FIG party continues as yield-chasing technicals win out

A dramatic rally in Italian government bonds, 10-year Bunds breaching the ECB depo rate and more rate-cut talk over poor inflation expectations capped an eventful week in capital markets. High-beta credits remain very much in vogue.

News that the European Commission is holding off an Excessive Deficit Procedure against Italy in light of the government’s fiscal adjustments that will push the headline deficit back into SGP compliance had Italian government bonds off to the races this past week.

Ten-year BTPs tightened by a dramatic 47bp in the belly of the week and spreads are down over 100bp over the past month. Two-year Italian government bonds entered negative yield territory. There was a little profit-taking reported from leveraged and other accounts into week’s end. But rather than the rally having run out of steam, the feeling seems to be that the market is just taking a breather and that there is more tightening out there.

Some participants are expecting new lows on Italy-Germany and Greece-Germany spreads, even as 10-year Bunds continue plumbing new lows, breaching the -40bp ECB depo rate in the week.

Capital markets, ever quick to sense an opportunity, duly delivered a well-timed senior preferred offering from Monte dei Paschi di Siena and a subordinated Tier 2 from UBI Banca. MPS got a EUR 500m three-year senior preferred away at a yield of 4%, equivalent to a spread of MS+439bp, pulling in demand of over EUR 1.1bn. Yield IPTs had been 4.25%-4.375% for what started out as a minimum EUR 300m issue.

UBI Banca, meanwhile, sold a no-grow EUR 300m 10NC5 Tier 2 offering at a spread of MS+475bp. Solid demand enabled leads to pull pricing in from MS+485bp guidance and IPTs of an optically very generous 510bp. The coupon is fixed to the call, resetting then to five-year mid-swaps plus the initial margin.

If the timing of the Italian issues was particularly opportunistic this past week, the fact remains that as more and more of the government and corporate bond market trades at negative yields, investors are ever more desperate for yield. Any notion that it’s a buyer’s market out there seem long gone as sellers take their chances to print at bargain-basement prices. Issuers are going with the flow, pushing out along the maturity curve not just to lock in favourable rates but as a means to offer investors a positive yield experience. The fact that UBI’s book was 4.7x covered and pricing tightened 35bp from IPTs tells its own story.

Secondary markets have also been good in recent weeks; performance is never linear, but June saw solid tightening across FIG segments as the market pushes inexorably towards those early 2018 spread lows.

It’s not just high beta risk names that are in demand. Case in point: Commerzbank had the market pretty excited with its much-anticipated debut AT1, which went into marketing on 2 July and priced on the following day. The USD 1bn 5.125%-trigger non-cumulative fixed-to-reset trade pulled in around USD 11bn of demand, enabling leads to fix the yield at 7%, the tight end of 7.125% +/- 0.125% WPIR guidance and nicely though IPTs of 7.50%-7.75%.

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As successful as the trade clearly was, the hoopla was not all about Commerbank as a credit. While the bank has gone a long way to de-risking its balance sheet, it still needs to prove that its strategy can generate a decent return now that its dalliance with Deutsche Bank is over.

Demand was driven perhaps even more by general yield-chasing behaviour, by the lack of German AT1s (Deutsche Bank not expected at this point to bring capital issuance this year), the lack of European AT1 supply in dollars, a general paucity of European bank AT1 supply now that a lot of banks have gone some ways to filling their 2019 requirements, and poor secondary liquidity making it difficult to source paper in size. In the round, a 7% handle was too good to pass up, particularly as sell-side analysts had fair value below that level.

Issuing conditions in the capital markets generally are so good that banks with big funding programmes are front-loading and coming back in quick succession multiple times to take money from an open market. Market participants have clearly put macroeconomic and geopolitical issues – which have not by any means gone away – to the side. June was a blockbuster month for primary issuance, including in FIG. Activity continued into the first week of July, with a mixture of returning national champions and some high beta names.

In the past couple of months, around 70 Western European banking groups have tapped the primary bond market. That number excludes groups that have multiple issuing entities (such as Santander, UniCredit and the UK banks). Those that didn't emerge during May and June either did so earlier in the year or in the second half of last year.

Bearing in mind most Western European banks underneath the large national champions have limited funding needs so won't tap the market much anyway, or will fund away from the public capital markets, the entire realistically-addressable universe of Western European O-SII/G-SIIs – and more – has now accessed the bond market in recent weeks up and down the capital and funding spectrum. With chatter about poor inflation expectations having the ECB preparing an imminent rate cut, spread product should remain at the top of buying lists.

In acquisition financing news, Swiss consumer finance company Cembra Money Bank completed a trio of transactions to finance its acquisition of cashgate AG, a fellow consumer finance and auto finance provider. On 4 July, Cembra sold a CHF150m AT1 with a 2.5% coupon. This followed a CHF 112.8m placement of treasury shares (equivalent to 4% of its share capital) and a CHF 250m seven-year senior unsecured zero-coupon callable convertible private placement on 2 July. The 30% conversion premium was struck at the top of the range; and the 100.88 issue price came near the bottom of the price range. The overall yield-to-maturity of the CB was a negative 0.125%.

Summary of key FIG debt issuance June 28 through July 5 (to 12:30 CET)

AXA Home Loan SFH priced its debut EUR 1bn eight-year OFH covered bonds backed by French collateral at MS+7bp, a small single-digit NIP, with books reaching EUR 1.5bn. Leads had initially gone out with guidance of MS+10bp area. The borrower had been on a pan-European roadshow.

Arkea Home Loans pushed out MS+11bp area IPTs on 5 July for a no-grow EUR 500m 10-year mortgage covered bond, and tightening to guidance of MS+6bp, by which time demand had exceeded EUR 2bn.

Banco Santander may have been cautious to get its EUR1.5bn 10-year covered bond away on 3 July. Going for size over spread is a reasonable stance and MS+15bp was still a reasonably tight print, the bottom of MS+16bp +/-1bp WPIR guidance. Demand, nevertheless, hit EUR 3.7bn, enabling leads to pull pricing in from MS+20bp area IPTs. Some chatter intimated the leads could have gone tighter in light of the small NIP and the strong market.

Bankia returned quickly after its EUR 500m five-year SNP, extending its curve with a EUR 750m seven-year senior non-preferred that priced on 2 July at MS+88bp, a reported small single-digit NIP; books closing above EUR 2bn at the final spread (EUR 2.25bn at the highs). Guidance had been MS+90bp-95bp and IPTs MS+110bp area.

Bank of Ireland set the spread of its EUR 600m 5NC4 holdco senior unsecured offering at MS+115bp, having retained demand at print of around EUR 2.7bn. At their height, books had reached over EUR 3.5bn. The depth of demand enabled leads to move in from IPTs of MS+145bp area and guidance of MS+125bp area.

Banque Federative du Credit Mutuel's EUR 1bn five-year senior preferred offering priced at a spread of MS+43bp, a low single-digit basis point concession, and the tight end of MS+45bp area +/-2bp guidance. Books closed at over EUR 1.5bn. IPTs had been MS+high 50s.

La Banque Postale priced EUR 750m of seven-year senior preferred notes at MS+43bp, pulling in orders of over EUR 2bn. Pricing came at the tight end of MS+45bp +/-2bp WPIR guidance. IPTs had been MS+60bp area. The 43bp seven-year spread was identical to that paid by BFCM's five-year outing. In late June, French regulators approved La Poste's takeover of CNP Assurances. Caisse des Dépôts et Consignations and the government will transfer their stake in CNP to La Banque Postale.

BNP Paribas tapped the Kangaroo market for its latest AT1 foray, an AUD 300m (roughly EUR 187m) PNC5.5, with the yield set at 4.50%. Heady demand of over AUD 2.4bn at close – much higher at the highs – enabled leads to pull the yield in from 5.25%-area guidance.

Canadian Imperial Bank of Commerce went out on July 3 with a EUR 1bn eight-year covered bond backed by prime Canadian residential mortgages, extending its curve by some four years. Initial guidance of MS+13bp area was revised to MS+10bp +/-1bp WPIR and pricing came at the tight end as demand went above EUR 1.9bn enabling the issue to price at or arguably through fair value.

Commerzbank generated USD 11bn of demand for its USD 1bn 5.125%-trigger non-cumulative fixed-to-reset rate AT1. The yield was fixed at 7%, the tight end of 7.125% +/- 0.125% WPIR guidance; IPTs had been 7.50%-7.75%. Management had met with over 140 investors on the roadshow.

Deutsche Hypothekenbank priced a no-grow EUR 250m tap of its six-year EUR 750m covered bond issued on 14 June. Guidance emerged at MS+1bp area and the spread was fixed at MS flat, equivalent to a yield of -0.157%, perhaps accounting for so-so demand of EUR 280m, even though it offered a mid-single-digit concession.

Fineco Bank, the Italian retail broker and investment advisor in which UniCredit has a large minority stake, goes on the road on 8 July ahead of a potential EUR 200m PNC5 5.125%-trigger temporary write-down AT1.

Lloyds Bank Corporate Markets, the group's non-ring-fenced entity, went on the road on 1 July following publication of its EMTN programme and into the market on 4 July to price a debut GBP 500m offering of five-year senior unsecured notes at 132bp over Gilts. The book was covered 2x. Guidance had been MS+135bp area and IPTs +145bp area. LBCM is expected to be a regular issue of opco senior debt.

NIBC Bank priced EUR 500m of five-year senior preferred notes at MS+110bp; books closing around EUR 1.8bn, having hit a high of EUR 2.2bn. Guidance had been MS+120bp area and IPTs, MS+140bp area.

Societe Generale SFH went on the road on 3 July throughout Europe to present its Positive Impact Covered Bond Framework and ahead of a debut euro-denominated intermediate to long-maturity soft-bullet positive-impact OFH to refinance eligible green mortgage loans.

Toronto-Dominion Bank sold AUD 1.25bn in five-year senior unsecured bail-in-able notes split into an AUD 550m fixed-rate tranche (priced at ASW+100bp, -5bp to launch spread) and an AUD 700m FRN (BBSW+100bp).

Bank of Bahrain and Kuwait followed its Middle East, Asia and London roadshows with a USD 500m five-year senior unsecured priced at MS+375bp on 2 July (IPTs MS+high300s), with books climbing to over USD 2bn.

Kuwait's **Burgan Bank** priced a USD 500m PNC5 AT1 at a 5.75% yield as books hit USD 2.2bn. Demand enabled leads to tighten low 6% IPTs to 5.875%-6.00% guidance. Kuwait's second largest conventional bank by assets had roadshowed in Asia, the Middle East and the UK. Concurrently with the new AT1, the bank launched a tender for its existing USD 500m capital securities offering.

(Source for basic bond data: Bond Radar (www.bondradar.com).

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