Bank+InsuranceHybridCapital Briefing

Downside risks return to the fore after resurgent primary phase for FIG issuance

The first euro benchmark AT1 deals of the year have successfully hit the market amid a string of FIG trades, as issuers have sought to take advantage of a recovery in sentiment to get ahead in funding plans. But with spreads having now largely recovered and downside risks imposing themselves, the tone may turn tougher. *Neil Day* reports, with insights from Crédit Agricole CIB syndicate and strategists.

Financial institutions enjoyed resurgent primary markets coming into April, as markets rebounded from wides and investors put cash back to work, but last week there were signs of sentiment turning, as spreads neared early-year tights, and risk factors could regain the upper hand.

After a tentative restart of FIG supply on 14 March — when Crédit Agricole and UBS sold the first senior preferred and HoldCo issues, but in maturities limited to three years — the recovery gradually gathered momentum to the extent that on 23 March Intesa Sanpaolo was able to print the first euro benchmark Additional Tier 1 (AT1) of the year.

The Italian national champion priced its €1bn perpetual non-call 6.5 issue, rated Ba3/BB- (Moody's/Fitch), at 6.375%, following initial price thoughts of the 6.625% area on the back of some €3bn of demand, with the final reset spread of 556bp over mid-swaps representing a new issue premium of around 25bp.

The market has since proved accommodating to AT1 from diverse credits, namely Deutsche Bank, Rabobank and Banco BPM.

Deutsche Bank issued its €750m perp non-call seven AT1, rated Ba3/BB-/BB, on 28 March at 569bp over mid-swaps and 6.75%, following IPTs of the 7.125% area and on the back of an order book of some €5.7bn — the German, like Intesa, paying a NIP of around 25bp. Rabobank sold its €1bn perp non-call 7.7 AT1, rated Baa3/BBB (Moody's/Fitch) on 30 March, paying 4.875%, equivalent to 372bp over, mid-swaps following IPTs of the 5.375% area and with a book of over €6bn helping the Dutch bank limit its NIP to around 12.5bp.

Jerome Powell and Lael Brainard. Photo: Federal Reserve

And Banco BPM on Tuesday issued a sole-led €300m perp non-call five AT1, rated B3/B (Moody's/DBRS), at 7% and 604bp over mid-swaps, following guidance of the 7.25%-7.375% area and on the back of €1.15bn of orders.

"The market demonstrated great resilience and capacity to digest more potential bad news from Ukraine," said Vincent Hoarau, head of FI syndicate at Crédit Agricole CIB (CACIB), "and has been getting used to the concerning inflation figures and their impact on the pace of rate hikes in the US and Europe.

"Globally, the market was less volatile — investors were ready to deploy the solid cash balances they were sitting on and issuers understood that there is a lot of upside in de-risking funding plans before spread potentially widen again and rates go higher."

The senior non-preferred/HoldCo segment had demonstrated its capacity early on in this phase, with JP Morgan Chase raising €2.5bn in an eight year non-call seven HoldCo deal on 16 March, tightening from IPTs of the 130bp area to 110bp on the back of some €8bn of orders, in a trade that by early last week had tightened to 78bp.

But the recent strength of the market was perhaps best exemplified when BNP Paribas on 31 March approached the market with a 10 year senior non-preferred offering: the long-dated issue attracted some €4bn of demand that allowed it to tighten pricing from IPTs of the 125bp area to 90bp, and come slightly inside fair value. Toronto-Dominion Bank the same day raised €1.5bn of eight year bail-in debt at 80bp over mid-swaps, 20bp inside IPTs and at a NIP of 11bp, after attracting some €2.5bn of orders.

"On a spread basis, we have retraced almost all the losses that occurred from mid-February," said Hoarau, "but on an absolute basis the yields on offer are much higher than where we were back then, having skyrocketed over the last month."

The five year swap rate, for example, moved from 0.32% on 1 March to 1% on 1 April.

It has been a similar story in the US market, where spreads and new issue premiums have come down from early March highs.

"Just after the war started and with the Fed having just hiked, the markets were more chaotic and deals were coming to market with 20bp-25bp new issue concession for both Yankee banks and US institutions," said Daniel Kim, director, US syndicate, CACIB, "as investors demanded an incremental adjustment to reflect the underlying rates volatility — if you look at the two year Treasury, it's gone from 140bp at the beginning of March to 250bp.

"But as time has progressed, that new issue concession has been averaging 10bp-15bp — much closer to what we saw prior to 17 February and the war — so from that perspective, we have somewhat normalised."

As in Europe, risk appetite also increased.

"There's been an incremental move to duration and higher beta names," added Kim. "There has been a longing for yieldy securities, much of that driven by overseas investors, and we've been witnessing outsized demand for 10 year and lower-rated securities."

On 22 March, for example, HSBC Holdings sold a $2bn (€1.84bn) 4.762% 11 non-call 10 Tier 2, expected ratings Baa1/BBB/A-, at Treasuries plus 240bp, 35bp inside IPTs and with a new issue premium of just 5bp-7bp on the back of more than $8bn of demand. And last Tuesday, as part of a $3.35bn three-tranche trade, Bank of Nova Scotia issued a $1.25bn 4.588% 15 non-call 10 subordinated bond, expected ratings Baa1/BBB+/A (Low) (Moody's/S&P/DBRS), at Treasuries plus 205bp, 20bp inside IPTs and with a new issue premium in the teens, despite coming in the wake of heavy supply from the jurisdiction.

However, signs are emerging that a turning point is being reached on both sides of the Atlantic, as monetary policy tightening returns to the front page.

On Tuesday, Federal Reserve Board Governor Lael Brainard emphasised the "paramount importance" of getting inflation down, and FOMC minutes released on Wednesday suggested the pace of the Fed's quantitative easing will be at the faster end of expectations. A 50bp hike is meanwhile considered a near certainty at the 3-4 May meeting, and 25bp or 50bp in June the next of many expected this year.

"This past week, we've seen the momentum ease and more of a balance between supply and demand," said Kim. "The market is realising that the accelerated balance sheet reduction is going to hit the back end of the curve, whereas the shorter end is a little bit more anchored now.

"I wouldn't say that 10 year demand has been completely eradicated, but we're getting more demand at the front of the curve — when investors are getting spreads of 75bp to 100bp on a two or three year note, they're now getting a 3.50% yield, which is pretty good."

The governing council of the European Central Bank will hold its latest meeting on Thursday and could provide more guidance on when its Asset Purchase Programme will end, as a prelude to a first rate hike. Louis Harreau, head

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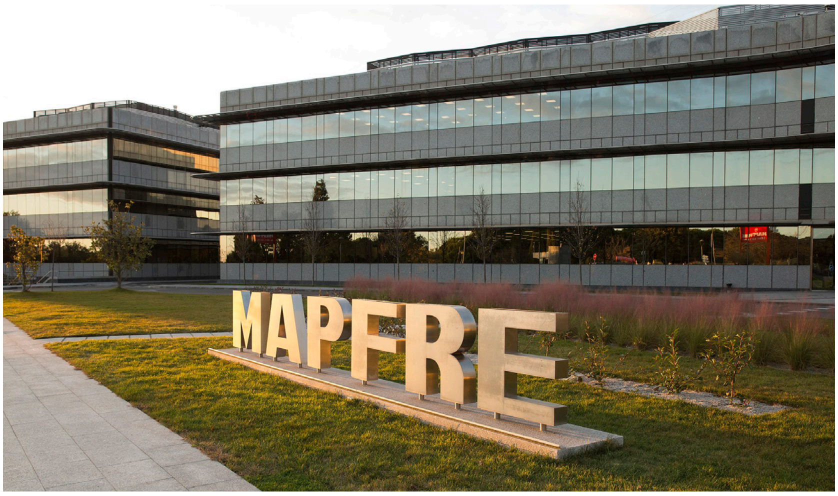
Selected recent euro bank issuance

Issue date	Issuer	Format	Size (m)	Coupon	Maturity	Re-offer spread	IPTs/ guidance	NIP	Books	Cover
14 Mar	Crédit Agricole SA	SP/OpCo	1250	1.000%	Sep-25	45	60/65	7.5	1800	1.4x
14 Mar	UBS Group	SNP/HoldCo	1500	1.000%	03/25NC03/24	80	100a	20	4200	2.8x
15 Mar	BFCM	SP/OpCo	1500	1.000%	May-25	50	70a	7.5	2300	1.5x
16 Mar	Banco Sabadell	SNP/HoldCo	750	2.625%	03/26NC03/25	220	250a	25	4200	5.6x
16 Mar	JP Morgan Chase	SNP/HoldCo	2500	1.963%	03/30NC03/29	110	130a	22	8000	3.2x
17 Mar	Credit Suisse	SNP/HoldCo	2000	2.125%	10/26NC10/25	160	185a	25	4100	2.1x
17 Mar	Credit Suisse	SNP/HoldCo	1500	2.875%	04/32NC04/31	195	220/225	30	6000	4.0x
17 Mar	Deutsche Bank AG	Tier 2	1500	4.000%	06/32NC03/27	330	360a	25	6500	4.3x
21 Mar	Nykredit	SP/OpCo	500	1.375%	Jul-27	65	85a	9	675	1.4x
22 Mar	KBC Group NV	SNP/HoldCo	750	1.500%	03/26NC03/25	90	110a	10	1900	2.5x
23 Mar	Intesa Sanpaolo	AT1	1000	6.375%	PNC09/28	6.375%/556	6.625%a	25	3000	3.0x
25 Mar	BNP Paribas	Tier 2	1500	2.500%	03/32NC03/27	160	185/190	10	5000	3.3x
28 Mar	AIB Group plc	SNP/HoldCo	1000	2.250%	04/28NC04/27	130	155a	10	1850	1.9x
28 Mar	Deutsche Bank AG	AT1	750	6.750%	PNC04/29	6.75%/569	7.125%a	25	5700	7.6x
29 Mar	Erste Group	SP/OpCo	500	1.500%	Apr-26	55	75/80	7	2100	4.2x
30 Mar	Rabobank	AT1	1000	4.875%	PNC12/29	4.878%/372	5.375%a	12.5	6000	6.0x
31 Mar	BNP Paribas	SNP/HoldCo	1500	2.100%	Apr-32	90	125a	-2.5	4000	2.7x
31 Mar	Bank of Ireland	SNP/HoldCo	1000	1.875%	06/26NC06/25	110	130a	12.5	2000	2.0x
31 Mar	Toronto-Dominion	SNP/HoldCo	1500	1.952%	Apr-30	80	100a	11	2500	1.7x
04 Apr	Mizuho Financial	SNP/HoldCo	750	1.631%	Apr-27	65	90a	7	1300	1.7x
04 Apr	Mizuho Financial	SNP/HoldCo	750	2.096%	Apr-32	92	115/120	12.5	1600	2.1x
05 Apr	Banco BPM SpA	AT1	300	7.000%	PNC04/27	7%/604	7.25/7.375%	18.75	1150	3.8x
05 Apr	CaixaBank	SNP/HoldCo	1000	1.625%	04/26NC04/25	80	100/105	10	1450	1.5x
06 Apr	Zürcher Kantonalbank	Tier 2	500	2.020%	04/28NC04/27	90	110a	-	1600	3.2x

Source: Crédit Agricole CIB

Mapfre Tier 3 debut achieves minimal NIP



Mapfre paid a negligible new issue premium when issuing the first subordinated insurance trade in euros since Russia's invasion of Ukraine on Wednesday, a €500m eight year deal that drew close to €1.7bn of orders despite being launched into a weakening market.

Spain's largest insurer, Mapfre announced its Tier 3 — the first from the country — on Tuesday, and engaged with 85 accounts ahead of its first deal since August 2018, when it sold a €500m 30 non-call 10 Tier 2. The inaugural Tier 3 makes use of some €1.3bn of capacity for Tier 2/Tier 3 issuance, of which €600m is for Tier 3.

Following initial price thoughts of the mid-swaps plus 200bp area for the €500m no-grow eight year Tier 3, expected rating BBB- from Fitch, a first update put books above €1bn, and the leads then moved straight to launch at a spread of 175bp on the back of books above €1.6bn. The deal then tightened around 5bp in the aftermarket.

"This issuance serves as yet another illustration of the confidence institutional investors have in Mapfre," said CFO Fernando Mata. "We continue optimising our debt position, and we are doing so in very satisfactory financial conditions, even within a complex market context such as the current one."

André Bonnal, FIG syndicate at joint bookrunner Crédit Agricole CIB, said that although the market deteriorated on the days the deal was announced and launched — with rates backing up around 10bp on Tuesday, for example, and spreads widening — the issuer and syndicate took comfort from strong feedback and indications of interest received from investors during premarketing.

"After all, it's a name that is very rare in the markets," he added, "and their trades are usually successful given this scarcity element. It's also an issuer that gives you exposure to Spain and some interesting EM exposure, and has super-solid solvency ratios (SCR coverage of 206.3% FY 2021).

> It's a name that is very rare in the markets

"It is also shorter in duration than the typical insurance Tier 2, had eye-catching IPTs of 200bp combined with a final yield of 3%, and the small size of €500m helped."

The softer market nevertheless affected pricing discussions, with comparables comprising French Tier 3 issues widening around 5bp between announcement and launch, also reflecting French presidential election opinion polls showing stronger support for far right candidate Marine Le Pen.

Taking into account the relative levels of French insurers' Tier 2 and Tier 3 spreads, and Mapfre's relative credit strength, the leads put fair value pre-announcement at around 165bp, and ultimately 170bp-175bp, also taking into account investor feedback.

"I don't think any other subordinated issuance could easily get done so close to fair value in this market," said Bonnal, "especially when bank HoldCo or senior non-preferred need to pay 10bp-plus of new issue premium."

He noted that the Tier 3 offering also enabled Mapfre to achieve a saving of some 50bp versus the fair value of a callable Tier 2 with same duration — its 2048 non-call 2026 issued in 2018 was quoted at 221bp over. The Tier 3 also allowed Mafpre to offer investors a shorter-dated transaction than typical Tier 2 structures.

The new issue has an expected rating of BBB- from Fitch, which — unlike S&P, who also rates Mapfre — gives the Tier 3 equity credit. The Tier 3 ranks pari passu with Mapfre's Tier 2. ●

of developed markets macro and strategy at CACIB, expects this to be a 25bp move in December, while the market has been pricing in an outside chance of a 25bp move in September, with 7.5% headline inflation numbers buoying hawks.

According to Hoarau at CACIB, the past week in the euro primary market showed signs of fundamentals reasserting themselves against the liquidity that had been driving the market tighter, as spreads plateaued and investors demonstrated greater diligence on pricing.

"The bounce in risk appetite looks overdone," he said. "The street is certainly now less inclined to load risk and more inclined to go short, so we are potentially entering a phase of higher volatility in the second quarter.

"Earnings season is starting soon and there is scope for major disappointment in growth expectations — we have already seen the Treasury curve inverting, signalling greater risk of recession. There is still great uncertainty as to how long the war will last and, overall, fundamentals are not rosy at all." ●

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