May-Jun 2016

Bank+Insurance Hybrid Capital

Your problem now, Matteo

Italy hit as Brexit blues highlight weaknesses

Axa
Quality return

EBA
Pillar 2 split

Fitch
Solvency II Tier 1

building success together

JUNE 2016

Sabadell

BANCO SABADELL

EUR 1,000,000,000

0.625% Cédulas Hipotecarias Due 2024

Joint Bookrunner

JUNE 2016

DKB

DEUTSCHE KREDITBANK AG

EUR 500,000,000

Senior Unsecured Green Bond June 2021

Joint Bookrunner

MAY 2016

Santander CONSUMER FRANCE

SANTANDER CONSUMER FINANCE, S.A.

EUR 750,000,000

1.000% Senior Unsecured Due 2021

Joint Bookrunner

MAY 2016

DG HYP

DG HYP

EUR 500,000,000

Mortgage Pfandbrief March 2026

Joint Bookrunner

MAY 2016

MAPFRE

MAPFRE S.A.

EUR 1,000,000,000

1.625% Senior Unsecured Due 2026

Joint Bookrunner

APRIL 2016

COMPAGNIE FINANCEMENT FONCIER

COMPAGNIE DE FINANCEMENT FONCIER

EUR 1,000,000,000

0.500% Covered Bond Due 2024

Joint Bookrunner

APRIL 2016

TD

TORONTO-DOMINION BANK

EUR 1,000,000,000

0.375% Covered Bond Due 2023

Joint Bookrunner

APRIL 2016

Allianz

ALLIANZ SE

EUR 750,000,000

0.000% Senior Unsecured Due 2020

EUR 750,000,000

1.375% Senior Unsecured Due 2031

Joint Bookrunner

APRIL 2016

BMO

BANK OF MONTREAL

EUR 1,500,000,000

0.125% Covered Bond Due 2021

Joint Bookrunner

APRIL 2016

CRÉDIT AGRICOLE S.A.

CRÉDIT AGRICOLE SA

EUR 1,500,000,000

1.250% Senior Unsecured Due 2026

Sole Bookrunner

APRIL 2016

ABN·AMRO

ABN AMRO

EUR 2,250,000,000

1.000% Covered Bond Due 2031

Joint Bookrunner

APRIL 2016

LLOYDS BANK

LLOYDS BANK PLC

EUR 1,250,000,000

0.500% Covered Bond Due 2023

Joint Bookrunner

www.ca-cib.com

CRÉDIT AGRICOLE
CORPORATE & INVESTMENT BANK

Bank+Insurance HybridCapital

Contents

Bank+Insurance HybridCapital

Contents

Who's irresponsible now?

"That country now has collapsed — politically, economically, monetarily and constitutionally, and you will have years ahead of you to get out of this mess."

Dutch prime minister Mark Rutte's hyperbole can be understood given the heated atmosphere in the European Parliament where he was addressing UK MEPs including Brexiteer Nigel Farage. But — for the sake of its own citizens — the diminished EU would be better advised to reflect on its own future.

Indeed, the UK's decision to leave the EU has acted as something of a mirror for remaining member states, where support for the union enjoyed a bounce in opinion polls conducted in the immediate aftermath of the Brexit vote, possibly as electorates saw the chaotic financial aftermath of the surprise referendum result.

How will EU leaders themselves respond? The head of the liberal group in the parliament, former Belgian prime minister Guy Verhofstadt, characterised the European Council's attitude as "we shouldn't change anything, just implement existing European policies" — which he condemned as "shocking and irresponsible".

An early and portentous test will be whether, and if so how, the problems of Italy's banking system are addressed. Here, "national specificities" — to borrow a Brussels euphemism — clash with a Bank Recovery & Resolution Directive that has been placed at the centre of the EU's post-crisis financial architecture.

What will be sacrificed: principle, or Italian retail investors' savings?

Perhaps compromise is in the air: a European Banking Authority decision on 1 July to split Pillar 2 and thereby ease coupon payment concerns in the AT1 market looks like nothing less than a U-turn, albeit dressed up in face-saving language.

Can Europe's leaders perform a similar trick? With Italy's own referendum — on constitutional reform — due by November, the clock is ticking.

Neil Day,
Managing Editor
Bank+Insurance Hybrid Capital

Bank+Insurance Hybrid Capital

Published by Newtype Media

Neil Day
Managing Editor
+44 20 3269 2058
nday@bihcapital.com

Tom Revell
Reporter
+44 20 8961 8220
trevell@bihcapital.com

In association with

CRÉDIT AGRICOLE CORPORATE & INVESTMENT BANK

Vincent Hoarau
MD, Head of FIG Syndicate
vincent.hoarau@ca-cib.com
+44 20 7214 6162

Christian Haller
MD, Head of DCM Financial Institutions
christian.haller@ca-cib.com
+49 69 78901680

Julian Burkhard
MD, Head of Hybrid Capital & Liability Management
julian.burkhard@ca-cib.com
+44 20 7214 5472

Visit us at
bihcapital.com

Please see important disclaimer on page 37

Fulfilment & distribution
Celeritas Solutions

Newtype Media
184 Acton Lane
Park Royal
London NW10 7NH
United Kingdom
+44 20 3269 2058

Market news

Brexit lockdown stymies AT1 after Spring green shoots

The second quarter proved more constructive for Additional Tier 1 than had the mostly torrid opening months of the year, but although regulators did their part in bringing stability to the asset class, the positive sentiment was at first subdued and then dealt a body blow by the UK's Brexit referendum.

The second quarter had opened with the market still riding the impact of the European Central Bank's second wave of QE measures: the increase in the asset purchase programme's monthly target from Eu60bn to Eu80bn, a new round of targeted longer term refinancing operations (TLTRO II), and a cut in the deposit rate.

After no AT1 had been launched in between mid-January and mid-March, in the US dollar market BNP Paribas followed on the heels of a UBS reopener and in April BBVA and Rabobank tapped euros. However, the recovery in sentiment after a turbulent first two months of the year was most strongly felt in Tier 2, where a steady stream of supply hit the market through April and May — albeit still subject to short windows.

The AT1 market itself enjoyed a last pre-UK referendum hurrah in euros as Erste Group Bank sold the first Austrian AT1 on 25 May. The Eu500m perpetual non-call October 2021 deal was the first subordinated issue from Austria since 2014 — during which Erste had missed a coupon on legacy Tier 1 — and came after the announcement of an agreement between the Austrian government and Heta bondholders. The deal hit a strong primary market to attract more than Eu2.25bn of demand from over 200 accounts, and was priced with a coupon of 8.875%.

The first semester nevertheless effectively ended a month early as the UK referendum loomed, with opinion polls increasingly showing a likelihood that the electorate would vote to leave — even if the market at the time of the vote failed to price in such an eventuality. Erste's issue was the last AT1 in euros, while the last US dollar AT1 of the first half was an ANZ international debut on 6 June *(see separate article)*.

UKIP MEP Nigel Farage
Photo: European Parliament

"The whole market was in lockdown for Brexit for the whole of the month," said Nigel Brady, credit financials trader at Crédit Agricole CIB. "The market then started to price in the fact that we would remain and obviously got massively caught offside — we were trading close to the highs in a lot of names and that's why the move we saw was so large."

> 'Expect a bumpy ride into year-end'

Amid the wider sell-off in financial markets — not least of sterling — AT1 fell between five and 10 points, with UK and peripheral names being the worst hit. However, prices soon rebounded and the AT1 market emerged from the Brexit fallout relatively unscathed.

"Over the course of the week we got back pretty much all of the losses," said Brady, "apart from the UK names, which were still trading probably three to four points lower than pre-Brexit. Core European names and peripheral names retracted all of the losses we saw on the Friday."

Indeed, some market participants have been taken aback by how the fixed income markets had apparently taken the UK vote in its stride.

"In the past days, one has wondered how the market took the shock vote some 13 days ago," said one syndicate banker. "Explanations have been given of good positioning going into the vote, well working hedges, half year-end, high cash balances, lack of street inventory, central bank support and stimulus expectations.

"Besides currency and yield predictions, most of the post-vote scenario analysis from research departments were wrong."

Another market participant said that supply/demand dynamics help explain the supportive tone.

"Right now, people are struggling to find the paper that they really want to buy," he said. "There wasn't much paper around in the street and there was very little selling on the back of all the events.

"What you can tell from that is that there really is an underlying fundamentally strong demand for this sector."

A new general election in Spain on Sunday, 26 June passed off relatively harmlessly as fears that the country could experience a similar political upheaval eased. Meanwhile, on the Friday the UK referendum result was announced, the ECB also revealed take-up in the first round of TLTRO II at the low end of expectations — sending mixed signals to the market.

On the regulatory front, the European Banking Authority on 1 July then addressed a key factor in the AT1 market's turbulence early this year by following up on encouraging noises from the European authorities to confirm a split in Pillar 2 requirements that eases MDA calculation and hence coupon payment concerns *(see regulatory section for full details)*.

However, in the first days of the second half UK risks began — using the expression of Bank of England governor Mark Carney — to "crystalise" and rumours that the Italian government would recapitalise its banks reached fever pitch *(see Italy feature for more)*. The latest EU bank stress test results are due on 29 July and further ahead Italy is due for its own referendum, on constitutional change, in the autumn.

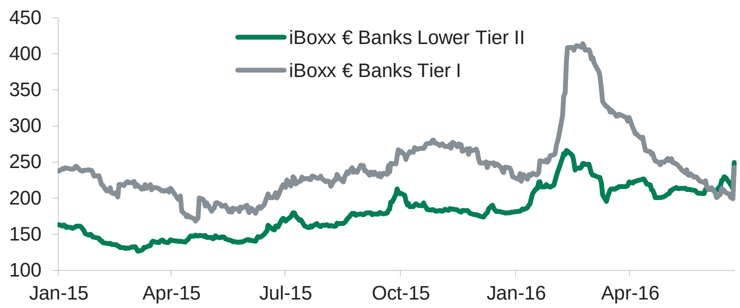
Political risk overall is expected to remain centre stage and cast a shadow over the market in the second half of the year.

"Everyone expects volatility to remain, what with the uncertainty on the macro-political side," said Viet Le, financial institutions syndicate manager at Crédit Agricole CIB. "In the short term, I can hardly see where any positive triggers are going to come from to get us out of this prolonged period of volatility.

"We've seen some buying on dips of stronger names across the capital structure, but underlying volatility makes it difficult for investors to take a stance and position in the high-beta space, so in terms of issuance there I wouldn't expect much in the coming weeks. You always want to stay optimistic, but given headline risk looming — Brexit/EU concerns, Italian banks, etc — expect a bumpy ride into year-end and consequently tight windows of opportunity for issuance." ●

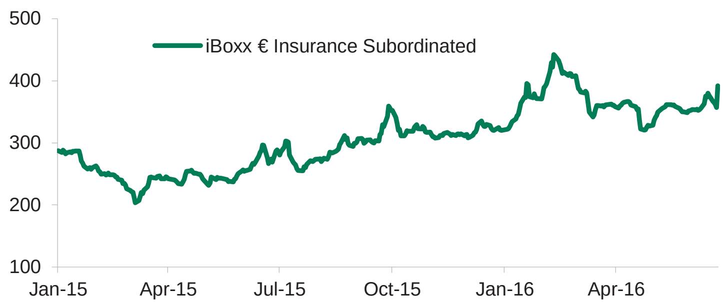
Photo: Erste Bank/Christian Wind

Secondary bank subordinated indices



Source: Markit, Crédit Agricole CIB

Secondary insurance subordinated index



Source: Markit, Crédit Agricole CIB

ANZ US$1bn blow-out takes Aussie AT1 offshore

Australia & New Zealand Banking Group (ANZ) launched the first Basel III-compliant Additional Tier 1 issue into international markets from Australia on 7 June with a US$1bn (A$1.36bn, Eu881m) perpetual non-call 10 deal.

The transaction is the first hybrid Tier 1 security from Australia since 2009, with only a break-through in the tax treatment of the new international issue making the re-entry possible. Hybrid Tier 1 issuance — usually structured in the form of mandatory convertible securities domestically — is treated as equity for tax purposes in Australia, with investors receiving part of their coupons in the form of tax credits.

According to John Needham, head of capital and structured funding, group treasury, at ANZ, provisions in Australia's tax legislation allow banks to pay coupons gross if issuing via foreign branches into international markets, but only through recent work with the Australian Tax Office has the administration of the provisions been updated to allow issuers to do this in practice, paving the way for the first international Basel III-compliant Australian AT1 issue.

"If you look back 10 years, ANZ had Tier 1 issues denominated in US dollars, sterling, euros and Aussie dollars," said Needham. "There were then a range of market and regulatory limitations that resulted in all of our AT1 being issued in Australian dollars and largely to Australian retail investors.

"So diversification of that investor base was our key objective, both in terms of investor type, country and currency. We've got some US dollar-denominated risk weighted assets so having US dollar AT1s is very helpful in hedging that."

He said that the US dollar market's ability to accommodate longer tenors was also key.

"The first call date is 10 years," said Needham, "while the recent deals in the

Australian market have had call dates in the five to six year period only. The way we view our funding profile is that we aim to complete senior debt at five years and then lengthen out our capital profile to 10 years."

With the deal being the first international AT1 from the country, investors were focused on the way in which risks such as loss absorption and coupon deferral are treated in Australian structures, said Needham.

'A validation by global capital markets'

"And ANZ's consistent profitability and its earnings generation, which is really the key to understanding the consistency of coupons," he added.

ANZ's issue has an equity conversion trigger at 5.125% of Common Equity Tier 1 capital or at PONV, subject to a conversion floor of 20% of the share price at issue. ANZ's structure also includes a dividend stopper, which is considered attractive for AT1 investors but not an option for EU issuers under CRD IV. The issuer could also avoid the uncertainty around the interaction between Pillar 2 and MDA that caused volatility in EU AT1 issuance.

Leads ANZ, Citi, Deutsche, Goldman Sachs and Morgan Stanley went out with initial price thoughts for the Baa1/BBB-/BBB perpetual non-call 10 issue of the 7.125% area and after attracting US$18bn of orders priced the US$1bn deal at 6.75%. Market participants described the deal as a blow-out and noted that the level achieved compared favourably for ANZ to international issuers.

Needham said that the US dollar transaction, on an after-swap basis, came in line with ANZ's Aussie dollar curve.

"There was such strong demand," he added. "It reflects the level of interest in exposure to the Australian banking system and is a validation by global capital markets of the structure."

Needham acknowledged that expectations of limited supply from ANZ and other Australian issuers played into both the level of oversubscription and investors' interest in the paper. ANZ is targeting an AT1 level of around 2% of RWA, which is equivalent to around A$8bn.

"We have a mandatory convertible that comes up to its call date in December, of A$2bn," said he said. "So this transaction was about partially refinancing that security to keep us at 2% of RWAs."

"Our AT1 requirements are pretty much around refinancing our existing portfolio as it comes around to our relevant call dates, with a little bit of asset growth. The net result was that we were only ever going to go for US$1bn, and the market understood that."

Now that ANZ has reopened the international market, the way is clear for its peers to enter the market — albeit for similarly limited needs given the limited amount of new AT1 that the Australian banking system requires.

"For all the reasons that we executed a transaction, you would think that would also be of some attraction to the other banks here," said Needham. ●

SMFG euro Japanese HoldCo debut impresses

Sumitomo Mitsui Financial Group (SMFG) launched the first HoldCo transaction in euros from a Japanese G-SIB on 7 June and attracted Eu2.75bn of demand to its Eu1.5bn 10 year deal at a level deemed attractive for the issuer.

Atsushi Ouchiyama, senior vice president, investor relations department, SMFG *(pictured)*, said that — having previously sold HoldCo debt in US dollars — the issuer targeted the euro market as one of the deepest and broadest bond markets in the world.

"In order to comply with TLAC regulation, having access to the euro market is very important in terms of diversifying the investor base for SMFG," he said. "The transaction strengthened SMFG/SMBC's liquidity profile and TLAC requirements, further diversifying SMFG/SMBC's funding sources with a maturity profile in line with overseas loan growth."

The deal was the latest in a series of successful moves into the TLAC/MREL-eligible liability space, and Ouchiyama said that these had been encouraging.

"To be honest with you, we did not see the KBC and Nykredit transactions as having direct impact on our transaction because KBC, Nykredit and SMFG are in different jurisdictions and each issuer targeted a different tenor," he said. "However, the strong demand for those transactions and strong secondary performance were a very positive sign for us to decide to jump into this market."

Leads Goldman Sachs, SMBC Nikko, Barclays, BNP Paribas, Deutsche Bank and HSBC went out with initial price thoughts of the mid-swaps plus 110bp area and priced the Eu1.5bn 10 year deal at 105bp over on the back of Eu2.75bn of demand. A banker away from the leads put the new issue premium at "only" 10p and market participants were impressed at the level paid by the Japanese name.

"We understand some market participants expected wider HoldCo-OpCo spreads in euros for our transaction by comparing with European banks' HoldCo-OpCo spreads," said Ouchiyama. "The tight HoldCo-OpCo spread shows investors' comfort with the strong TLAC framework in Japan."

He said that the distribution — 64% to Europe and 36% to Asia — was similar to past OpCo issuance, but with slightly more demand from Japan, reflecting the negative yield environment there.

"The success of the transaction is a testament to the Japanese name," added Ouchiyama. "We believe the transaction offers a benchmark for future Japanese issuance.

"SMFG/SMBC would like to solidify frequent issuer status in the euro market going forward to broaden its investor base further." ●

League tables

Bookrunners all European FI hybrids (euros and US dollars)
01/01/2016 to 30/06/2016

	Managing bank or group	No of issues	Total EUR m	Share (%)
1	HSBC	18	5,850	13.6
2	BNP Paribas	14	4,863	11.3
3	UBS	14	3,562	8.3
4	Barclays	7	2,463	5.7
5	Goldman Sachs	12	2,098	4.9
6	Morgan Stanley	14	2,008	4.7
7	Crédit Agricole CIB	7	2,006	4.7
8	Deutsche Bank	8	1,975	4.6
9	BAML	11	1,836	4.3
10	JP Morgan	11	1,720	4.0
11	Citi	9	1,668	3.9
12	Natixis	8	1,520	3.5
13	Credit Suisse	9	1,303	3.0
14	UniCredit	4	663	1.5
15	Société Générale CIB	5	629	1.5
	Total	73	42,918	

Source: Dealogic, Thomson Reuters, Crédit Agricole CIB

Bookrunners all financials (euros)
01/01/2016 to 30/06/2016

	Managing bank or group	No of issues	Total EUR m	Share (%)
1	Goldman Sachs	27	10,985	8.8
2	HSBC	36	10,384	8.3
3	BNP Paribas	34	9,639	7.7
4	Deutsche Bank	31	8,590	6.9
5	Crédit Agricole CIB	20	8,277	6.6
6	Société Générale CIB	26	7,726	6.2
7	Barclays	31	6,687	5.4
8	Citi	20	5,857	4.7
9	Natixis	13	5,434	4.4
10	UBS	22	5,396	4.3
11	JP Morgan	27	5,107	4.1
12	Credit Suisse	17	4,272	3.4
13	Morgan Stanley	16	3,190	2.6
14	RBS	11	2,973	2.4
15	Commerzbank	13	2,453	2.0
	Total	199	124,770	

Includes banks, insurance companies and finance companies.
Excludes equity-related, covered bonds, publicly owned institutions.

Innovative Nykredit SRN augurs well for Tier 3

Nykredit Realkredit launched what has been touted as the first Tier 3 instrument in the new bail-in era on 6 June, a Eu500m three year "senior resolution note" (SRN) that sits in between the issuer's senior unsecured debt and junior loss-absorbing debt and whose reception was said to augur well for similar forthcoming issuance.

While issuers in the UK and Switzerland, for example, have been issuing HoldCo debt to meet MREL/TLAC-type requirements, other European countries — such as France and Spain — have been working on creating new classes of instruments specifically tailored to these. However, Nykredit's new issue differed from either of these routes by being both issued by the operating company of the group and based on not a legislative but a contractual structure.

"The senior resolution note is designed to do the same trick as the instruments you have in other countries," said Morten Bækmand Nielsen, head of investor relations at Nykredit.

Danish mortgage credit institutions — not being deposit-taking — are exempt from MREL, but have to hold a bail-in buffer of 2% of their mortgage assets. For Nykredit Realkredit, this is equivalent to approximately Eu3bn and the SRN contributes towards funding that, according to Nielsen.

The SRNs are also expected to support Nykredit Realkredit's Standard & Poor's rating by contributing to its ALAC buffer and helping maintain one notch of ALAC support for its senior credit rating. S&P cut the issuer's rating from A+ to A, on negative outlook, in July 2015 when removing systemic uplift from its Danish bank ratings upon BRRD implementation, but a further notch of downgrade was avoided by measures including a commitment by Nykredit to build up an ALAC buffer of 5% of risk-weighted assets by mid-2017 — which it had already started doing before the SRN through, for example, Tier 2 issuance.

The SRNs are rated BBB+ by S&P, two notches below Nykredit Realkredit's senior unsecured rating, but Fitch rated it at the same level as senior unsecured debt, A.

Nykredit embarked on a two-team roadshow on 30 May to explain the new structure.

"It was basically the first time anyone had tried to issue a similar instrument," said Nielsen. "Given that in our specific case it was not based on legislation but rather on a contractual set-up, we thought we would have to explain this very thoroughly so we could be absolutely sure that people are on board.

"And the feedback we got from investors that this was a nice, clean story. Nykredit is relatively easy to understand, and they could also see the legal structure and where this instrument would sit."

'It was positioned in line with HoldCo senior'

Discussion then turned to where the new instrument should be priced in the wide range between senior unsecured and Tier 2.

"There were two schools of thought," said Nielsen. "The majority of investors came back and said they were around the area we eventually opened the book — at 125bp. And then there were some investors, but not a lot, who saw it around 30bp wider — they were more in the Tier 2 camp, so to speak.

"But there were so many in the lower spread camp that it didn't really matter."

After leads BNP Paribas, Goldman Sachs, Morgan Stanley and Nykredit Markets went out with the initial price thoughts of the 125bp over mid-swaps area for the Eu500m no-grow transaction, they were able to re-offer the paper at 110bp over on the back of more than Eu2bn of orders from some 165 accounts, and the paper tightened in the aftermarket.

"It went well above expectations," said Nielsen. "No-one had done this before, so we didn't really know what to expect.

"But we were happy when we printed it and investors were happy with the performance. It can't get much better than that."

A banker at one of the leads said that the pricing compared with fair value of 95bp-105bp over based on HoldCo-OpCo and HoldCo-Tier 2 differentials.

"It was positioned in line with HoldCo senior from the Brits and the Swiss," said Nielsen. "And then we probably also benefitted from the fact it was our first transaction of this kind, and that our funding need in this instrument is relatively limited, compared to the likes of HSBC and the other big guys.

"We said quite clearly that we could have an issuance need of up to Eu2bn. So you can see that we wouldn't flood the market with this type of this instrument, but there could be other issues."

A syndicate official away from the leads said that, with MREL and the right tools to address it being the hot topic, the outcome was "good news". ●

Arkéa, La Banque Postale return with Tier 2 deals

Crédit Mutuel Arkéa returned to the Tier 2 market for the first time in eight years in May and was joined by La Banque Postale the following week, with the two financial institutions launching their Eu500m subordinated trades ahead of the introduction of France's new non-preferred senior debt instrument.

Crédit Mutuel Arkéa attracted close to Eu2.8bn of orders for its Eu500m 10 year Tier 2 issue on 25 May, taking advantage of favourable market conditions to launch its first Tier 2 transaction since 2008.

According to Jean-Pierre Gulessian, head of capital markets at Crédit Mutuel Arkéa, the institution decided to launch its first Tier 2 issue in some eight years to optimise its capital structure, with its existing Tier 2 issue due to be redeemed in 2018, and to build its bail-in buffer.

"We have said that we want our senior bondholders to be completely non-bail-in-able," he said, "and as a consequence we have to increase the proportion of bail-in-able debt."

The issuer decided to approach the market after a roadshow following the announcement of its annual results in mid-April, with market conditions having improved after the turbulent start to the year for subordinated debt markets.

"We issued at this time due to stable market conditions and for internal considerations," said Gulessian *(pictured)*. "Before issuing, we wanted to make a roadshow presenting our 2015 annual results — as we regularly do after our annual and semi-annual results."

Starting on 13 April, the roadshow took in Germany, the Netherlands, Denmark and the UK.

"We discussed our financial results during this roadshow, but as they are very solid and our capital ratios and liquidity ratios are among the best of European banks, it was not the main topics," said Gulessian. "We mainly discussed the development of our business and the new strategic plan, ARKEA 2020, we have set out for the next five years.

"Risk management, capital requirements and all the new regulations — MREL, TLAC, Basel IV — of course came

up. We also had some questions about our ongoing internal conflict of interest with CNCM (Confédération Nationale du Crédit Mutuel)."

A press release was published by CNCM on 18 May discussing an informal proposal from Crédit Mutuel Arkéa to reach an agreement with CNCM consisting of organising an orderly split from the wider Groupe Crédit Mutuel. This proposal was rejected, and Gulessian said that the issuer has been transparent with investors about the situation and that, while the issuer gave investors time to assess the latest development, the news did not really affect investors' sentiment.

'We have succeeded in developing our investor base'

"We were able to proceed on 25 May and it was clearly a real success," he added.

Leads Crédit Agricole CIB, Crédit Mutuel Arkéa, LBBW, Nykredit and Santander opened books for the no-grow 10 year bullet Tier 2 issue — rated BBB by Standard & Poor's — with initial price thoughts of the mid-swaps plus 290bp area and demand surpassed Eu1bn within an hour and a half. Guidance was set at plus 280bp after demand passed Eu1.5bn and the Eu500m issue was ultimately re-offered at 270bp over on the back of more than Eu2bn of orders.

"The investor base was very large and the order book highly granular, with around 200 accounts involved," said Gulessian. "And we were very pleased to see that in terms of geographic diversification roughly 61% of the deal was bought by foreign investors in different European countries — such as Germany, the UK and Austria — and even a small part in Asia.

"We have been developing our investor relations for several years now and the results we have here proven that we have succeeded in developing our investor base, and that investors are confident in our name and in the quality of our credit risk profile."

A banker at one of the leads said that the pricing of 270bp over mid-swaps compared with levels of around 220bp-230bp for more frequent French issuers, although noted that pricing was largely based on feedback from investors.

"We are very satisfied with the outcome in terms of pricing," said Gulessian, "given that we had not been in this market for eight years and that we are not a frequent issuer, and this was thanks to the very strong momentum we achieved with the transaction."

La Banque Postale finds window

La Banque Postale entered the subordinated debt market the week after Crédit Mutel Arkéa, selling a Eu500m no-grow 12 year bullet Tier 2 transaction on the back of a twice oversubscribed order book on 31 May.

The deal comes after a Eu750m 12 year non-call seven Tier 2 deal for the French issuer in November 2015 and a Eu750m 12NC7 in April 2014.

"In recent years we have been a bit more regular in Tier 2 than we used to be because of the growth in lending activity and changes in regulations," said Dominique Heckel, head of long term funding at La Banque Postale. "It also provides us with a nice opportunity to develop the investor base. We are more active in covered bonds in the primary market, but as we have almost no real funding need, we are not at all active in the benchmark unsecured space for the moment.

First French non-preferred senior expected post-summer

The first issuance resulting from France's solution to creating a class of liabilities to meet MREL/TLAC requirements — so-called non-preferred senior — is expected in the autumn, with the relevant law in the middle of being approved by the French parliament.

The relevant legislation — the "Loi Sapin 2", of which Article 51 includes non-preferred senior debt — was approved by the lower house of parliament on 14 June and is expected to be approved by the upper house in July. France's national champions could then open the market after the summer lull.

"We are hearing that it could get voted on in July," said one market participant, "so maybe that will give issuers the opportunity to get prepared in terms of amending their documentation accordingly, and maybe do some investor work to be ready to enter the market as soon as possible this year. Some of them need to issue before year-end."

Dominique Heckel, head of long term funding at La Banque Postale, said that the expected supply later in the year — of either Tier 2 or the new instrument — contributed to the issuer proceeding with its Tier 2 issue in the first half of the year. La Banque Postale itself could take up the instrument, he added.

"Non-preferred senior definitely might be an interesting tool for us to fulfil our MREL requirements," said Heckel (*pictured*). "I would say that once the legislation is in force, we will consider it in our funding and capital mix.

"We first need to know what the requirements will be, and we will then follow the developments in terms of pricing and investor demand. So let's see."

Crédit Mutuel Arkéa is also considering the new instrument.

"We will follow what happens with the non-preferred senior bonds," said Jean-Pierre Gulessian, head of capital markets at Crédit Mutuel Arkéa, "and we will carefully assess the advantages of these instruments versus Tier 2 — the difference in terms of pricing, and what will be the appetite from the investor side."

He added that the issuer now has limited need to issue non-bail-inable bonds and if it does return with either a non-preferred senior issue or Tier 2, it would probably be for a similar amount to its recent Tier 2 deal. ●

"Tier 2 is something that is always quite important for us in terms of accessing the market."

Heckel said that the issuer decided to frontload part of its Tier 2 issuance for the year, targeting a deal before the summer holiday period and also before the UK referendum on EU membership.

"We clearly identified some good, stable market conditions and also that more volatility could come in the following weeks, making it more difficult for issuers to access the market, particularly in the capital space," he said. "So it was very important for us not to wait too much into June."

La Banque Postale hit the market on the last day of May, on a Tuesday following a UK public holiday on the Monday and ahead of a European Central Bank meeting on the Thursday and US non-farm payrolls on the Friday.

"The market windows were quite limited," said Heckel. "So we decided to be as quick and as fast as possible, taking the first window available once we had decided that we were going to issue.

Leads Crédit Agricole, Credit Suisse, Deutsche Bank and Natixis going out with IPTs of the mid-swaps plus 235bp area for the Eu500m no-grow 12 year bullet, rated BBB- by S&P. Guidance was moved to the 230bp area with books over Eu1bn, and the paper was re-offered at 225bp over, representing a new issue premium of around 10bp.

"This was in line with our objective," said Heckel, "and at the lower end of the pricing range indications we got from syndicate desks in the weeks before launch. The limited size helped to achieve the competitive pricing, but it was also a way to address a very clear message to investors regarding our limited needs."

The deal came amid a busy period for sub debt and on the same day HSBC entered the Tier 2 market, also selling a 12 year bullet, with the UK bank raising Eu1bn at 240bp over mid-swaps following IPTs of 250bp-255bp on its A2/BBB+/A+ deal.

"The bookbuilding process was somewhat slower as a result," said Heckel. "With HSBC offering some premium on a better rated security, we can understand that it took investors more time to see how exactly they would allocate their orders.

"So it was interesting and challenging, but in the end both transactions were successfully launched — before we saw conditions rapidly become more volatile."

The choice of a 12 year bullet structure for the new issue reflected prevailing appetite for longer maturities, according to Heckel, who said that HSBC's deal underlined this.

"We identified it as a sweet spot for some insurance companies," he said. "It was also a good way to offer a 3% investment to those investors.

"We thought that after our two callable transactions it would be good to diversify the capital term structure as well."

Heckel added that the longer maturity limited somewhat the investor base and ultimate level of demand, but he said the Eu500m size meant the issuer was comfortable with this, and that the book was high quality and granular. ●

Photo: Shiny Things/Flickr

Axa
Quality return after volatility

Axa reopened the euro hybrid insurance sector on 23 March to sell its first new subordinated issue since 2014, a Eu1.5bn 31.25NC11.25 Tier 2 deal. Here, Nicolas Benhamou-Rondeau, Axa head of funding and capital markets activities — group treasurer, discusses the trade's execution and how evolving regulations are affecting the insurance hybrid space.

What was the rationale for this transaction?

The transaction was part of our funding programme for 2016, aiming at refinancing part of our outstanding debt.

The choice of a Tier 2 instrument was in line with the group's strategy communicated in December during our investor day, which gave some guidance on our capital management framework. With our group benefiting from a strong capital base and significant capital generation, we have the flexibility to rebalance our hybrid debt mix from Tier 1 to Tier 2. This obviously allows a cost optimization whilst taking advantage of our available Tier 2 capacity. The new Tier 2 was therefore a natural and efficient refinancing operation.

From a marketing perspective, we were confident a Tier 2 structure would be well received. The instrument is well understood by the market and is attractive to investors given the absence of loss absorption mechanism, cash cumulative coupons and step up.

Therefore, we considered the instrument would offer a good mix between risk and return in the current market environment. Additionally, we believed negative swap rates up to five years (or close) would clearly invite investors to move further on the maturity curve and in the subordination spectrum, which is very positive for the insurance hybrid market.

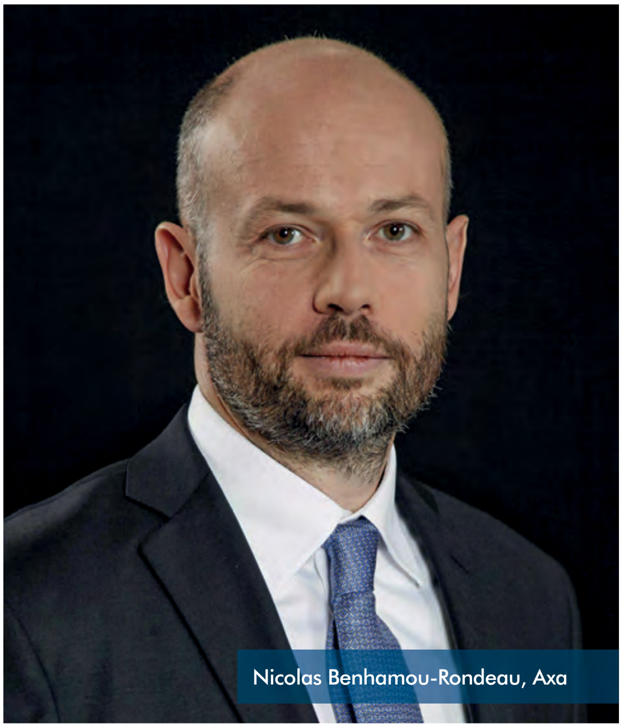
Market conditions were challenging in the first few months of the year, with subordinated products feeling the full force of the volatility. How did you navigate this difficult environment to execute a successful transaction?

Indeed, markets were extremely volatile early in the year and remain volatile so far this year, and we knew that a timely execution would be decisive. We had to be patient while keeping abreast of potential market turnarounds. We had the structuring phase finalised by January and we wanted to be in a position to hit the right market window.

Market conditions did not allow any execution in February given the strong risk-off sentiment mostly driven by concerns on oil prices and global growth, which pushed hybrid secondaries materially wider. The negative backdrop on AT1 amplified that sell-off.

By early March, the tone in the credit market became stronger, finally catching up with the rally we had been seeing over the previous few weeks in the equity markets, and the primary markets showed signs of life. However, our key concern was the potential for a very elevated new issue premium being required by investors given such volatile markets.

Two key triggers validated our execution window. First, the BNP Paribas 10 year Tier 2 deal — which, if I remember correctly, was the first subordinated euro deal since the market dislocation in January — was positively received with a limited new issue concession. Axa, like BNPP, benefits from strong name recognition and it was very encouraging to see that investors were now fully engaged in the hybrid space, at least for strong names.



Nicolas Benhamou-Rondeau, Axa

The second driver was obviously the latest round of ECB stimulus announced at its March meeting.

Post-ECB announcement, the primary markets were extremely supportive, being the only place where investors can add risk in size. In secondary, even if activity was fairly limited, our Tier 2 levels had retraced most of the early 2016 widening move, most likely also supported by the recently published strong set of results.

Yet, we had not seen any subordinated insurance deals in the euro market in 2016. So we felt that the first mover would have the greatest advantage.

We therefore decided to target the week of 21 March to take advantage of the constructive tone and to avoid the growing pipeline in the FIG primary markets post-Easter break.

The tragic events in Brussels on 22 March led us to wait further and we finally decided to announce the deal the day after, with a constructive market backdrop and investors still very much engaged despite Easter approaching.

At the end of the day, we achieved the lowest coupon ever (3.375%) for an Axa subordinated transaction.

With more than 300 investors involved in the transaction, is that an encouraging sign of investors' confidence in Axa's credit and also insurance hybrid markets more generally?

The extremely granular order book, with around 300 investors participating, clearly demonstrated Axa's very strong access to capital markets and the very good understanding of investors of its credit.

We were confident that the transaction would garner a lot of interest. First as I previously mentioned, fixed income investors are currently searching for yieldier products but would also tend to favour strong investment grade credit.

Secondly, Axa remains a relatively rare issuer in the hybrid capital space. The last time we came to the markets was in November 2014 and still it was only available to investors participating in our exchange offer. So basically our last public deal was actually in May 2014.

Finally, the euro market is our natural and core market and has proven depth.

We were extremely happy with the quality of the book. The final order book of more than Eu4.3bn was very granular, dominated by UK and French real money investors.

This overwhelming interest from investors allowed the order book to build very quickly, reaching the Eu2bn mark after only 90 minutes. The momentum in the transaction continued, with books growing steadily despite a 15bp tighter move from initial price thoughts.

With secondary levels having moved marginally since then, we believe we achieved the right level.

More generally — to fully answer the question — insurance hybrid paper is probably a rare asset class in the FIG space and investors are often keen on diversifying their investments. With Solvency II disclosure starting to be very well understood by the investor community, receptiveness to insurance hybrid paper is building up consistently.

What were the determining factors for the longer 31.25NC11.25 rather than the standard 30NC10 structure?

First and foremost, having a first call in 2027 helps smooth our debt maturity profile. Given the grandfathering period, the 2025/2026 bucket is relatively full with several Tier 1s having their first call dates around this period.

Axa remains a relatively rare issuer in the hybrid capital space

Furthermore, a long 31NC11 instrument allowed us to have our six month look-back pusher fully operational as Axa's dividend is usually around May.

Finally, given the flattening of the rate curve, investors' appetite remains strong for longer maturities.

With a size of Eu1.5bn, this was the largest subordinated Axa trade ever. What was the rationale for printing such a size?

The group targeted a benchmark size with the idea of printing at least Eu1bn. A Eu1.5bn deal was at the high end of our target. But given the very few available windows so far and the potential headwinds to come this year from macro news, namely the Brexit referendum, the Greece/Spanish uncertainties, or central banks' sometimes hard to decode messages, we chose to maximize the size.

The choice was even made easier given the granularity and the size of the order book, which allowed the large size not to be detrimental to the pricing.

How did you take into account the ACPR's position on tax-related features in subordinated instruments?

We incorporated the recent recommendation of the ACPR on Tier 2 to extend from five to 10 years the early redemption right for tax reasons on withholding tax.

We understood from our regulator that they consider the gross-up clause combined with a call option as an incentive to redeem. As a result, the possibility to redeem the bond in such an event is now optional and cannot be done before 10 years, unless replaced by instruments of at least the same quality.

Preserving the gross-up concept was, however, key, in our view, in order for French insurance paper to stay on that aspect in line with industry practice, investors' expectations, but also banks' and corporates' standards.

Finally, it should be noted that we included a "redemption alignment clause" allowing us to come back to the initial minimum five year maturity should the regulation change.

An "insolvent insurance affiliate winding-up" event has been inserted in the conditions to redemption and purchase. What is the purpose of this new provision?

After the PRA and the DNB positions on Recital 127 of the Delegated Act, we understood a specific contractual provision would be desirable to our regulator. The intention of Recital 127 is notably to prevent the repayment of any hybrid debt at the holding level should an insolvency event occur within any affiliate of the group.

Given the scale of our group, with many affiliates (sometimes with a relatively limited size) and several joint-ventures outside the EU, we were concerned that the automatic and systematic nature of such mechanism could have unexpected adverse consequences without necessarily solving the issue.

To mitigate this systematic effect, we have added a clause that allows the bond to be redeemed even if an "insurance affiliate winding-up" event has occurred should prior approval by the ACPR be exceptionally given. This allows for some form of materiality test on the event prior to blocking the bond repayment.

What are your plans for issuing other capital instruments such as Solvency II Tier 1?

As mentioned previously, the group has flexibility in terms of hybrid instruments and Tier 1 is not a priority for the moment.

This does not, however, preclude future use of Solvency II Tier 1, but not immediately.

Do you expect issuers to view Solvency II Tier 1 instruments as a viable way to raise capital?

Most of the recent SII publications showed strong Solvency II ratios, and that despite the market volatility. Moreover, as currently designed, the instrument would probably in most cases not cure any breach of the Solvency Capital Requirement (SCR), but would only strengthen the capital structure.

In addition, the structuring uncertainties that remain — for instance on the write-down/write-up mechanism — make it complicated to fully structure it for the time being.

Finally, pricing-wise, we can expect a significant premium versus old-style Tier 1.

In short, there is in theory no hurry to issue under such a format and most likely some fine-tuning to be performed. This being said, ongoing discussions of certain issuers with their local regulator and specific needs in some cases might result in Tier 1 issuances coming to the market in some jurisdictions sooner rather than later.

Tier 1 is not a priority for the moment

From an investor's perspective, the demand should be strong. Most investors likely to participate in new SII T1 transactions are already active in the bank Additional Tier 1 space. They are familiar with the concept of coupon and principal at risk.

I expect the key focus to be around the distance to trigger and the availability of distributable items to serve RT1 coupons. The recent disclosure on Solvency II provided more comfort to investors on European insurers' solvency positions, notably in terms of granularity of the capital structures, the capital targets, the sensitivities of the ratio.

I am also convinced that the structure could be seen as more friendly than AT1 given, for instance, the wider distance to trigger, investment grade rating for prime issuers, and no Maximum Distributable Amount concept for the time being.

What do you think of contingent capital instruments designed to mitigate the volatility of the solvency ratio margin?

Mitigating the volatility of the Solvency II ratio is a key objective in the insurance sector. This can actually be achieved with various capital management strategies targeting either the SCR itself or the available solvency capital.

When considering available solvency capital, there are a variety of contingent capital instruments currently being marketed. Some structures aim, for example, at building on the concept of ancillary own funds introduced by Solvency II.

Different triggers, host securities and conversion instruments can be envisaged, some being more efficient than others to mitigate the ratio's volatility.

However, for those that have been publicly issued, I personally still view them as expensive tools, in particular when the instruments do not provide any capital recognition on day one. ●

Belfius Stepping into Tier 2

Belgium's Belfius Bank launched its first Tier 2 transaction on 28 April, a Eu500m 10 year bullet. Here, *Ellen Van Steen*, head of long term funding at Belfius, explains how the debut fits into and builds on the bank's improving credit story.

What was the rationale for the Tier 2 transaction?

There were several reasons for Belfius to issue an inaugural Tier 2. The issue will increase our total capital ratio, which is already quite strong at a level of 17.7% phased-in at the end of 2015. A Tier 2 instrument is a logical step in the further establishment of the long term funding strategy of Belfius and, coming after the issuance of covered bonds and senior unsecured benchmarks, allows Belfius to climb up the ladder of juniority. It also contributes towards optimizing the maturity profile of our funding, and towards meeting the expected capital requirements. Finally, it is a further diversification of funding sources and of the investor base.

Why did you choose a 10 year bullet structure?

The feedback from investors clearly showed interest for the 10 year bullet format. We felt we could meet the deepest demand and have the interest of good quality investors with this structure. For an inaugural trade, we wanted all potential investors to be on board. Some investors, like insurance companies, for example, do not always like callable structures.

Ellen Van Steen, Belfius

Since your official roadshow last year, did you carry out some specific marketing in the meantime to prepare this transaction?

We have been meeting investors regularly since the official roadshow of May 2015. In fact, we have had an active investor relations strategy since the rebranding of Belfius Bank. With every yearly or half yearly results, we were able to show the improvement of Belfius and the realization of our objectives. The increasing profitability, the good results of the franchise, the accelerated tactical de-risking, the improvement in the capital ratios, a lower cost/income ratio… these were closely followed and appreciated by investors. We feel there is a continuing and increasing interest in and positive market sentiment towards the Belfius name.

After the release of our excellent 2015 results, we were on the road again meeting investors, and we were happy to notice again the increasing interest, and the positive feedback on a potential Tier 2 benchmark.

What messages about your credit story did you communicate to investors? We note that you were upgraded by Moody's in January and by Fitch in April.

Our messages concern the main topics of interest of the investors and rating agencies. Profitability, strategy, capital, funding and liquidity, the reduction of the "Side" (legacy) portfolio… are subjects they have been analyzing during the last couple of years. The bank has been evolving positively and constantly since 2012.

Photo: Belfius

We feel that we have made intensive communication on the one hand on the improvements — e.g. on the complete separation with the Dexia Group, the tactical de-risking of the Side portfolio and the strong results of the franchise — and on the other hand on our focus on the future, the strategy of Belfius for the coming years: the bancassurance model, the retail strategy, the focus on digital developments, the investments in the Belgian economy based on business and corporate activities and public and social sector.

How did you decide the timing of the trade?

We released our yearly results on 25 February. They were followed by an investor call and investor meetings. We received positive feedback and clear interest for Belfius issues. We also saw this interest in our private placement activity. Investors were spontaneously asking about the timing of our subordinated trade.

In April, the market was receptive to Tier 2 issues, with an important tightening of spreads, strong bookbuilding and secondary market performance.

With secondary spreads at their tightest level for months, and a positive market tone, we felt that we had all the elements in place to benefit from a constructive window to successfully issue our Tier 2 benchmark.

Were you satisfied with the result?

We are very satisfied with our inaugural Tier 2 benchmark — the transaction was a real success. We benefited from fast and fluent bookbuilding, demonstrating the interest in Belfius. Over 115 good quality accounts subscribed to the transaction, resulting in a well diversified and granular book of Eu2.1bn. The spread achieved was mid-swaps plus 255bp, which is very attractive in the current market environment. The bond also performed in the following days in the secondary market.

After the issuance of our Tier 2 benchmark we have seen that since the beginning of May markets have been more volatile, with some pressure on secondary spreads in Tier 2, which confirms that we benefited from good timing by reacting to a positive window.

Looking ahead, do you expect to continue to be active the subordinated segment, Tier 2 or AT1?

Belfius has no intention of issuing AT1 in the coming months, as it benefits from a strong Core Tier 1 ratio. The discussions around subordinated instruments and potential MREL-compliant instruments will be monitored closely. Belfius will further develop its issuing strategy to cover the MREL needs, which are limited.

Belgium has not implemented any modification to senior unsecured status, in contrast to what other European countries have done. What is your view on this topic?

Belfius does not have a HoldCo structure, and issues directly from the bank, which is the operating company. Belfius is analyzing the different solutions on MREL-eligible instruments proposed in Europe, and is considering the potential impact on its situation. For the time being, there is no official decision yet of the Belgian regulator on the preferred route. We consider that the French solution would be practical, straightforward and transparent for investors and issuers. ●

Efforts in the past year such as NPL reform and the launch of the Atlante fund raised hopes that alternatives to bail-outs/ins could be found to address capital pressures facing Italian banks — but then Brexit struck. *Neil Day* reports, and interviews two issuers who successfully raised Tier 2 before problems came to a head.

Italy's Ministry of Economy and Finance has over the past 18 months been running a Twitter campaign using the hashtag #prideandprejudice, aiming to highlight a purported gap between perceptions of Italy's economy and the reality. A March presentation from the Ministry on the topic was sub-titled "Something that no-one is saying about Italy".

While the Ministry has a right to feel aggrieved about ill-informed opinions, it may itself have spoken too soon about one of the points it highlighted as a virtue: a lack of state aid for Italian banks. In its presentation it noted that in the 2007-2014 period German banks received Eu262bn of state aid and UK banks Eu207bn, but Italian banks just Eu4bn — which as of March had fallen to Eu1.1bn.

Unfortunately, since the UK vote to leave the EU on 23 June, almost all discussions about Italy's economy have centred on the Italian government's efforts to find a way to support its banks, possibly to the tune of Eu40bn.

Within a week of the UK referendum the European Commission had approved use of an existing, precautionary scheme for up to Eu150bn of government guarantees for Italian bank debt — admissible under the Bank Recovery & Resolution Directive (BRRD) as "extraordinary public financial support". The move came as Italian bank shares tumbled after the Brexit vote and while the Italian government reportedly negotiated with the Commission about ways in which it could recapitalise its banks — with the latest European Central Bank stress test results looming on 29 July.

False dawns

Any state aid would be a last resort given Italy's previous efforts to address the problems its banks are facing — notably the impact of non-performing loans NPLs) on their balance sheets.

"In the first phase of the crisis in Europe a number of countries put a lot of government money on the table through state aid to the banking sector," says Lorenzo Codogno, visiting professor in practice at the London School of Economics' European Institute and founder and chief economist of LC Macro Advisors, who was formerly chief economist and director general at the Treasury Department of the Italian Ministry of Economy and Finance. "Then the Commission decided that enough is enough, so they introduced state aid rules with a transitional period until mid-2013 offering a last window of opportunity, and Italy decided at that time not to take it — contrary to many other countries.

"Then NPLs started to rise and in late 2014 Italy decided that it was about time to do something about it, and to introduce a bad bank. There were then very difficult and lengthy negotiations with the Commission lasting more than a year, and they resulted in a very modest outcome, which is basically that Italy was not allowed to introduce a bad bank, but was allowed to introduce guarantees for the most senior tranches of NPLs securitised into vehicles that banks can pay for only at market prices."

Since 2007 the stock of NPLs in the Italian banking system has quadrupled, with the deterioration mainly coming during the second leg of the financial crisis, from 2011 onwards, notes Codogno.

"Non-performing loans have mainly increased for two reasons," he says. "One is the depth of the recession, which inevitably caused problems for companies and increased the non-performing loans. And secondly, the length that it takes for banks to recover the credit in case of insolvency. In Italy insolvency procedures take much more time than in many other countries. Effectively for a bank to recover the collateral on a non-performing loan takes between six and eight years. And so inevitably with this situation, the stock of non-performing loans tends to rise."

Moreover, another observer points

UK and Italian prime ministers David Cameron and Matteo Renzi
Photo: European Union

Pride before a fall?

out that until recently Italian banks were not incentivised to properly provision NPLs by an extremely long tax amortisation period. As part of a package of Italian government reforms, this has now changed, although new more favourable measures will only impact new NPLs and not the existing stock.

"Why are NPLs so important?" adds Codogno. "Because clearly they absorb capital, they reduce profitability of banks, and they keep them busy with this rather than with providing new financing to the economy."

In February — as another element of its package of reforms — the Italian government introduced a scheme, Garanzia Cartolarizzazione Sofferenze (GACS), whereby banks can pay a fee for guarantees of investment grade senior tranches of securitisations of NPLs in which at least half of the junior tranches have been sold by the bank to other investors.

However, this was viewed as a bit of a non-starter by many.

"The perception is that it is not going to be particularly effective," says an analyst. "At the margin, it is probably a positive move, but in itself is not hugely effective, because it basically touches only on the senior tranche of securitised NPLs, and of course you need to sell the junior tranche first."

Twofold mission

On 11 April came an announcement that was touted by proponents as a breakthrough, but which was also been met with a large dose of scepticism in some quarters due to its limited size.

Quaestio Capital Management, an asset manager, launched an alternative investment fund backed by state bank Cassa Depositi e Prestiti, national champions Intesa Sanpaolo and UniCredit, and a variety of smaller banks, insurance companies and other investors, including some from abroad. An announcement two weeks later confirmed its size at Eu4.249bn.

Named Atlante (Italian for the Atlas of Greek mythology), the fund's aim has been twofold: resolving the NPL problem; and ensuring the success of capital increases required of Italian banks by acting as a backstop.

Lorenzo Codogno: NPLs absorbing capital, reducing profitability, and a distraction from new financing

The latter came onto the agenda thanks in part to the transformation into joint stock companies of the country's 10 largest cooperative banks (banche popolari) by the end of this year (alongside the consolidation of smaller cooperative banks — banche di credito cooperative — into larger groups). Despite being another well-intentioned element of the government's reform programme, the initiative forced some of Italy's banks to come to market to raise capital — to address their deteriorating balance sheets and meet European Central Bank requirements for CET1 ratios of 10% or more — at an inopportune time: Banca Banca Popolare di Vicenza and Veneto Banca were each due to raise Eu1bn-plus by May.

"In February we had this very difficult situation of low stock market values for most Italian banks," says a banker in Milan, "which triggered a lot of concern for these two IPOs. In absolute numbers those are not big transactions, but it was pretty evident that it would have been very difficult if not impossible to launch them."

Another notes that Banca Popolare di Vicenza faced uncertainty due to a misselling scandal involving the equity of the bank itself being sold to retail customers — another deterrent to investors.

As expected, the ultimate failure of Banca Popolare di Vicenza's IPO resulted in Atlante underwriting the entire Eu1.5bn capital increase and becoming 99.33% owner of the bank, and then at the end of June the fund became 97.64% owner of Vento Banca after its Eu1bn offering suffered a similarly disappointing fate.

Codogno says that given what was at stake, the industry had no choice but to support Atlante's interventions.

"The government cannot put in money and private investors are not willing to invest," he says. "So you have two choices: either close down the bank — which would be extremely risky given that under BRRD you have to bail-in bondholders and potentially retail investors. Or arrange some kind of private support for the banks, and this is exactly what Atlante did.

"Without its intervention, the failed IPO could have triggered a bank run, not only for Popolare di Vicenza, but maybe for a number of other weak banks in Italy."

Moody's reacted to the announcement of the fund by deeming it credit positive for weaker smaller and mid-sized banks in Italy, but less positive for stronger banks.

"For weaker banks in Italy, the new fund would help them improve their solvency and avoid a bail-in of bonds, including those held by retail investors," said the rating agency. "However, for healthier banks, the fund may create an expectation of ongoing support to weaker banks in the system, thus creating contingent liabilities."

However, proponents of Atlante point out that institutions such as Intesa and UniCredit would have been on the hook for the failed IPOs and any other aftershocks, while the banks themselves have highlighted the longer term benefits of the NPL initiative in combination with other government-led reforms.

"A comprehensive structural solution to the NPLs of the banking system may be reached through the introduction of measures, announced by the government, aimed at halving the NPL recovery time, bringing this into line with the European average," Intesa said when announcing its participation in the fund.

"The strengthened solidity of our country's banks, resulting from this solution, will allow them to provide more support to the real economy, increasing lending availability to households and businesses. It will also dispel the unfavourable perception of the market as to the stability of the banking system, which is detrimental to the savings of Italian people."

UBI reopens Tier 2 for Italians with Eu750m deal

UBI Banca launched the first Italian Tier 2 issue of 2016 on 27 April, a Eu750m 10 year non-call five deal priced at 4.25% from IPTs of the 4.5% area on the back of a Eu1.5bn book featuring some 180 accounts. Here, Giorgio Erasmi, head of funding at UBI Banca, discusses the reopener and its background.

Giorgio Erasmi, UBI Banca: 'The implemented measures are all steps in the right direction'

UBI had not been in the subordinated wholesale market for a long time. What was the rationale for the new deal?

We issued the new Tier 2 to maintain a Total Capital Ratio in line with our target range of 14%-15%. Before the transaction our Total Capital Ratio was in the lower part of our target; now it's 14.9%.

Market conditions were not obvious — what gave you the confidence that you could get the trade done?

During our marketing exercise we approached 100 investors! We met investors with an explicit interest in the Tier 2 asset class and the key one-on-ones were in Italy, London and Paris.

After the Atlante announcement there has been a reduction in volatility and market conditions were more stable, and we exploited that market window.

What are international investors' main concerns on Italy?

The main concerns were around NPL management and M&A. Thanks to Atlante's backstop on BP Vicenza and Veneto Banca, the "capital increase story" was not the main focus anymore.

Did the roadshow help you refine the transaction's features? How did you go about positioning the credit?

We started with a 10NC5 structure, allowing greater flexibility and with a target size of Eu750m. Positioning the credit was challenging due to the lack of a UBI Tier 2 curve. Looking at spreads, the main comparables on the market were Intesa Sanpaolo and UniCredit, but our reference point was Intesa rather than UniCredit because we have similar business models.

How did the transaction go? Were you satisfied with the amount, pricing and demand?

It went well. We reached all our targets thanks to the interest we got from investors — a Eu1.5bn book with 180 orders.

How have the new bail-in rules affected your capital funding through the retail channel? Is it a temporary "ban"?

On the senior retail bonds side, customers are rolling roughly 60% of what is maturing — this is also in part due to the low rate environment and to the focus of customers on higher yield investments.

On the Tier 2 side, at the moment our view is to sell our Tier 2 only to institutional investors. We can't rule out for the future that the retail market, with clearer disclosure and awareness, could again be viable for subordinated products, since higher risk products in general, such as equity, are purchased by retail customers.

What is your view on the role played by the Atlante fund? Did it indirectly helped your trade?

Yes, as mentioned, Atlante reduced investors' concerns on capital increases from the two banks in the Veneto region. Without this backstop the market volatility would have been much higher.

What more could be done to fix the NPL issue?

The implemented measures (GACS, Atlante, the speeding-up of repossessions…) are all steps in the right direction. With time these will bear fruit.

What do you expect in terms of final MREL requirements? What is your opinion of the Italian solution regarding eligible liabilities?

We don't have any specific expectations/figures regarding MREL — around 15% for the Total Capital Ratio is our main target. We find the new French non-preferred senior option an interesting solution given the fact that it introduces a further instrument, junior to senior bonds, with a cost lower than Tier 2. ●

Buy-back buoys Eu750m UniCredit Tier 2 return

UniCredit on 26 May sold its first Tier 2 issue since October 2013, a Eu750m 10.5 year non-call 5.5 transaction, after buying back Eu414m equivalent of old-style Tier 1 and Lower Tier 2 euro and sterling bonds. Here, Waleed El-Amir, head of group finance at UniCredit, discusses its return to Tier 2 and wider capital issues.

Why did you come to the market at this time?

There were a number of reasons. Firstly, we had concentrated issuance of Tier 2 on the retail market in the last couple of years to satisfy the significant customer demand we were seeing. It thus felt important to diversify and tap the institutional market, given our long absence and to prove our ability to successfully do deals in that market. Secondly, we had seen a significant rally in our bonds on the back of the buy-back we announced previously. They tightened quite significantly, roughly 65bp, before we came with the Tier 2.

It was a classic liability management exercise. We ran the capital buy-back, buying back bonds from investors that potentially wanted to sell, created new space for new issuance, helped our secondary curve tighten, and then on the back of that, and a pretty positive backdrop, we effectively issued a Eu750m deal that was two times oversubscribed.

We moved very quickly — we closed the buy-back on the Tuesday and issued on the Thursday of the same week.

Was the size of the Tier 2 set from the start?

We said Eu500m-plus. We could have potentially done a Eu1bn deal, as we had a Eu1.5bn book, and if the book had been over Eu2bn we may have considered this. But most of the deals that have come recently, including the recent Deutsche Tier 2, have all been around Eu750m. So we decided we'd rather have a deal that's slightly smaller to try and have it trade well in the secondary market, rather than stretch the book out to allocate Eu1bn.

You mentioned attractive backdrop — are you thinking more of the general market conditions in the capital space, or related to Italian banks and UniCredit?

It's a combination of both. You need the market to be in decent shape, and more importantly you need people to have a positive stance on your credit.

Having a 60bp rally in your credit in the week leading up to issuance is a pretty compelling sign that people are going long your credit — mainly because of the buyback, but also potentially a positive momentum around the credit story.

It was an interesting choice of day, because we decided to come the day of Corpus Christi, with Germany and Austria shut, so part of the investor base was unavailable. The decision we took was that if we didn't come on the Thursday, effectively Friday was going to be very difficult because there was a Monday bank holiday in the UK and the Germans off on the Friday as well as Thursday, with a lot of people taking long weekends — so even fewer people were going to be at their desks. And Friday is never a great day to do a deal. So effec-

Shouldering the burden

While Atlante may have averted disaster on the capital-raising front, its contribution to these exercises was seen as diminishing its firepower for addressing the NPL problem.

"The fund is large enough to support cash calls," said one analyst, "but does not have the scale to tackle the banks' enormous NPL problem."

However, others have argued that it could still leverage the circa Eu1.75bn left after the Popolare di Vicenza and Vento Banca capital increases to support buying of Eu30bn-Eu50bn of gross NPLs. This assumes an equity tranche of the NPL ABSs of 20%-35% (with 65% senior and potentially the balance mezzanine) and the originating banks taking 49% of the equity tranche.

Crucially, it also assumes valuing the NPLs at a price of around 34 cents to the euro. The Milan banker points out that although Italian banks have provisioned NPLs at an average of around 40 cents to the euro, a precedent of 18 cents was set by transactions last year.

"Then question is then, is the correct price 40 cents to the euro or 18 cents to the euro?" he says. "The 18 cents to the euro was a precedent that was set last November using a precedent of last summer, so in a very, very thin market there is one price set for a very, very illiquid and difficult category composed of NPL positions extremely diversified in nature."

"Now, since then there have been quite a few things done that would justify a modification in the price for NPLs."

The Italian government has undertaken a series of legal initiatives aimed at accelerating and simplifying enforcement for NPLs, with further insolvency reforms on the way.

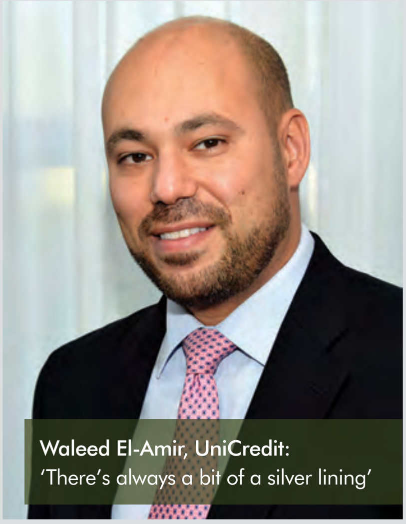
"There has been an unprecedented number of legislative initiatives in 2016 aimed at helping banks to repair their balance sheets, including changes to improve the work-out of impaired loans," commented Fitch. "This shows the authorities are committed to tackling the problems."

This, alongside the GACS scheme could help Atlante engender a virtuous circle for NPL prices, helping both banks that wish to dispose of NPLs and that those that will keep them on their balance sheet.

Although a figure of as much as Eu350bn has been touted for Italy's stock of NPLs, the volume of truly distressed loans is some Eu210bn before taking into account provisions, according to the banker.

"If you value those at 40 cents on the euro, we are talking about some Eu85bn tively that pushed you to Tuesday, but we knew beforehand competing supply was imminent, and Generali did in fact come on Tuesday at roughly the same spread as us, plus another three Tier 2 deals. So the choice was: do you go on Thursday knowing that you don't have the German investor base, or go on Tuesday knowing you probably go head-to-head with a very similar credit with a similar spread and with a lot of supply coming.

I think we made the right choice. We avoided having a head-to-head with Generali, we avoided having to deal with competing supply, and it may have cost us Eu200m or so in orders but the book was well over what we needed to get a nice trade done.



Waleed El-Amir, UniCredit: 'There's always a bit of a silver lining'

with the Tier 2. So there's always a bit of a silver lining.

You mentioned you'd done retail Tier 2 — will that be more difficult going forward?

At the moment, given some of the political noise around this, yes, I think that's going to be more difficult. I think it's important to underline that Consob has not banned the sale of retail Tier 2. But I think given the political climate, it is harder to place Tier 2 in the retail network today, yes.

To what extent did the buyback play into that?

The buy-back kind of fulfilled the desire of certain clients to get out, and actually not a lot of clients sold. We were looking to buy Eu700m, and only around Eu400m was tendered.

You can read that in two ways. You can say, well, that wasn't too great… But it's also actually a pretty positive reflection on the credit. People have seen a sell-off in the credit and asked for a liquidity event, but interestingly when you say, OK, put your money where your mouth is and sell me the paper, they're still saying no – some people are not willing to part with their paper even for a three point premium. So on the basis of that, and the rally we had because of the buyback, and some people actually asking for more paper, we went ahead

Looking at the credit side, there's been these moves with the Atlante fund. Is that a credit positive, and is it playing into people being attracted to Italian credits again?

Yes, I think it's definitely credit positive. It's fulfilling two roles, right: making sure that recaps of banks like Vicenza — and we're waiting to see what the result is going to be on Veneto Banca — effectively have a backstop for their equity capital raisings; and secondly, also as an additional tool to help Italian banks divest of their NPL stock.

There's no magic wand. I think the market's expectation on NPLs is perhaps not realistic. A stock of anywhere between Eu170bn and Eu300bn, depending on how you classify it, is not going to disappear overnight, but Italy is making good progress in addressing this important issue over a reasonable timeframe. ●

and if you consider that you have firepower of Eu30bn to Eu50bn, it's actually not a small number," he says. "You could move the market."

Contagion or confusion?

Such calculations could now prove academic. Whereas pre-Brexit discussions centred on potentially increasing the size of Atlante or on Atlante II, post-Brexit talk has turned to a government-backed fund directly run by Cassa Depositi e Prestiti as being one of the options on the table.

"The key issue here is that in order to provide state aid, and to be compliant with the BRRD, there must be a restructuring plan by the bank involving some kind of bail-in," says Codogno, "probably not in the form of bail-in of depositors — because it is perceived to be systemically dangerous, and we have already seen that in Italy — equity investors will definitely be hit and I think the degree of involvement of bondholders is up for negotiation."

Fitch was quick to highlight the difficulty of finding a satisfactory outcome acceptable to all.

"Measures that would strengthen asset quality or capital without triggering bail-in could be positive for Italian banks' Issuer Default Ratings," it said. "But the impediments under EU legislation to using public funds will make a solution difficult to achieve.

"We believe it will be difficult to reach the political consensus necessary to inject public funds as equity under Article 108 of the Treaty on the Functioning of the EU, which would be exempt from EU state aid rules, at least in the short term," it added.

However, others argue that rather than the folly of Brexit, those involved in Italian banks would be better advised to focus on the British wartime slogan to "keep calm and carry on". The Milan banker points to the successful outcome, just ahead of the UK referendum, of a Eu1bn Banca Popolare capital-raising undertaken to prepare for its merger with Banca Popolare di Milano.

"We don't know what would have happened if Brexit hadn't occurred," he says. "Possibly you would not have had such an issue with the banks. And you really have to wonder what the direct link between Brexit and the banks is.

"So I am a bit confused by the signals the market is sending out. My reading is that Italian bank equity is one of the ways in which you can take a position on the market, being liquid and accentuating overall market trends. But it doesn't seem to me that the banks have lost access to the market." ●

Tier 1 awaited after Solvency II arrival

Although Solvency II is not triggering changes to Fitch's ratings of insurers, it is a credit positive for the European industry, according to Harish Gohil, managing director, EMEA insurance, Fitch Ratings, who discusses the framework's impact and shares his expectations regarding Tier 1 issuance.

How is Solvency II affecting the amount of capital insurers need?

What Solvency II has done is increase capital requirements, through the introduction of the risk-based regime. However, the higher capital requirements do not necessarily lead to an increase in the capital actually held, mainly because most insurers were already holding capital well in excess of the previous Solvency I requirements.

One of the reasons would have been ratings; most of the larger insurers are rated and they tend to be rated in the higher rating categories and to achieve those ratings they always needed to be quite well capitalised.

Another important factor is that insurers have been preparing for Solvency II for several years. Even when the requirements were only just being developed and were uncertain, they were managing capital with that very much in mind, so we would say they were generally somewhat cautious in how they were managing their capital. What they certainly wouldn't have wanted to do was get in a position where Solvency II arrives and suddenly they find that they need to go and raise additional capital.

There are clearly some exceptions. The most publicised is Delta Lloyd, which found itself in a situation where it had to actually go and raise capital externally. Also, smaller and medium-sized insurers may have been less well prepared for Solvency II, so it's more likely that they may need to look to boost capital, by raising additional capital, or by finding other ways of covering or mitigating their capital requirements, such as reinsurance solutions, changing asset strategies, hedging, and so on.

As you mentioned, the larger insurers have been well capitalised and highly rated, but how does Solvency II affect the credit profile, or the inputs into the ratings, and the outlook for them?

From a ratings perspective, Solvency II overall is neutral, in that there haven't been any ratings changes or any expected as a direct result of Solvency II.

On the other hand, overall we would say it's been positive for the credit quality of the insurance sector because it has improved risk management. A big part of Solvency II is around risk management and governance, which as a result has improved across the industry as a whole. The risk-based framework is also a very big step forward from the old Solvency I regime. There are clearly many challenges with Solvency II, in terms of lack of consistency between different countries, even between different companies within a country. But overall it is a big step forward from what we had before, the old Solvency I regime.

On both of those points — improved risk management and the risk-based regime — Fitch believes the larger insurers were already developing those aspects, even before the advent of Solvency II. So, if you went back even as long ago as 10 years, especially the largest insurers across Europe were improving their risk management and governance, partly as a response to the previous crisis that the industry faced in around 2001/2002. That led to many changes in the industry, in terms of improvements in risk management and governance. Most of the larger insurers were also already focusing on some kind of economic capital metrics, and managing themselves to those. So, Solvency II is a further development of that, but it is not fundamentally new, for the largest insurers, anyway.

Would you have any general views on the quality of Solvency II disclosures and how you factor that into your credit analysis?

It's early days in terms of Solvency II disclosure. Obviously Solvency II only came in on 1 January 2016 and there is no mandatory requirement for any public disclosures until 2017, so it will be around spring 2017 when we first see the mandatory disclosures from the insurers.

But of course all the larger insurers and medium-sized insurers have been disclosing their Solvency II ratios, and also providing some sensitivities on those Solvency II ratios in terms of how they might change in response to changes in credit spreads, equity market movements and other drivers. And that's certainly very helpful for understanding the resilience of insurance companies' solvency positions.

But at this stage there isn't that much detail beyond this. For example, it is rare for companies to disclose what benefit they have taken for transitional relief on Solvency II requirements, and that will become more evident next year when we have the public disclosure, which would then make the Solvency II ratios more comparable. Right now, you have to be careful how you compare the reported Solvency II ratios because there are various differences behind those calculations, one of the main differences being around transitional benefits.

How will you go about assessing what ratings the Solvency II Tier 1 instruments should have?

In terms of the ratings criteria that will apply, they will be the same that we have applied for the last few years. Our criteria for rating debt capital instruments has evolved over the years, but we haven't specifically made any changes in response to Solvency II as such. The difference will be in the instruments that are issued under Solvency II. We will apply the principles we have set out in the Fitch criteria to different instruments, instruments that may look quite different from what has been issued in the past, particularly around the Tier 1 instruments.

In terms of rating capital instruments, there are two aspects in our criteria that are key. One is the level of subordination, and what that implies for recovery prospects or loss severity in the event of the insurer being wound up or liquidated or resolved in some way. And the other aspect is what we call non-performance risk, by which we mean the risk of something like a coupon deferral or principal loss-absorption on a going-concern basis. So the first aspect, the level of subordination and recovery prospects, is more an end-game

Harish Gohil, Fitch

scenario, what happens at the end of a company's life. The second aspect, risk of non-performance, is the risk of loss for an investor on the instrument on a going-concern basis, while the company is continuing to operate.

On Solvency II Tier 1 instruments, clearly there have been no such instruments issued yet, so all we have at the moment is the minimum Solvency II requirements. How they get rated in practice will very much depend on the actual detailed terms and conditions of the instruments. With that caveat in mind, I can nevertheless comment on what the likely considerations will be and how we might rate them in practice.

Under our criteria, we have an anchor rating and then notch down from that anchor rating to reflect the different characteristics of different instruments. On subordination, let's say, if you take the example of a purely European insurance group — because how we rate the instruments would be different for a European group with a significant non-EU operation — operating under a Solvency II group solvency regime, we would typically notch down two for the level of subordination. That's because a Tier 1 instrument would be deeply subordinated, so we are notching down two from the anchor rating of the holding company.

On the second part, the risk of non-performance, can you — taking into account your caveat about there not being any issuance yet — give any views?

For Solvency II Tier 1 it would be coupon cancellation we'd be talking about and in relation to that on Tier 1 there would be two types of triggers that would be key features. Firstly, Tier 1 instruments are required to have a mandatory trigger related to meeting the Solvency II Solvency Capital Requirement (SCR). That's actually similar to Tier 2, the trigger itself.

However, on Tier 1 the key feature for us, from a Fitch criteria perspective, is the fully flexible coupon cancellation feature that a Tier 1 instrument would have to have — fully flexible, at management discretion, so that management has the unconditional right to cancel the coupon at any time. For us, that feature is the one that is key to how we would reflect the non-performance risk in our ratings. The key unknown at this stage is around how regulators might put pressure on management to exercise this feature, so whether it is possible that the regulators might be looking to force a coupon cancellation quite early on, before the company has actually got close to its SCR. On this point, we've been talking to regulators and other market participants to form a view. Our current assumption is that the regulators are likely to be less assertive than on the banking side. So, if we draw a comparison with how Fitch has rated bank Additional Tier 1 (AT1) instruments, this feature, the fully flexible coupon cancellation feature, has been seen as the most relevant for assessing non-performance risk, and this risk has been reflected by notching down three just for this particular feature. On the insurance side, our current view is that we are most likely to notch down two for the risk from this feature because we think the insurance regulators are less likely to force a coupon cancellation than on the banking side. It is only when we get actual Tier 1 issuances that our interpretation of this risk will firm up — as the experience develops in the market and it becomes clearer over time exactly

how this fully flexible feature will work in practice.

And on the types of loss absorption — equity conversion or write-down, permanent or temporary — is there anything you can add?

On this particular question about whether we would make a distinction between equity conversion and permanent write-down or temporary write-down, the short answer is no. Under Fitch's criteria the main consideration really is around the likelihood of the trigger being breached, so it's not so much about what happens when the trigger is breached — so we treat each of those features the same — the key consideration is when the trigger comes into play. So say, for example, the loss absorption feature is linked to 100% of SCR, it's that 100% of SCR that is most relevant for us, so that would feed into our assessment of the likelihood of this feature being triggered. But the feature itself — whether it is a temporary write-down, a permanent write-down or equity conversion — that doesn't affect the rating, or at least it's not typically expected to affect the rating.

> There are actually significant differences between the two as well

You've already drawn some comparisons with the banking side. What other differences or similarities could there be between the Solvency II Tier 1 instruments we might see and the bank AT1 structures that have evolved?

There are some similarities, not least in terms of the investor base — we think the kind of investors that may buy Solvency II Tier 1 instruments are likely to be the same investors that are buying into bank AT1, so there is clearly a commonality there, which obviously then begs the question which you asked.

In terms of how we go about rating Solvency II Tier 1 instruments, we would certainty want to be ensuring we are consistent with how we rate the bank AT1 instruments, given some similarities, at a high level at least, around the coupon cancellation and other loss absorption features.

However, we recognise that there are actually significant differences between the two as well. The bank and insurance capital regimes are quite different, and that then affects how the instruments might behave in different circumstances. One simple difference there that I would maybe highlight is that on the bank side there is the concept of the Common Equity Tier 1 ratio as part of the overall bank capital regimes. There isn't really a comparable ratio on the insurance side. You clearly have the Solvency II SCR requirement, but that's it; there isn't the same thing as a CET1 ratio and the buffers that you have to maintain in relation to that. That will then lead to differences in terms of how these Solvency II Tier 1 — Restricted Tier 1, or RT1, as they are being referred to — and the bank AT1 might behave in practice, and we would then reflect that in how we rate the instruments.

To what extent will the use of such instruments complement the existing capital structures of insurers, and help improve the overall financial stability of the sector?

There is certainly a lot of discussion in the market, with arrangers and insurers themselves, about the potential for RT1 as part of insurers' capital structures. So we would certainly say there is potential for RT1 to complement the existing capital structures. It remains to be seen how important they actually will be in practice as part of the insurers' capital structures.

There will be a market; the uncertainty is about how large, how significant the Solvency II RT1 asset class will become. For some insurers it may be a relatively important part, but not necessarily for others. For example, Axa has said very clearly that they don't intend to issue RT1 instruments. They have legacy Tier 1, grandfathered Tier 1 instruments, but they don't expect to issue any new-style RT1 instruments. As their current instruments come up for refinancing, they would issue Tier 2 rather than Tier 1. That's a first very clear example where they don't see a role for Tier 1 in their capital structure.

But, overall, it certainly has a role to play for the industry as a whole. For example, some insurers certainly feel that the right kind of RT1 instrument could be a way to manage and support their Solvency II ratios on the downside in stress scenarios. ●

Regulatory updates

Effective EBA Pillar 2 split offers AT1 relief

The European Banking Authority (EBA) offered relief to the Additional Tier 1 (AT1) market on 1 July when it announced that stress test-related Pillar 2 requirements need not be included in MDA calculations, thereby easing fears of coupon payment restrictions that had plagued the sector.

In an information update on the 2016 EU-wide stress tests — the results of which are due on 29 July — the regulator effectively said that it would split out from Pillar 2 "Capital Guidance" it deems necessary to cover potential shortfalls in own funds based on the outcomes of the stress tests.

The move breaks from the EBA's previous stance of Pillar 2 wholly being included in maximum distributable amount (MDA) calculations — a surprise position announced in December that wrought havoc upon the AT1 market in the first quarter, as market participants had to try to reassess upwards the likelihood of coupons not being distributed.

A relaxation of the moves had been anticipated after pressure from various quarters including the European Parliament, and European Central Bank and EBA representatives had in recent months flagged a likely change. Danièle Nouy *(pictured, right)*, chair of the supervisory board of the SSM at the ECB, for example, said on 8 June that Pillar 2 would be split into binding and non-binding guidance, with only the binding element relevant to MDA.

In its update, the EBA said that the quantitative results of the stress test should be used by Competent Authorities to assess whether a bank will be in a position to meet its Total SREP Capital Requirement (TSCR) under all scenarios (i.e. also the most severe scenarios) and what would be the impact on the Overall Capital Requirement (OCR). In EBA terminology, the TSCR refers to the sum of Pillar 1 and Pillar 2 capital requirements, and the OCR to TSCR plus the applicable Combined Buffer Requirement (CBR — the sum of the Capital Conservation Buffer, systemic buffers, countercyclical buffers, etc).

The EBA then clarified what Competent Authorities may undertake in the event of a breach of the TSCR under the stress test. If there is no danger of imminent TSCR breach, then the Competent Authorities should perform additional analysis as per paragraph 366 of the EBA SREP Guidelines.

Following this analysis the EBA details two specific measures the Competent Authorities could consider:

- Potential restrictions on dividend payments to shareholders; and/or
- The setting of additional Capital Guidance, positioned above the CBR.

According to Doncho Donchev, capital solutions, debt capital markets, Crédit Agricole CIB, of critical importance are the EBA's clarification that (i) the Capital Guidance sits above the CBR and (ii) the Capital Guidance is not included in the calculations of the MDA, i.e. a breach of the Capital Guidance does not lead automatically to distribution restrictions, including the payment of coupons on AT1.

He said that the EBA is effectively introducing into the EU framework a split between Pillar 2 into Pillar 2A and 2B — akin to that used by the UK Prudential Regulation Authority (PRA), where Pillar 2B (equivalent to the Capital Guidance) is dubbed the PRA buffer.

"Provided the ECB/SSM applies the EBA statements in this update, then the Pillar 2 included for SSM banks supervised by the ECB should be reduced and thus the threshold for restrictions which apply to AT1 coupon payments should be lowered by the amount of the stress test-related component currently included in Pillar 2," said Donchev.

He said that this should provide welcome relief to the sector.

"After the surprise SREP decisions which led to the sell-off — the violence of which obviously surprised even the regulators — they have sought to calm the market and make structural improvements," said Donchev. "So, following the informal announcements from Danièle Nouy and Sabine Lautenschläger, now we have the first regulatory announcement in writing, which obviously provides a further brick on the road to regulatory repair."

He noted that if the stress tests reveals the danger of an imminent TSCR breach, Competent Authorities nevertheless have the flexibility to include the Capital Guidance in the Pillar 2 requirement, i.e. Pillar 2B is added to Pillar 2A and repositioned below the CBR.

The results of the stress tests must be factored into the 2016 SREP, applicable from 2017. ●

EU COUNCIL

EU Council publishes conclusions on a roadmap to complete the Banking Union and ECON publishes working document on EDIS: On 17 June, the Council of the European Union published conclusions on the roadmap towards completion of the Banking Union. Among work highlighted was:

- proposing amendments to the legislative framework in view of implementing TLAC and reviewing MREL
- putting forward a proposal on a common approach to the bank creditor hierarchy, to enhance legal certainty in case of resolution
vproposing amendments to the CRR/CRD IV as part of an overall review exercise, which would result in implementing and finalizing remaining Basel reforms including the introduction of a Leverage Ratio, possibly set higher than 3% for systemic banks, and the introduction of a net stable funding ratio
- annually assessing the progress made towards completing the Banking Union

Separately, the European Parliament Committee on Economic & Monetary Affairs (ECON) released a working document on the legislative proposal for a European Deposit Insurance Scheme (EDIS) and the Commission communication "Towards the Completion of the Banking Union". The working paper describes the in general terms the linkages between the EDIS proposal and certain other legislative texts and existing structures.

EUROPEAN COMMISSION

Commission launches consultation on the supplementary supervision of financial conglomerates: On 9 June, the Commission launched a public consultation on the Financial Conglomerates Directive (FICOD) and its implementation to date. The consultation is part of the evaluations the Commission is carrying out under its Regulatory Fitness & Performance Programme (REFIT):

- The purpose of the evaluation is to assess whether the current FICOD regulatory framework is proportionate and fit for purpose, and delivering as expected considering its objective of identifying and managing risks that are inherent to financial conglomerates to ensure financial stability.
- The purpose of the consultation is to gather evidence on the performance of FICOD.
- For the purposes of the consultation, at least the following stakeholders will be targeted: financial conglomerates; financial institutions in general; the Single Supervisory Mechanism; the European Supervisory Authorities; national ministries; non-governmental organisations and others (e.g. think tanks and academics); and the other European institutions

Comments are due by 20 September.

BRRD: Commission adopts Delegated Regulation on MREL: On 23 May, the Commission specified criteria for banks holding "bail-in-able" instruments:

- The draft regulation is intended to enable each individual resolution authority to be responsible for setting the minimum MREL requirements for the purpose of loss absorption and recapitalisation on a case-by-case basis. It will also enable the resolution authority to exercise discretion on the composition of MREL as appropriate for each bank. The bank-specific nature recognises the diversity of business models and funding strategies among European banks.
- The draft regulation is subject to a three month objection period by the EU Council and Parliament.
- As per Article 45 of the BRRD, an MREL review is mandated to be carried out by end-2016, which is also expected to include a proposal to introduce international TLAC into EU law before 2019.

CRD IV: Commission on "bail in" derivatives: On 23 May, the Commission adopted the regulation on valuation of liabilities arising from derivatives:

- BRRD provides that resolution authorities may bail-in relevant derivatives liabilities provided that the authority complies with certain conditions, including exercising bail-in power only after closing out the derivatives and ensuring that derivatives subject to netting agreements are bailed in on a net basis following the terms of their netting agreement.
- Before resolution the resolution authority is required to carry out independent valuation of its assets and liabilities.
- The draft regulation specifies the following parameters when assessing valuation of derivative liabilities:
    i. Methodologies to determine the appropriate value of classes of derivatives
    ii. Addressing guidance/rules to establish the relevant point in time at which a value of a derivative position should be established

These updates are split into bank and insurance, and listed according to the relevant body, topic or country, with the most recent first therein.

Michael Benyaya,
Julian Burkhard, Badis Chibani,
Veronique Diet-Offner,
Doncho Donchev, Jimmy Liu,
Pinal Patel, Samuel Susman
DCM Solutions
Crédit Agricole CIB
Capital.Structuring@ca-cib.com

iii. Methodologies that would compare value destruction that would arise from closing out positions and bail-in of derivatives with the amount of losses that are borne by derivatives in bail-in

CRD IV: Commission on G-SIIs: On 18 May, the Commission adopted the amended Delegated Regulation on methodology for identifying G-SIIs:

- The amendment to Commission Delegated Regulation (1222/2014/EU) aims to ensure consistency in the methodology between regulations and the Basel framework.
- The Basel Committee on Banking Supervision (BCBS) published a revised reporting template for the 2016 data collection exercise, based on 2015 year-end data.

Draft RTS to the BRRD article 52(12): On 10 May, the Commission released a draft Regulatory Technical Standards (RTS) related to article 52(12) – business reorganisation plans:

- The draft RTS further specify (a) the minimum elements that should be included in a business reorganisation plan and (b) the minimum contents of the reports in relation to the business reorganisation plan described in Articles 51 and 52 of Directive (EU) No 2014/59.
- The business plan should:
  I. Address the causes of the institution's failure
  II. Clearly set out how the firm will be restored to long term viability
- Restoring long term viability of the institution should include:
  i. Ability to meet its Internal Capital Adequacy Assessment Process (ICAAP) requirements, according to relevant provisions of Directive 2013/36/EU (CRD IV)
  ii. Fulfil all the relevant prudential and regulatory requirements, such as liquidity, regulatory

Ecofin chair Jeroen Dijsselbloem

capital and MREL (article 45 of BRRD)
  iii. Have a viable business model that is considered sustainable in the long term and does not threaten the capacity to meet requirements (i) and (ii) above
- Viability analysis should include significant, albeit plausible, set of worse case assumptions relating to the context in which the firms will operate.

Commission consults on EU insolvency framework: On 23 March, The Commission launched a consultation on ensuring an effective insolvency framework in the EU, which builds on previous work and consultations, most recently the Capital Markets Union (CMU) action plan.

- This consultation seeks stakeholders' views on key insolvency aspects. In particular, it seeks views with regard to common principles and standards that could ensure that national insolvency frameworks work well, especially in a cross-border context.
- The responses will be used to identify which aspects may possibly be dealt with-in the legislative initiative and which in other possible complementary actions in this field.

The consultation ended on 12 June 2016.

ECOFIN

EU to consider sovereign exposure limits, risk-weights: On 22 April, EU finance ministers met at the ECOFIN committee to discuss risk weightings of sovereign exposures. A leak published by the *Financial Times* described five different options to change the treatment banks have to apply to their holdings of sovereign debt:

1. The baseline option: i.e. keeping everything the same
2. Further enhancements to Pillar 2 and/or 3: i.e. more extensive supervision and better disclosure may be required
3. Enhancements to Pillar 1 addressing credit risk: i.e. creating a non-zero risk weight (e.g. introducing a sovereign risk-weight floor)
4. Enhancements to Pillar 1 addressing concentration risk: i.e. limiting exposure to an individual sovereign, encouraging pan-European diversification
5. Addressing both credit and concentration risk ("hybrid option"): i.e. a mix of changing risk-weight and exposure limits

ECB

ECB releases public guidance on the qualification of AT1 and Tier 2: On 6 June, the ECB set out public guidance of the review of the AT1 and Tier 2 capital instrument compliance procedure:

- Under Article 4(1)(d) of Council Regulation (EU) No 1024/2013 (SSM regulation) the ECB is required to ensure all firms are adhering to the requirements set out, in particular Article 52 and 63 of the CRR, for AT1 and T2.

● The guidance lays down the procedure followed by the ECB in reviewing qualification for AT1 and T2 instruments.
● Entities are responsible for ensuring that their capital instruments are fully compliant with all the relevant provisions of the CRR and RTS of Own Funds.
● The CEO or a person duly authorised by the management body to sign on its behalf should send in a signed letter with an attachment in an email to the coordinator of the relevant Joint Supervisory Team. The letter should cover:
  o reasons of issuance and how it fits in with the three year capital planning exercise,
  o provide a description of the main features, per the prescribed forma,
  o include a self-assessment of the instruments vs. the requirements in the CRR,
  o confirm the validity of the information and,
  o provide supporting documentation as specified in the guidance note.
● The ECB at any time may carry out an ex post assessment of AT1 and T2.

ECB launches second public consultation on harmonising options and discretions available in EU law: On 18 May, the ECB consulted on a draft addendum to guide on options and discretions available in EU law:

● The ECB provided a draft addendum to the exercise of some of its options and discretions provided for in CRD IV and the CRR available under Union law (published 24 Mar 2016).
● The addendum addresses eight options and discretions applicable on a case by case basis, applicable to credit institutions classified as "significant".

The closing date of the consultation was 21 June.

ECB issues guidance on recognition of significant credit risk transfer: On 24 March, the ECB wrote to the management of significant banks to provide guidance on the recognition of significant credit risk transfer.

● Articles 243 and 244 of the Regulation on the Single Supervisory Mechanism (SSM) set out the conditions under which a significant risk transfer (SRT) by an originator institution is recognized.
● The ECB's guidance lays down the procedure to be followed by significant supervised entities as defined under the SSM Framework Regulation when acting as originator institutions with regard to the recognition of SRT.
● The ECB recommends that entities follow the guidance with respect to all securitisation transactions issued after its publication.

EBA

EBA consults on LCR: On 11 May, the European Banking Authority launched a consultation on its draft Guidelines on Liquidity Coverage Ratio (LCR) disclosure:

● LCR is intended to ensure financial institutions are to maintain an adequate level of liquidity buffer to cover net liquidity outflows under stressed conditions over a 30 day period. The EBA has now published the disclosure of liquidity risk management under article 435 of reg (EU) no 575/2013 CRR
● As credit institutions are only in the scope of the LCR Delegated act, the scope of application of the draft guidelines is limited to them
● The draft guidelines include:
  o a qualitative and quantitative harmonised table for the disclosure of mainly information on liquidity risk management as laid down by the CRR; and
  o quantitative and qualitative harmonised templates, with their corresponding instructions, for the disclosure of information on the LCR composition.
● The application of these guidelines is not expected to take place before 30 June 2017.

The deadline for comments to the EBA is 11 August.

List of banks identified as systemically important in the EU: On 25 April, the EBA published the first list of Other Systemically Important Institutions (O-SII) in the EU.

● The institutions have been identified by relevant authorities across the EU according to harmonised criteria provided by the EBA.

- The EBA Guidelines provide additional flexibility for relevant authorities to apply their supervisory judgment, when deciding to include other institutions that might have not been automatically identified as O-SIIs.
- The identification of institutions as O-SIIs in the EU is based on 2015 data and will be updated on an annual basis.

EBA public hearing on Leverage Ratio: On 15 April, the EBA held in London a public hearing on the Leverage Ratio. CACIB Capital Solutions team attended the conference:

- The results of the quantitative analyses performed by the EBA suggest that a 3% level of calibration for the Leverage Ratio is generally consistent with the objective of a "backstop" measure that supplements risk-based capital requirements. In particular, a (Tier 1 capital-based) Leverage Ratio calibrated at a level of 3% would constitute a higher capital requirement than a risk-based Tier 1 capital requirement of 8.5% for around 33% of the analysed credit institutions.
- The results of a simulations-based analysis suggest the potential impact of introducing a Leverage Ratio requirement of 3% on the provision of financing by credit institutions would be relatively moderate when put into the context of the overall size of the banking sector.
- The quantitative benchmarking results give indications for a potentially elevated exposure to risk of excessive leverage in the case of the largest and most complex credit institutions, in particular for those that operate the business model of a "cross-border universal bank" and are at the same time G-SIBs.
- The empirical results indicate that the Leverage Ratio is somewhat more sensitive to the economic cycle than a risk-based capital requirement, and potentially countercyclical.
- Developments in Basel (6 April 2016 Consultative Document) are being monitored.
- The EBA does not want the Leverage Ratio to be constraining and wants a balance between risk-weighted measures and the Leverage Ratio.
- Leverage Ratio work is to be finalized by the end of 2016.

EBA publishes report and recommends supervisory best practices on securitisation risk retention, due diligence and disclosure: On 12 April, the EBA published a report analysing measures taken by Competent Authorities in 2014 to ensure compliance by institutions with securitisation risk retention, due diligence and disclosure requirements.

- The report highlights that institutions are generally undertaking appropriate actions to comply with such requirements. In total, 10 cases of non-compliance with risk retention and due diligence have been reported. Sanctions in the form of additional risk-weights as per Article 407 of the CRR were applied in one out of the 10 cases.
- According to the EBA analysis, it also appears that ensuring compliance with risk retention, due diligence and disclosure requirements has a lower priority in the supervisory processes of Competent Authorities.
- The report also assesses how the EBA recommendations enhancing regulation of risk retention, due diligence and disclosure rules, as specified in the EBA Opinion of December 2014, have been taken on board in the proposals of the new securitisation framework issued by the Commission in September 2015.

EBA consults on draft amending standards on CVA proxy spread: On 6 April, the EBA launched a public consultation on draft amending RTS on credit valuation adjustment (CVA) proxy spread. These RTS propose limited amendments to the Commission's Delegated Regulation (EU) No 526/2014 based on two policy recommendations contained in the EBA's CVA report published on 25 February 2015. Through the proposed amendments the EBA expects to ensure a more adequate calculation of own funds requirements for CVA risk. The consultation runs until 6 July.

ESMA

ESMA publishes statement on selling bail-in securities: On 2 June, the European Securities & Markets Authority (ESMA) with the EBA published a statement on firms' responsibilities when selling bail-in debt.

- The statement sets out concerns that investors may be unaware of the risk associated with buying instruments that can be bailed in and reminds firms that they must comply with their obligations under MiFID and issues relating to:
  - o Providing investors with up-to-date complete information
  - o Managing potential conflict of interest; and
  - o Ensuring that products are suitable and appropriate for the investor.

BASEL COMMITTEE

Basel Committee sets bank standards to manage interest rate risk: On 21 April, the Basel Committee on Banking Supervision issued new standards for Interest Rate Risk in the Banking Book (IRRBB). The standards revise the Basel Committee's 2004 Principles for the management and supervision of interest rate risk, which set out supervisory expectations for banks' identification, measurement, monitoring and control of IRRBB as well as its supervision.

The key updates to the 2004 Principles include:

Insurance

IAIS releases updated G-SII assessment Methodology: On 16 June, the International Association of Insurance Supervisors (IAIS) updated its methodology for identifying and assessing G-SIIs. Revisions to the initial assessment methodology, which was first published in 2013, were informed by three previous designation exercises and public comments received on two IAIS consultation papers issued in November 2015.

- The updates to the methodology include the use of absolute reference values for derivatives trading, financial guarantees and reinsurance indicators.
- The paper also sets out the reasoning behind the IAIS's discontinuation of the "non-traditional, non-insurance" (NTNI) product label.

FSB releases guidance on resolution planning for systemically important insurers: Financial Stability Board (FSB) Guidance released on 6 June sets out considerations for determining a preferred resolution strategy and identifies a range of elements that need to be in place so that a resolution strategy can be credibly and feasibly implemented. The Guidance has been revised in light of the comments received during the consultation. Below a summary of the comments received and reflected by the FSB in the final Guidance:

- Resolution strategies should be developed with the aim of protecting policyholders as well as maintaining financial stability.
- Differences between the insurance and the banking sector have been acknowledged in the final Guidance. In terms of resolution tools, some respondents noted that an approach based on the bail-in of liabilities would not be appropriate given the structure of insurers' balance sheets. There is a clear preference for portfolio transfer and run-off tools. The "loss absorbing capacity" terminology has also been avoided in the final Guidance.
- Regarding the point of entry into resolution, the final Guidance retains both the OpCo and the HoldCo level or a combination of both. Several respondents suggested that, in insurance groups, entry into resolution will generally be at the OpCo level because each entity is locally supervised and because resolution measures are generally taken under local resolution regimes, and where relevant, local policyholder protection schemes are triggered.

EIOPA launches the EU-wide Insurance Stress Test 2016: On 24 May, the European Insurance & Occupational Pensions Authority (EIOPA) launched an EU-wide stress test for the European insurance sector. The exercise was launched a week before initially anticipated. The Stress Test 2016 focuses on two major market risks:

- The prolonged low yield environment.
  - o Due to the low-for-long nature of the scenario, the extrapolated part of the curve, defined according to the Solvency II methodology, is projected utilising a reduced ultimate forward rate (UFR) defined according to the assumption of the scenario.
- The so-called "double-hit", i.e. a negative market shock to asset prices combined with a low risk-free rate.

The exercise focuses on long term business performed by solo undertakings (no insurance groups). In order to include a higher number of small and medium size insurers, the participation target was increased from a 50% in 2014 to a 75% share of each national market in terms of gross life technical provisions. The results will be published in December in an anonymised and/or aggregated way.

EIOPA consults on methodology to derive UFR: On 20 April, EIOPA released a consultation paper seeking feedback on the methodology to derive the ultimate forward rate. According to EIOPA, the proposed UFR methodology strives for a balance between the stability of the UFR and the need to adjust the UFR in case of change in long term expectations about interest rates and inflation. In the current context, a decrease of the UFR from the current level of 4.2% looks unavoidable. This is a major topic for insurance companies as the Solvency II disclosures have shown a significant sensitivity of the Solvency margin to a lower level of the UFR.

EIOPA proposes amendments to the current approach, for example in terms of the time-span for the real rate component or the determination of the inflation rate component. Based on the revised methodology, the UFR would be 3.7% in 2016 for 19 currencies including euros. EIOPA proposes various phase-in alternatives, bearing in mind that the revised methodology includes a limitation of annual changes to 20bp.

The consultation period will end on 18 July and EIOPA plans to decide on the outcome of the review in September. The currently used UFRs will not be changed until at least the end of 2016. ■

- More extensive guidance on the expectations for a bank's IRRBB management process in areas such as the development of shock and stress scenarios as well as key behavioural and modelling assumptions to be considered by banks in their measurement of IRRBB.
- Enhanced disclosure requirements to promote greater consistency, transparency and comparability in the measurement and management of IRRBB. This includes quantitative disclosure requirements based on common interest rate shock scenarios.
- An updated standardised framework, which supervisors could mandate their banks to follow or banks could choose to adopt.
- A stricter threshold for identifying outlier banks that has been reduced from 20% of a bank's total capital to 15% of a bank's Tier 1 capital. In addition, interest rate risk exposure is measured by the maximum change in the economic value of equity under the prescribed interest rate shock scenarios.

Standardisation of bad loan definition: On 14 April, the Basel Committee launched a consultation on proposed definitions of non-performing exposures and forbearance. After the tentative proposal of the EBA to have relatively standardised data during the stress tests, the Basel Committee plans to harmonise the definition of bad loans into two broad categories.

- Loans at least 90 days past due will be categorised as non-performing.
- Other loans on which forbearance has been granted, whereby the loan's terms have been modified, will be classified in the other category.

Comments on the proposals are due by 15 July.

The Basel Committee's willingness to harmonise better across European member countries is positive, although such an exercise may lead to higher costs for banks (collateral, internal models).

Revisions to Basel III Leverage Ratio framework: On 6 April, the Basel Committee released a consultative document entitled Revisions to the Basel III Leverage Ratio framework that sets out the Committee's proposed revisions to the design and calibration of the Basel III Leverage Ratio framework. Among the areas subject to proposed revision in this consultative document are:

- measurement of derivative exposures;
- treatment of regular-way purchases and sales of financial assets;
- treatment of provisions;
- credit conversion factors for off-balance sheet items; and
- additional requirements for global systemically important banks (G-SIBs).

Comments on the proposal are due by 6 July.

Second report on risk-weighted assets in banking book: On 1 April, the Basel Committee published a second report on risk weighted assets (RWAs) in the banking book. The study examines the variability of RWA in banks that use internal models to calculate their credit risk regulatory capital requirements:

- The study finds a reasonable relationship between estimates of probabilities of default and actual default rates.
- A weaker relationship is observed between loss outcomes and other parameters estimated by credit risk models (such as loss-given-default). At an individual bank level, there is much greater variation between parameters estimated using credit risk models and actual outcomes.
- The report also evaluates the variability in estimates of exposure at default for all asset classes. These reveals wide variation in bank practices that can contribute materially to overall RWA variability.

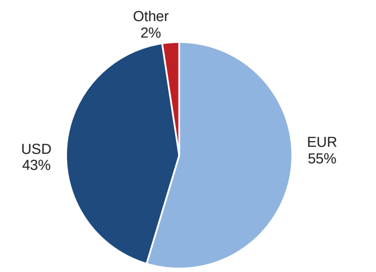
Basel Committee proposes measures to reduce the variation in credit risk-weighted assets: On 24 March, the Basel Committee released a consultative document on reducing the variation in credit risk-weighted assets. The Basel Committee's key proposals are:

- To remove the internal ratings-based (IRB) model option for bank and large corporate exposures (more than Eu50bn in assets), which will be subject to the standardised approach instead. Also the removal of internal model option for Credit Valuation Adjustment (CVA) risk and a floor for counterparty risk models.
- To adopt exposure-level, model-parameter floors:
    - Minimum probability of default (PD) increases from 3bp to 5bp.
    - Loss given default (LGD) is set to 25% for unsecured corporate exposure and 0%-20% for secured exposures.
    - Minimum exposure at default (EAD) includes 50% weight for off-balance sheet exposures using the applicable credit conservation factor (CCF) in the standardised approach.
- To constrain the parameter estimation in banks internal models:
    - PD estimate should include 10% weight on downturn years and a constraint on banks' LGD.
- To replace the Basel I floor, the Basel Committee is considering a new floor in the range of 60%-90% of the standardised approach
- The proposals will be subject to an extensive Quantitative Impact Study

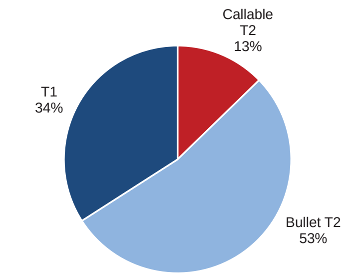
The consultation ended on 24 June and the Basel Committee aims to finalise the rules by end-2016. ■

Currencies, structures and distribution

Bank hybrid issuance by currency (2016 ytd)

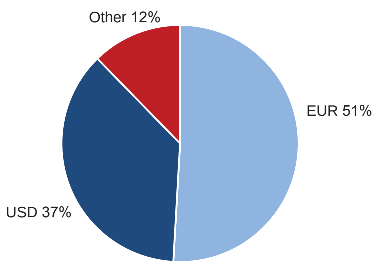


Bank issuance by instrument/structure (2016 ytd)

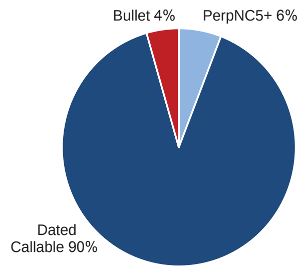


Source: Crédit Agricole CIB

Insurance hybrid issuance by currency (2016 ytd)

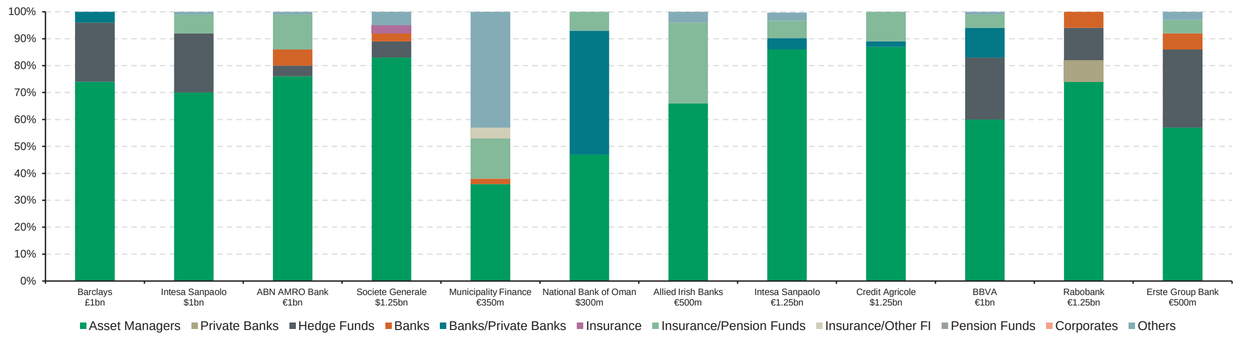


Insurance issuance by instrument/structure (2016 ytd)

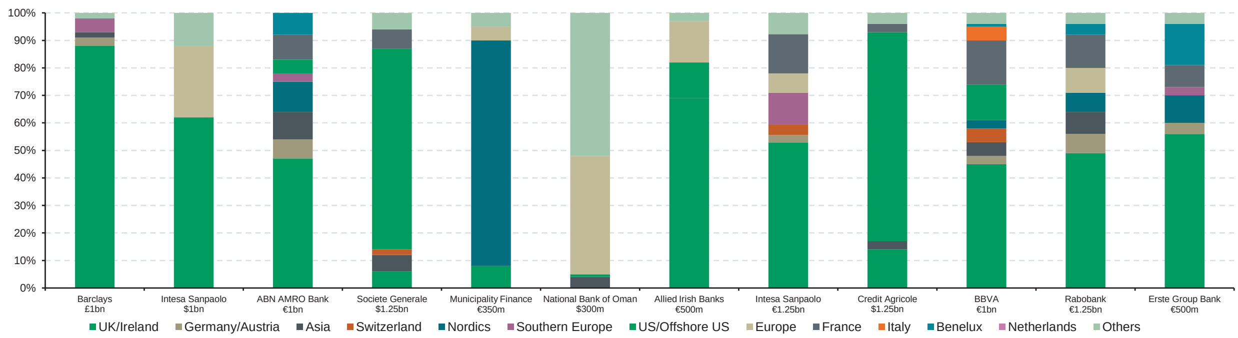


Source: Crédit Agricole CIB

AT1 distribution by investor type



AT1 distribution by geography



Source: Crédit Agricole CIB

AT1, Tier 2 CoCos

AT1 performance monitoring (as at 28/6/16)

Launch	Issuer	Issue ratings	Currency	Amount (m)	Coupon	Maturity date	First call date	Principal loss absorption	Trigger	Price	I-Spread	Yield to call
25-May-16	ERSTBK	Ba3u/BB/-	EUR	500	8.875%	Perpetual	15-Oct-21	TWD	5.125%	94.17	1,066	10.33
28-Apr-16	BKTSM	Ba3/-/-	EUR	200	8.625%	Perpetual	10-May-21	CE	5.125%	100.76	879	8.43
19-Apr-16	RABOBK	Baa3/-/BBB-	EUR	1,250	6.625%	Perpetual	29-Jun-21	TWD	7%/5.125%	97.86	735	7.14
07-Apr-16	BBVASM	Ba2/-/BB	EUR	1,000	8.875%	Perpetual	14-Apr-21	CE	5.125%	94.55	1,084	10.33
12-Jan-16	ISPIM	Ba3/B+/BB-	EUR	1,250	7.000%	Perpetual	19-Jan-21	TWD	5.125%	89.78	1,019	9.84
26-Nov-15	AIB	B3u/-/B	EUR	500	7.375%	Perpetual	03-Dec-20	TWD	7.000%	84.54	1,245	11.97
22-Sep-15	HSBC	Baa3/-/BBB	EUR	1,000	6.000%	Perpetual	29-Sep-23	CE	7.000%	93.35	719	7.19
15-Sep-15	ABNANV	Ba1u/BB/BB+	EUR	1,000	5.750%	Perpetual	22-Sep-20	TWD	5.125%	90.70	872	8.40
11-Jun-15	BKIR	B2/B+/-	EUR	750	7.375%	Perpetual	18-Jun-20	TWD	5.125%	90.37	1,082	10.40
10-Jun-15	BNP	Ba1/BBB-/BBB-	EUR	750	6.125%	Perpetual	17-Jun-22	TWD	5.125%	93.27	769	7.55
27-Apr-15	IPMID	-/-/-	EUR	125	8.625%	Perpetual	01-Apr-21	CE	7.000%	78.28	1,546	15.36
19-Feb-15	NYKRE	-/BB+/BB+	EUR	500	6.250%	Perpetual	26-Oct-20	TWD	7.125%	97.50	718	6.93
13-Feb-15	UBS	-/BB+/BB+	EUR	1,000	5.750%	Perpetual	19-Feb-22	PWD	5.125%	99.13	596	5.93
11-Feb-15	DANBNK	Ba1u/BB+/BB+	EUR	750	5.875%	Perpetual	06-Apr-22	TWD	7.000%	96.50	674	6.61
10-Feb-15	BBVASM	Ba2/-/BB	EUR	1,500	6.750%	Perpetual	18-Feb-20	CE	5.125%	82.30	1,374	12.93
05-Feb-15	POPSM	Caa1u/-/B-	EUR	750	8.250%	Perpetual	10-Apr-20	CE	7.000%	80.73	1,606	15.03
15-Jan-15	RABOBK	Baa3/-/BBB-	EUR	1,500	5.500%	Perpetual	29-Jun-20	TWD	7%/5.125%	92.50	802	7.72
04-Aug-15	BACR	Ba2/B+/BB+	GBP	1,000	7.875%	Perpetual	15-Sep-22	CE	7.000%	87.83	1,000	10.57
03-Jun-15	SANUK	Ba2/B+/BB+	GBP	750	7.375%	Perpetual	24-Jun-22	PWD	7.000%	90.75	883	9.41
07-Jun-16	ANZ	Baa1/BBB-/BBB	USD	1,000	6.750%	Perpetual	15-Jun-26	CE	5.125%	101.75	517	6.51
24-May-16	HSBC	Baa3/-/BBB	USD	2,000	6.875%	Perpetual	01-Jun-21	CE	5.125%	98.00	639	7.37
23-Mar-16	BNP	Ba1/BBB-/BBB-	USD	1,500	7.625%	Perpetual	30-Mar-21	TWD	5.125%	98.00	718	8.14
14-Mar-16	UBS	Ba1u/BB+/BB+	USD	1,500	6.875%	Perpetual	22-Mar-21	PWD	7.000%	95.50	693	8.04
12-Jan-16	ACAFP	Ba2u/BB/BB+	USD	1,250	8.125%	Perpetual	23-Dec-25	TWD	7.000%	98.00	721	8.43
22-Sep-15	SOCGEN	Ba2/BB+/-	USD	1,250	8.000%	Perpetual	29-Sep-25	TWD	5.125%	93.50	775	9.05
10-Sep-15	ISPIM	Ba3/B+/BB-	USD	1,000	7.700%	Perpetual	17-Sep-25	PWD	5.125%	85.00	896	10.25
12-Aug-15	BNP	Ba1/BBB-/BBB-	USD	1,500	7.375%	Perpetual	19-Aug-25	TWD	5.125%	95.50	679	8.08
05-Aug-15	RBS	B1u/B/BB-	USD	2,000	7.500%	Perpetual	10-Aug-20	CE	7.000%	87.50	1,061	11.35
05-Aug-15	RBS	B1u/B/BB-	USD	1,150	8.000%	Perpetual	10-Aug-25	CE	7.000%	89.50	858	9.75
31-Jul-15	UBS	-/BB+/BB+	USD	1,575	6.875%	Perpetual	07-Aug-25	PWD	7.000%	90.75	691	8.36
09-Apr-15	INTNED	Ba1/BB/BBB-	USD	1,000	6.000%	Perpetual	16-Apr-20	CE	7.000%	91.50	780	8.67
09-Apr-15	INTNED	Ba1/BB/BBB-	USD	1,250	6.500%	Perpetual	16-Apr-25	CE	7.000%	90.00	684	8.11
26-Mar-15	STANLN	Ba1/BB-/BBB-	USD	2,000	6.500%	Perpetual	02-Apr-20	CE	7.000%	88.00	957	10.44
23-Mar-15	HSBC	Baa3/-/BBB	USD	2,450	6.375%	Perpetual	30-Mar-25	CE	7.000%	92.75	625	7.52
19-Mar-15	DNBNO	Baa3u/BBB/-	USD	750	5.750%	Perpetual	26-Mar-20	TWD	5.125%	93.29	686	7.88
05-Mar-15	NDASS	Ba1u/BBB/BBB	USD	550	5.250%	Perpetual	13-Sep-21	TWD	8%/5.125%	95.25	525	6.34
18-Feb-15	SHBASS	Baa2/BBB/BBB+	USD	1,200	5.250%	Perpetual	01-Mar-21	TWD	5.125%	93.75	579	6.85
13-Feb-15	UBS	-/BB+/BB+	USD	1,250	7.000%	Perpetual	19-Feb-25	PWD	5.125%	101.13	545	6.82
13-Feb-15	UBS	-/BB+/BB+	USD	1,250	7.125%	Perpetual	19-Feb-20	PWD	7.000%	98.75	651	7.51
12-Feb-15	SWEDA	Baa3u/BBB/BBB	USD	750	5.500%	Perpetual	17-Mar-20	CE	8%/5.125%	98.50	509	5.95
18-Nov-14	DB	B1/B+/BB	USD	1,500	7.500%	Perpetual	30-Apr-25	TWD	5.125%	80.50	950	11.06

T2 CoCo performance monitoring (as at 28/6/16)

Launch	Issuer	Issue ratings	Currency	Amount (m)	Coupon	Maturity date	First call date	Principal loss absorption	Trigger	Price	I-Spread	Yield to call
08-Jun-15	ZKB	-/A/-	EUR	500	2.625%	15-Jun-27	15-Jun-22	PWD	5.000%	97.14	316	3.16
23-May-14	NYKRE	-/BBB/BBB	EUR	600	4.000%	03-Jun-36	03-Jun-21	PWD	7.000%	96.66	486	4.77
06-Feb-14	UBS	-/BBB+/BBB+	EUR	2,000	4.750%	12-Feb-26	12-Feb-21	PWD	5.000%	-	399	3.88
11-Sep-13	CS	-/BBB/BBB	EUR	1,250	5.750%	18-Sep-25	18-Sep-20	PWD	5.000%	-	466	4.53
22-Jan-16	RY	Baa1/A-/AA-	USD	1,500	4.650%	27-Jan-26	-	CE	5.000%	106.31	254	-
08-May-14	UBS	-/BBB+/BBB+	USD	2,500	5.125%	15-May-24	-	PWD	5.000%	101.00	370	-
12-Sep-13	ACAFP	-/BBB-/BBB-	USD	1,000	8.125%	19-Sep-33	19-Sep-18	PWD	7.000%	106.00	447	5.22
01-Aug-13	CS	-/BBB/BBB	USD	2,500	6.500%	08-Aug-23	-	PWD	5.000%	104.36	460	-
15-May-13	UBS	-/BBB+/BBB+	USD	1,500	4.750%	22-May-23	22-May-18	PWD	5.000%	101.25	328	4.05
03-Apr-13	BACR	-/BB+/BBB-	USD	1,000	7.750%	10-Apr-23	10-Apr-18	PWD	7.000%	101.00	642	7.13
17-Jan-13	KBC	-/BBB-/-	USD	1,000	8.000%	25-Jan-23	25-Jan-18	PWD	7.000%	107.38	245	3.14

Principal loss absorption: CE = conversion into equity; TWD = temporary write-down; PWD = permanent write-down

Source: Crédit Agricole CIB

Latest bank Tier 2, insurance hybrids

Latest Tier 2 performance monitoring (as at 28/6/16)									
Launch	Issuer	Issue ratings	Currency	Amount (m)	Coupon	Maturity date	First call date	I-Spread	Yield to call
06-Jun-16	SOCGEN	Baa3/BBB/A-	USD	500	5.100%	27-Jun-36	-	361	-
31-May-16	FRLBP	-/BBB-/-	EUR	500	3.000%	09-Jun-28	-	264	-
31-May-16	HSBC	A2/BBB+/A+	EUR	1,000	3.125%	07-Jun-28	-	285	-
26-May-16	UCGIM	Ba1/BB/BBB	EUR	750	4.375%	03-Jan-27	03-Jan-22	535	5.31
25-May-16	CMARK	-/BBB/-	EUR	500	3.250%	01-Jun-26	-	288	-
24-May-16	BNP	Baa2/BBB+/A	AUD	475	5.000%	31-May-28	31-May-23	285	4.99
12-May-16	DB	Ba2/BB+/BBB+	EUR	750	4.500%	19-May-26	-	485	-
11-May-16	SOCGEN	Baa3/BBB/A-	SGD	425	4.300%	19-May-26	19-May-21	277	4.47
05-May-16	BNP	Baa2/BBB+/A	USD	1,250	4.375%	12-May-26	-	276	-
05-May-16	BACR	Baa3/BB+/A-	USD	1,250	5.200%	12-May-26	-	341	-
28-Apr-16	CCBGBB	-/BBB-/-	EUR	500	3.125%	11-May-26	-	289	-
28-Apr-16	SABSM	B1/B+/-	EUR	500	5.625%	06-May-26	-	562	-
27-Apr-16	UBIIM	Ba2/BB/BBB-	EUR	750	4.250%	05-May-26	05-May-21	537	5.27
13-Apr-16	BPCEGP	Baa3/BBB/A-	EUR	750	2.875%	22-Apr-26	-	267	-
06-Apr-16	INTNED	Baa2/BBB/A	EUR	1,000	3.000%	11-Apr-28	11-Apr-23	301	3.09
29-Mar-16	BPCEGP	Baa3/BBB/A-	USD	750	4.875%	01-Apr-26	-	326	-
17-Mar-16	BFCM	A3/BBB/A	EUR	1,000	2.375%	24-Mar-26	-	232	-
17-Mar-16	LLOYDS	Baa2/BBB-/A-	USD	1,500	4.650%	24-Mar-26	-	323	-
16-Mar-16	ABNANV	Baa2/BBB-/A-	USD	300	5.600%	08-Apr-31	-	357	-
16-Mar-16	CMZB	Ba1/BBB-/BBB	EUR	1,000	4.000%	23-Mar-26	-	368	-
15-Mar-16	SANTAN	Baa2/BBB/BBB+	EUR	1,500	3.250%	04-Apr-26	-	371	-
04-Mar-16	BNP	Baa2/BBB+/A	EUR	750	2.875%	01-Oct-26	-	261	-
11-Jan-16	ABNANV	Baa2/BBB-/A-	EUR	1,000	2.875%	18-Jan-28	18-Jan-23	273	2.78
08-Jan-16	ISPIM	Ba1/BB/BBB	USD	1,500	5.710%	15-Jan-26	-	534	-
20-Nov-15	BPCEGP	Baa3/BBB/A-	EUR	750	2.750%	30-Nov-27	30-Nov-22	274	2.79
19-Nov-15	BNP	Baa2/BBB+/A	EUR	750	2.750%	27-Jan-26	-	259	-
19-Nov-15	AIB	B1/B+/BB	EUR	750	4.125%	26-Nov-25	26-Nov-20	662	6.49
17-Nov-15	SOCGEN	Baa3/BBB/A-	USD	500	5.625%	24-Nov-45	-	352	-
17-Nov-15	SOCGEN	Baa3/BBB/A-	USD	1,000	4.750%	24-Nov-25	-	326	-
12-Nov-15	SANTAN	Baa2/BBB/BBB+	USD	1,500	5.179%	19-Nov-25	-	410	-
10-Nov-15	NYKRE	-/BBB/A-	EUR	800	2.750%	17-Nov-27	17-Nov-22	318	3.22
10-Nov-15	FRLBP	-/BBB-/-	EUR	750	2.750%	19-Nov-27	19-Nov-22	269	2.73
04-Nov-15	BACR	Baa3/BB+/A-	EUR	1,250	2.625%	11-Nov-25	11-Nov-20	471	4.59
02-Nov-15	NDASS	Baa1/A-/A+	EUR	750	1.875%	10-Nov-25	10-Nov-20	195	1.82
29-Oct-15	SNSBNK	Ba1/BB+/BBB	EUR	500	3.750%	05-Nov-25	05-Nov-20	472	4.59
20-Oct-15	BPCEGP	Baa3/BBB/A-	AUD	175	5.400%	27-Oct-25	27-Oct-20	312	5.11

Insurance performance monitoring (as at 28/6/16)									
Launch	Issuer	Issue ratings	Currency	Amount (m)	Coupon	Maturity date	First call date	New issue spread	I-Spread
31-May-16	Prudential Plc	A3/A-/BBB+	USD	1,000	5.250%	Perpetual	20/07/2021	-	366.75
31-May-16	Assicurazioni Generali	Baa3/-/BBB	EUR	850	5.000%	08/06/2048	08/06/2028	-	448.86
25-May-16	Demeter (Swiss RE Ltd)	-/BBB+/-	USD	800	5.625%	15/08/2052	15/08/2027	-	390.84
24-May-16	Scor SE	-/A/A-	EUR	500	3.625%	27/05/2048	27/05/2028	290	316.51
17-May-16	Demeter (Zurich Ins)	A2/A/-	EUR	750	3.500%	01/10/2046	01/10/2026	295	300.35
27-Apr-16	Aviva Plc	Baa1/BBB/BBB+	CAD	450	4.500%	10/05/2021	-	-	250.64
23-Mar-16	AXA SA	A3/BBB/BBB	EUR	1,500	3.375%	06/07/2047	06/07/2027	275	289.11
18-Mar-16	Cloverie Plc Zurich Ins	A2/A/A-	USD	1,000	5.625%	24/06/2046	24/06/2026	392	355.57
02-Mar-16	Swiss Life AG	-/BBB+/-	CHF	450	3.750%	Perpetual	24/09/2021	439	301.42
02-Mar-16	Swiss Life AG	-/BBB+/-	CHF	150	4.375%	24/09/2046	24/09/2026	454	351.15
15-Jan-16	CNP Assurances	-/BBB+/-	USD	500	6.000%	22/01/2049	22/01/2029	-	409.91
02-Dec-15	Scor SE	-/-/A-	EUR	600	3.000%	08/06/2046	08/06/2026	225	310.97
01-Dec-15	CNP Assurances	-/BBB+/-	EUR	750	4.500%	10/06/2047	10/06/2027	360	484.17
05-Nov-15	Swiss Re	-/BBB+/-	USD	700	5.750%	15/08/2050	15/08/2025	-	424.08
04-Nov-15	Rothesay Life	Baa1/BBB+/-	GBP	350	6.125%	13/11/2028	-	-	482.26
29-Oct-15	Old Mutual Plc	Ba1/-/BB+	GBP	450	7.875%	03/11/2025	-	-	553.04
22-Oct-15	Rothesay Life Ltd	-/-/-	GBP	250	8.000%	30/10/2025	-	-	554.00
20-Oct-15	Gothaer Versicherung	-/BBB/-	EUR	250	6.000%	30/10/2045	30/10/2025	504	499.44
20-Oct-15	Assicurazioni Generali	Baa3/-/BBB	EUR	1,250	5.500%	27/10/2047	27/10/2027	435	371.85
19-Oct-15	Legal & General	Baa1/-/-	GBP	600	5.375%	27/10/2045	27/10/2025	-	347.74
24-Sep-15	Humanis	-/-/-	EUR	250	5.750%	22/10/2025	-	-	481.88

Source: Crédit Agricole CIB

Disclaimer

This material has been prepared by Crédit Agricole Corporate and Investment Bank or one of its affiliates (collectively "Crédit Agricole CIB"). It does not constitute "investment research" as defined by the Financial Conduct Authority and is provided for information purposes only. It is not to be construed as a solicitation or an offer to buy or sell any financial instruments and has no regard to the specific investment objectives, financial situation or particular needs of any recipient. Crédit Agricole CIB does not act as an advisor to any recipient of this material, nor owe any recipient any fiduciary duty and nothing in this material should be construed as financial, legal, tax, accounting or other advice. Recipients should make their own independent appraisal of this material and obtain independent professional advice from legal, tax, accounting or other appropriate professional advisers before embarking on any course of action. The information in this material is based on publicly available information and although it has been compiled or obtained from sources believed to be reliable, such information has not been independently verified and no guarantee, representation or warranty, express or implied, is made as to its accuracy, completeness or correctness. This material may contain information from third parties. Crédit Agricole CIB has not independently verified the accuracy of such third-party information and shall not be responsible or liable, directly or indirectly, for any damage or loss caused or alleged to be caused by or in connection with the use of or reliance on this information. Information in this material is subject to change without notice. Crédit Agricole CIB is under no obligation to update information previously provided to recipients. Crédit Agricole CIB is also under no obligation to continue to provide recipients with the information contained in this material and may at any time in its sole discretion stop providing such information. Investments in financial instruments carry significant risk, including the possible loss of the principal amount invested. This material may contain assumptions or include projections, forecasts, yields or returns, scenario analyses and proposed or expected portfolio compositions. Actual events or conditions may not be consistent with, and may differ materially from, those assumed. Past performance is not a guarantee or indication of future results. The price, value of or income from any of the financial products or services mentioned herein can fall as well as rise and investors may make losses. Any prices provided herein (other than those that are identified as being historical) are indicative only and do not represent firm quotes as to either price or size. Financial instruments denominated in a foreign currency are subject to exchange rate fluctuations, which may have an adverse effect on the price or value of an investment in such products. None of the material, nor its content, nor any copy of it, may be altered in any way, transmitted to, copied or distributed to any other party without the prior express written permission of Crédit Agricole CIB. No liability is accepted by Crédit Agricole CIB for any damages, losses or costs (whether direct, indirect or consequential) that may arise from any use of, or reliance upon, this material. This material is not directed at, or intended for distribution to or use by, any person or entity domiciled or resident in any jurisdiction where such distribution, publication, availability or use would be contrary to applicable laws or regulations of such jurisdictions. Recipients of this material should inform themselves about and observe any applicable legal or regulatory requirements in relation to the distribution or possession of this document to or in that jurisdiction. In this respect, Crédit Agricole CIB does not accept any liability to any person in relation to the distribution or possession of this document to or in any jurisdiction.

United States of America: The delivery of this material to any person in the United States shall not be deemed a recommendation to effect any transactions in any security mentioned herein or an endorsement of any opinion expressed herein. Recipients of this material in the United States wishing to effect a transaction in any security mentioned herein should do so by contacting Crédit Agricole Securities (USA), Inc. United Kingdom: Crédit Agricole Corporate and Investment Bank is authorised by the Autorité de Contrôle Prudentiel et de Résolution (ACPR) and supervised by the ACPR and the Autorité des Marchés Financiers (AMF) in France and subject to limited regulation by the Financial Conduct Authority and the Prudential Regulation Authority. Details about the extent of our regulation by the Financial Conduct Authority and the Prudential Regulation Authority are available from us on request. Crédit Agricole Corporate and Investment Bank is incorporated in France and registered in England & Wales. Registered number: FC008194. Registered office: Broadwalk House, 5 Appold Street, London, EC2A 2DA.