>
<th>Listed companies Net debt to equity ratios</th>
<th>2015 annual accounts</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Summary</strong></td>
<td><strong>Kospi</strong></td>
</tr>
<tr>
<td>Financials</td>
<td>132%</td>
</tr>
<tr>
<td>Telecommunications</td>
<td>55%</td>
</tr>
<tr>
<td>Utilities</td>
<td>75%</td>
</tr>
<tr>
<td>Information Technology</td>
<td>-42%</td>
</tr>
<tr>
<td>Health Care</td>
<td>19%</td>
</tr>
<tr>
<td>Industrials/Services</td>
<td>43%</td>
</tr>
<tr>
<td>Energy</td>
<td>123%</td>
</tr>
<tr>
<td>Materials</td>
<td>39%</td>
</tr>
<tr>
<td>Consumer discretionary</td>
<td>-6%</td>
</tr>
<tr>
<td>Consumer staples</td>
<td>60%</td>
</tr>
<tr>
<td>Total</td>
<td>48%</td>
</tr>
</tbody>
</table>

Source: Datascope
Comparing net debt to book equity of the ASX300 (300 largest companies listed in Australia), the KOSPI 200 Composite Index (200 largest companies listed in Korea) and the TSX Composite index (companies making up 70% of the market capitalisation in Canada). It is noted that Australian companies have debt levels similar to Canada on average whilst Korean listed companies have lower net debt levels.

The three highest geared industries on the ASX are financial, telecommunication companies and utilities. Telecommunication and utility companies require significant infrastructure such as networks and plants which account for the high levels of debt.

The abnormal TSX Healthcare ratio is mainly due to one company (Valeant Pharmaceuticals) who have accumulated significant debt on the back of acquisitions. The remaining sectors all have gearing levels less than 100% other than Energy Companies Listed on the KOSPI. These exchanges do not classify their constituent companies uniformly and we draw the conclusion that the remaining gearing levels are within expectations i.e. lower than banks, utilities and telecommunication companies.
Size and significance of capital flows into corporate bonds and equity

Bond markets

This section considers the size of bond markets and their composition. Bond markets are mostly segmented into government and corporate bonds. While the common theme in the 3 bond markets (Australia, Canada & South Korea) is regarding the stability the government bonds offer (so the lower returns), the high yielding bonds (non-government) have 3 factors that influence their returns:

- Interest rates have an inverse tendency on bond attractiveness,
- Consumer Price Index (CPI) puts pressure on the bonds and its returns,
- Credit ratings of the bonds and issuers have an implied value to its risk and therefore the yield.

In terms of the size of bond markets, only Canada is slightly larger when compared to Australia and Korea. While the Korean bonds are equally distributed between Financial companies (34%), Non-financial companies (33%) & General Government (33%); the Australian market is skewed where Financial companies ‘s taking majority of 58%; government bonds in Canada have a majority with 53%.

Source: (Bank for International Settlements, 2016)

Although the 3 Bond markets are similar in their sizes, they have differed in their offerings and composition. A summary of those markets follows.
Korean Bond Market

The Korean bond market has a bit of old style creativity embedded in its structure. The bonds are typically categorised by 4 types: government bonds, municipal bonds, special bonds, and corporate bonds. Government bonds are the nation-building bonds & municipal bonds are at state/local level equivalent to Government bonds (International Affairs Department, 2015). Corporate bonds are the ones with business/industrial objectives and the tier returns vary according to risk. The risks of these bonds are beared according to the type of bond (direct or indirect). Korea has a legal act that regulates bonds and its securities. It is called Secure Bond Trust Act (SBT). This act adds to investor confidence.

- Guaranteed bonds are similar to Australian bonds where issuing financial institutions provide guarantee.
- Collateral bonds are guaranteed recoveries in accordance to the SBT.
- High risk bonds are the ones where there is no guarantee from institutions. However, surprisingly most of the bonds are under this category (agencies with a credit rating of at least 2).

An interesting aspect of the Korean bond market is the way its secondary market functions. It has an over the counter (OTC) market where bonds are negotiated for price and terms. Though this appears not to be a standard, it is 80 -90% of the Korean bond market and is traded by the likes of institutional investors, companies and banks. In contrast the KOSPI national exchange (International Affairs Department, 2015) follows a competitive bidding process facilitated by automation. The figure below shows the Bond trading proportions between OTC and exchange markets.

![Graph](source: International Affairs Department, 2015)

Net foreign buying of bonds over the past decade shows that Government bonds and monetary stabilisation bonds (MSB) have a share above 99% of its total bond market (KRW 100.4tn by the end of 2014).
Canadian Bond Market

The Canadian bond market is categorised into regular and complex bonds (Ontario Securities Commission, 2016).

Regular bonds: These are just like any other bonds with a standard interest and period. Such bonds are issued by:
- Federal government & government agencies for nation building activities
- State and local governments (like municipal bonds)
- Corporate bonds issued by companies to raise capital for its business purposes

Complex bonds: These bonds are a mix of regular bonds in conjunction with other factors such as inflation. These corporate bonds subcategorised as Strip, Index and Real return bonds. These bonds generally have a higher yield compared to regular bonds.

Australian Bond Market

Bonds in Australia are categorised according to their interest payments and according to the issuer (ASX Bonds, 2016).

Bonds categorised based on interest
- Fixed rate bonds: As the rate of return is fixed, they have a risk of varying interest rates and their demand is reflective of the market interest rates.
- Floating rate bonds: They have flexible rates of return and the rates are adjusted periodically. Risks are lowered as rates are reflective of market rates during assessment periods. Most Corporate bonds fall into this category.
- Indexed bonds: These are long term bonds with interest rates reflective of inflation. Payments on maturity are adjusted based on face value of the bonds.

Bonds based on issuer
- Australian Government Bonds (AGB’s): These bonds are relatively less risky when compared to corporate bonds. Returns are tied to risk; AGB’s have less but secured returns. These bonds are issued as Treasury bonds & Treasury indexed bonds. These bonds are issued for typical fund raising activities by government and they are primarily used for nation-building purposes.
- Corporate bonds: These bonds are issued by companies raising funds for prospects. As they are listed by companies, their rates and conditions vary, details are usually in the prospectus. The yield is higher compared to AGB’s and is proportional to the risk.
**Domestic and international bonds**

While there is a similarity in the developed nations (Canada and Australia), Korea appears to have a different trend in terms of its local and international bond markets. International bond market in Korea is less than 10% of its total bond market (based on OTC markets). Data from the graph below show that Canada (38%) and Australia (31%) have higher diffusion and exposure to international markets (especially financial organisations). Australia has a strong financial portfolio whereby it displays risk management by distributing funds (superannuation and finance institutions) to spread its risks overseas along with local bond markets.

![International Bonds Chart](chart.png)

Source: (Bank for International Settlements, 2016)

In the domestic bond market, Korea and Canada have its bond wealth distributed evenly with 30% into non-financial corporations (industries), Australia (11%) has surprising low levels of bonds in the industries sector. This is due to the shifting manufacturing and other industries to Asian markets where Australia is now struggling with structural unemployment in these sectors. That said, Korea has better bond market where investment is favoured and entices investor contributions and trust in the industries sectors that has seen a substantial growth. With changes in the regulations of bond markets for foreign investors, there is an increase in foreign investment (due to confidence in a stable and growing Korean market). Thus, Korean investors don’t favour foreign bonds. However, Australian investors, mostly the superannuation fund managers and financial organisations, go overseas for investments.
Equity Markets

The USA leads the equity market with no other country having a size that is even half of the USA’s capitalisation. Australia, Canada and South Korean equity markets have seen a steady growth in their markets. Canada stands as the largest followed by Korea and Australia.

Source: (The World Bank, 2016)
Interestingly Korea has seen growth in its capitalisation for the past 2 years defying trends from Canada and Australia (figure below).

Source: (Index Mundi 2016)

Over the last decade, Canadian and Australian markets have made a higher contribution towards GDP due to the commodities sector. However, Canada has in recent years shown lower demand in the commodities sector by 15% total contribution towards GDP went downwards. On the other hand, Korea makes a healthy and steady display in its portfolio (industries and finance sectors) management making it more attractive to investors.
Korean increased by 135, Australia by 22 and Canada decreased with 149 delisting’s. Korean has experienced this phenomenal growth over a short period due to tax incentives offered by the Government to list in Korea.

Source: (The World Bank, 2016)

Regulatory review

The development of market economies weighs heavily on the role capital markets play. While fostering the development of the entire economy, the capital market’s regulatory and financing elements play an important role in a corporation’s financial structure. The following reviews how regulatory elements and other components of capital market design affect the balance of debt and equity issuance, investment and subsequently the availability of corporate financing options.

Government Policy and Taxation

In Korea, Government policy and the taxation system influence the balance of debt and equity issuance. The Korean government is actively involved in promoting the capital market. There are two unique policy stances implemented by the Korean government with regards to the capital market. Firstly, they gave tax incentives to encourage IPOs. Korea is the only developed country that has such pronounced government involvement in its stock exchange. This interventionist approach has allowed the Korean stock market to experience phenomenal growth over a short period. Secondly, Korean policy has been to lower firms’ debt-to-equity ratios.

In addition, Korea has instigated tax incentives for SME’s where if in certain rural districts or a technology company, tax on income is exempt for four years and reduced by 50% for the subsequent two years.

In Canada, the federal government offers guaranteed loans to encourage small business growth. The Canada Small Business Financing (CSBF) loan is designed to help businesses purchase, install, renovate and modernize
business equipment and other fixed assets. Established in 1961, the program gives access to loans of up to $1,000,000 for the financing of large assets, which then act as security to the loan.

One major change that has contributed to the informational efficiency of the Canadian-dollar bond markets occurred in 2000. The Bank launched a new system for regularly announcing its decision regarding the key policy rate, the overnight rate of interest. The Bank introduced a system of fixed announcement dates (FADS) which were designed to alleviate uncertainty around monetary policy in order to increase transparency regarding interest rate decisions.

In most countries, corporate dividends are taxed twice. Double taxation of dividends occurs when both a company and a shareholder pay tax on the same income. In other words, the company pays taxes on profits and subsequently distributes a dividend out of its after-tax profits. Shareholders must then pay tax on the dividend received as income. The double taxation situation can cause corporations to hold onto their earnings and give preference to debt over equity.

An arrangement in Australia, known as dividend imputation, eliminates the double taxation of cash payouts from a corporation to its shareholders. Australia has allowed dividend imputation since 1987. Through the use of tax credits called "franking credits" or "imputed tax credits," the tax authorities are notified that a company has already paid the required income tax on the income it distributes as dividends. The shareholder then does not have to pay tax on the dividend income.

For Korean companies that are lenders, interest income is to be included in ordinary income and is therefore subject to corporate tax at a rate of 11% to 24.2%, depending on the level of income. Interest income of offshore companies is to be withheld at 22%, while a reduced rate under a relevant tax treaty may be applied.

Capital gains from a Korean company’s transfer of equity must be included in ordinary income and is therefore subject to corporate tax at a rate of 11% to 24.2%, depending on level of income. Barring any exemption under a relevant tax treaty, an offshore entity’s capital gains on Korean shares is subject to capital gains tax at the lower of 22% of capital gains and 11% of the sales proceeds.

Transfers within the Korean market of Korean shares owned by an offshore entity are exempt from capital gains tax if the shares are listed. The shares are traded through the stock markets or the KOSDAQ market of the Korean Exchange provided the offshore entity’s ownership (that is, participation in the Korean company’s capital) has not exceeded 25% during the five year period preceding the transfer.

Australia collects capital gains tax only upon realised capital gains except for certain provisions relating to deferred-interest debt such as zero-coupon bonds. The tax is not separate in its own right but forms part of the income-tax system. The proceeds of an asset sold less its "cost base" (the original cost plus addition for cost price increases over time, however without adjustment for inflation) are the capital gain. Discounts and other concessions apply to certain taxpayers in varying circumstances. From 21 September 1999, after a report by Alan Reynolds, the 50% capital gains tax discount has been in place for individuals and for some trusts that
acquired the asset after that time and that have held the asset for more than 12 months. The amount left after applying the discount is added to the assessable income of the taxpayer for that financial year.

Currently, only 50% of realized capital gains are taxable in Canada at an individual’s tax rate. Capital gains made by investments in a Tax-Free Savings Account (TFSA) are not taxed.

The TFSA is an account that provides tax benefits for saving in Canada. Investment income, including capital gains and dividends, earned in a TFSA is not taxed, even when withdrawn. Contributions to a TFSA are not deductible for income tax purposes. A TFSA is not limited to cash savings only, but may contain cash and/or other investments such as mutual funds, certain stocks, bonds, or Guaranteed Investment Certificates (GICs).

There was an announcement in 2013 of an agreement between Ontario, British Columbia and the federal government to establish a cooperative capital market regulator. It is a system for one common regulator administering a single set of regulations to support efficient capital markets, protect investors, and manage risk. Similarly, in Australia confidence in the operation of the companies listed on the ASX is reinforced by the whole-of-market regulation undertaken by ASIC across all trading venues and clearing and settlement facilities, as well as the financial system stability oversight by the Reserve Bank of Australia (RBA) of ASX’s clearing and settlement facilities. ASIC also supervises ASX’s own compliance with the ASX Listing Rules as a listed company.

**Thin Capitalisation**

Thin capitalisation rules seek to limit the tax deductibility of interest paid on corporate debt, thus making it unattractive to increase leverage above certain levels, some countries apply this to foreign investors;

- In Canada if debt exceeds 1.5 times the shareholder equity, interest on the excess is not deductible,
- In Australia, this applies not only for foreign investors but Australian companies investing overseas and is applicable when debt exceeds 1.5 times the shareholder equity and the interest is greater than $2m,
- In Korea when debt exceeds 3-6 times the shareholder equity, depending on certain criteria, interest is not tax deductible.

**Corporate Financing Options**

According to Korean Capital Market Annual Review 2015, corporate financing through the Korean capital market (stocks and bonds) in 2015 reached KRW 131tn, up 7.5% from the previous year.

Market-based financing increased by 38.9% year on year, amounting to KRW 8tn. Both IPOs and paid-in capital increases once again showed better results than the year before, in particular, IPOs raised 1.7 times more capital, backed by offerings from industry giants such as Mirae Asset Life insurance. A 6% increase was witnessed for capital raised in the bond market.
The available corporate financing in Korea are: Bond market, fund market, equity market, derivatives market, trust market and pension market. Below is a table of corporate bond issuance from 1995 to an estimate in 2013.

<table>
<thead>
<tr>
<th>Year</th>
<th>KRW Listed Companies</th>
<th>Up-listed Companies</th>
<th>Subtotal</th>
<th>KRW Listed Companies</th>
<th>Up-listed Companies</th>
<th>Subtotal</th>
<th>ABS</th>
<th>Total</th>
<th>Redemption</th>
<th>Net Issuance</th>
<th>Outstanding (as of Year-end)</th>
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<td>11,763.45</td>
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</tbody>
</table>

Notes: Corporate bond issues, redemptions, and outstanding amounts by company size for all firms in Korea. Net Issuance is defined as total issues minus total redemption during the year. 2013 figures of issues and redemptions are estimated assuming the average amounts of issues and redemptions of Jan-Nov 2013 happened during December 2013. Outstanding amount as of 2013 year end is a trajectory assuming the same growth rate from its previous month. The unit is in KRW billion.

Source: Bank of Korea, Financial Supervisory Service.

(Source: Corporate Financing Choices in South Korea, Na Young Park 2015)
Regulatory components

Issuance costs

Issuance cost is a key component that affects the corporate bond market in Australia. The changes implemented over the last five years are expected to promote increased issuance into the retail corporate bond market.

Issuance costs, which have been cited as one of the key reasons why Australian corporates have refrained from issuing retail securities are gradually being reduced and flexibility in the nature of, and time period over which fixed income securities can be issued have both been increased. Global regulatory change may also indirectly play a role in the development of the Australian corporate bond market. For example, the International Regulatory Framework for banks commonly referred to as Basel III that is currently being phased in internationally is expected to increase the cost of bank lending to corporates and may encourage banks to take more of an advisory and management role in assisting corporates attract debt capital. There remains scope for further regulatory changes to place debt and equity on an equal playing field from a compliance cost perspective however the recent trend in this direction is expected to continue.

Superannuation Mandates

Additionally, the structure of the Australian superannuation has a twofold effect on the development of a corporate bond market. According to Dr Andrew Lepone, Dr Danika Wright 2014, Firstly, the largest average asset allocation of superannuation funds is to Australian equities (29%), while only 6% on average is allocated to Australian fixed interest securities. Secondly, while the vast majority of corporate bonds issued in Australia fall within the investment grade category (BBB- and above), Black et al (2012) report that most bonds issued by nonfinancial corporations in Australia are below the stringent mandates for most investment and superannuation funds. As such, many lower-rated companies find it cheaper to issue bonds offshore.
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Section 3


Section 4

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