



# **Bank Capital Equity vs Hybrid Instruments**

## **ABI Conference 2014**

Prepared by: HSBC

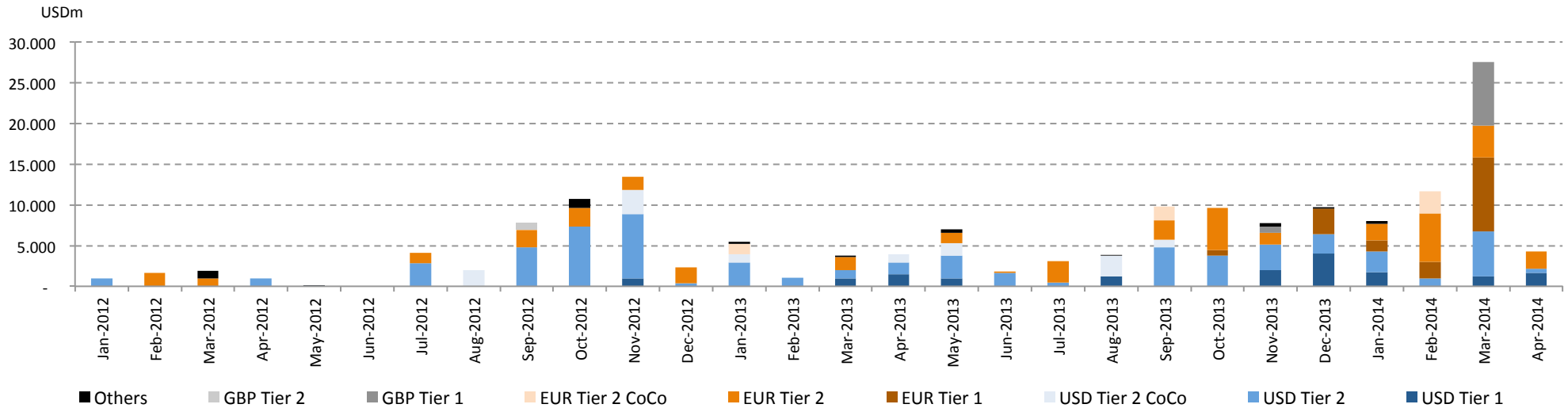
Date: May 2014



# EMEA Bank Capital Supply

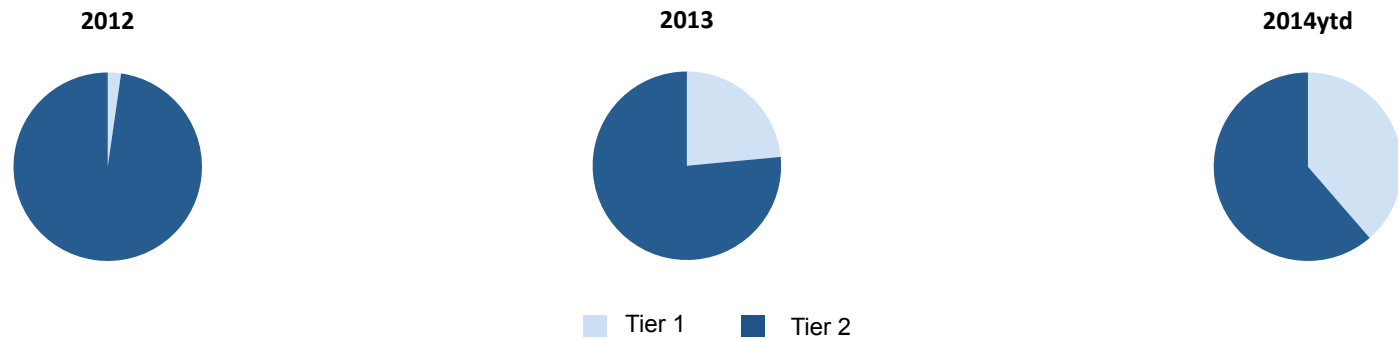
## Heightened Level of Activity

### Tier 1 vs. Tier 2 Issuance Volumes



Source: Dealogic, 01 May 2014, March Volumes include Lloyds AT1s issued in ECN exchange - USD6.9bn equiv. in March 2014 and USD1.675bn in Apr 2014

### Tier 1 vs. Tier 2 Issuance Volumes



Source: Dealogic, 01 May 2014

# Main Trends

## High Yield, Equity and Hybrid market

### iTraxx CDSI Generic 5 year – High Yield



### EURO STOXX Banks Index



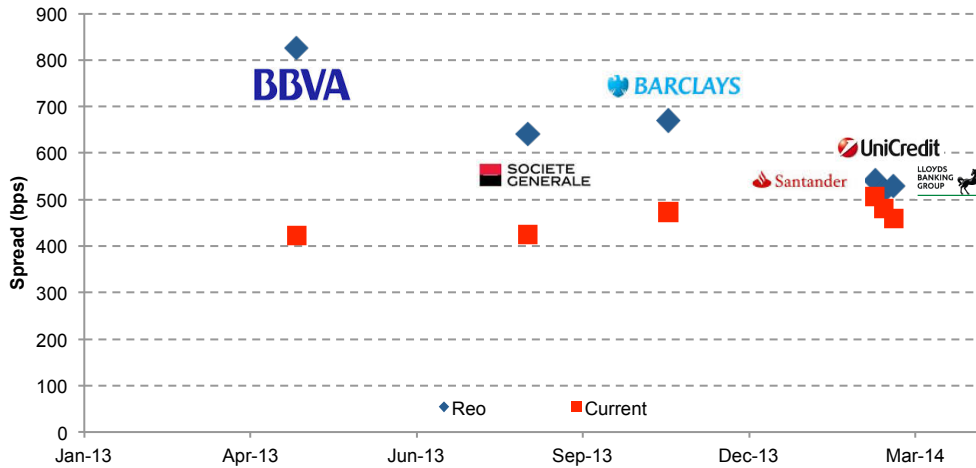
### USD SocGen 8.250% PerpNC5



- **Strong performance of High Yield credit spreads**
- **Positive equity trend**
- **Strong spread tightening on Hybrid recent issuances**

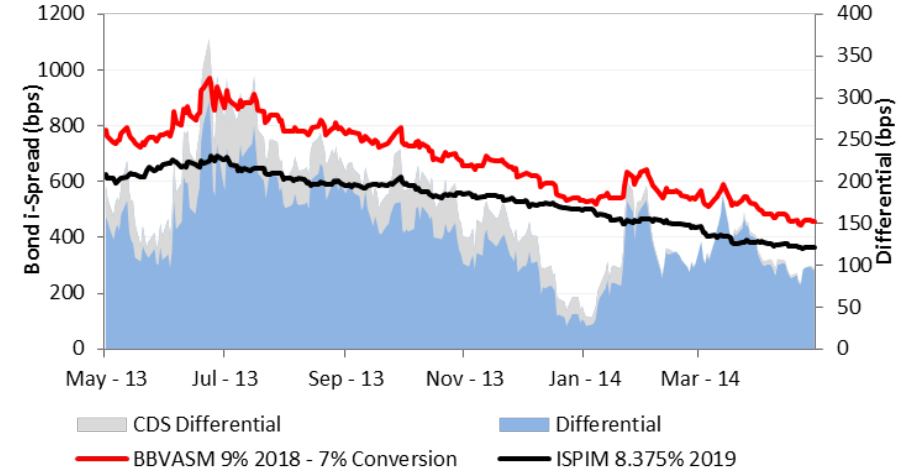
# Is AT1 Cheap for Issuers or Investors at the Moment ?

## Bank AT1: Issuance Spread Development



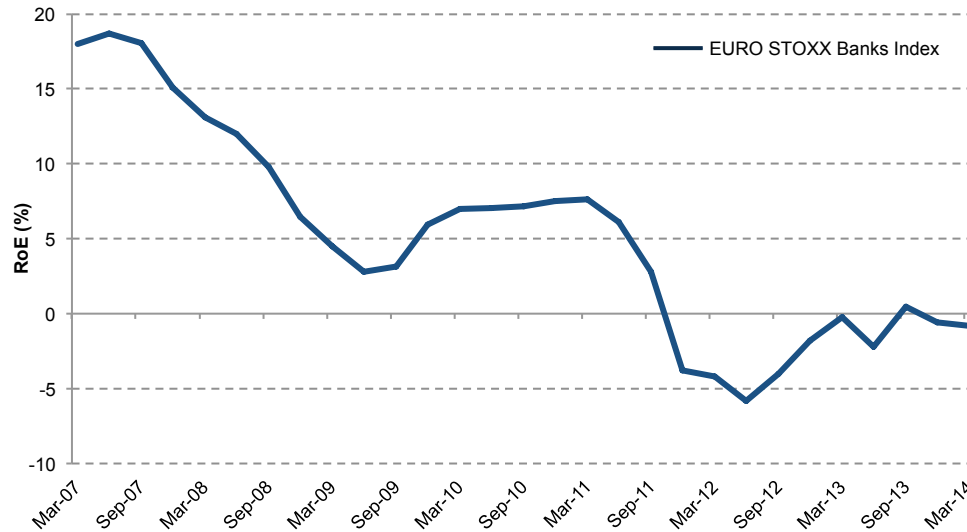
Source: Bloomberg, 06 May 2014

## New Style versus Old Style AT1 Instruments



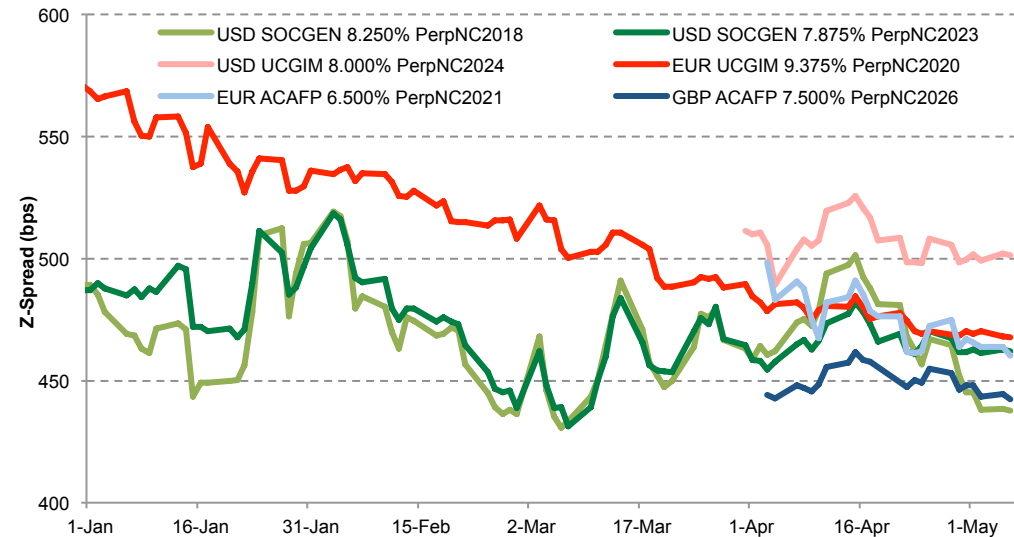
Source: Bloomberg, 06 May 2014

## Return on Equity is Decreasing











Source: Bloomberg, 06 May 2014

## Performance of Selected Recent AT1 Instruments



Source: Bloomberg, 06 May 2014

# Comparison of Additional Tier 1 Precedents

	 UniCredit	 KBC	 Danske Bank	 Santander	 CRÉDIT AGRICOLE	 BARCLAYS	 SOCIETE GENERALE	 BBVA																																																											
Size / Coupon	• USD 1.25bn (Reg S) 8.00%	• EUR 1.4bn 5.625%	• EUR 750m 5.625%	• EUR 1.5bn 6.250%	• USD 1.75bn 7.875% (144A) • EUR 1bn 6.50%	• USD 2bn 8.25% (SEC Reg) • EUR 1bn 8.00%	• USD 1.25bn 8.25% • USD 1.75bn 7.875%	• USD 1.5bn 9.00% (Reg S) • EUR 1.5bn 7.00%																																																											
Issue Date	• 27 March 2014	• 19 March 2014	• 19 March 2014	• 12 March 2014	• 15 Jan 2014 • 01 Apr 2014	• 13 Nov 2013 • 3 Dec 2013	• 29 Aug 2013 • 11 Dec 2013	• 30 April 2013 • 11 Feb 2014																																																											
Maturity Format	• Perp-nc-10	• Perp-nc-5	• Perp-nc-5	• Perp-nc-5	• Perp-nc-10 • Perp-nc-7	• Perp-nc-5 • Perp-nc-7	• Perp-nc-5 • Perp-nc-10	• Perp-nc-5 • Perp-nc-5																																																											
First Call	• 2024	• 2019	• 2019	• 2019	• 2024 • 2021	• 2018 • 2020	• 2018 • 2023	• 2018 • 2019																																																											
Trigger Metric*	Transitional CET1	Transitional CET1	Transitional CET1	Transitional CET1	Transitional CET1	Fully-loaded CET1	Transitional CET1	Transitional CET1																																																											
Trigger Threshold	5.125%	5.125%	7.000%	5.125%	5.125% (Bank) 7.000% (Group)	7.000%	5.125%	5.125%																																																											
Loss Absorption Mechanism	Temporary Write-down	Temporary Write-down	Temporary Write-down	Share Conversion	Temporary Write-down	Share Conversion	Temporary Write-down	Share Conversion																																																											
Instrument Ratings (M/S/F)	- / - / BB-	Baa1 / BB / BB	- / BB+ / BB+	Ba2 / - / -	- / BB+ / BB+	- / B+ / BB+	Ba3 / BB+ / BB	Ba2 / - / -																																																											
Key Takeaways	<ul style="list-style-type: none"> <li>• First Italian</li> <li>• First RegS USD PerpNC10</li> </ul>	<ul style="list-style-type: none"> <li>• First Belgian Issuer AT1 “bucket” filled in one go</li> </ul>	<ul style="list-style-type: none"> <li>• First Ever High Trigger W/D</li> <li>• First Scandinavian</li> </ul>	<ul style="list-style-type: none"> <li>• Lowest coupon at the time of pricing</li> </ul>	<ul style="list-style-type: none"> <li>• First to differentiate trigger level at Group vs Bank</li> </ul>	<ul style="list-style-type: none"> <li>• First SEC Registered AT1</li> </ul>	<ul style="list-style-type: none"> <li>• First French AT1</li> <li>• First Low Trigger w/d</li> </ul>	<ul style="list-style-type: none"> <li>• First EU AT1 Benchmark</li> </ul>																																																											
Capital Buffer at issue***	<table border="1"> <caption>Capital Buffer at Issue Data</caption> <thead> <tr> <th>Bank/Group</th> <th>Base Buffer (%)</th> <th>Additional Buffer (%)</th> <th>Total Buffer (%)</th> </tr> </thead> <tbody> <tr> <td>UniCredit Group</td> <td>5.125%</td> <td>0%</td> <td>5.125%</td> </tr> <tr> <td>UniCredit Bank</td> <td>5.28%</td> <td>21.50%</td> <td>26.78%</td> </tr> <tr> <td>KBC Group</td> <td>5.125%</td> <td>3.475%</td> <td>8.60%</td> </tr> <tr> <td>Danske Bank Bank</td> <td>7.000%</td> <td>4.900%</td> <td>11.90%</td> </tr> <tr> <td>Danske Bank Group</td> <td>7.000%</td> <td>0.700%</td> <td>7.70%</td> </tr> <tr> <td>Santander Bank</td> <td>5.125%</td> <td>2.025%</td> <td>7.14%</td> </tr> <tr> <td>Santander Group</td> <td>5.125%</td> <td>0.208%</td> <td>5.333%</td> </tr> <tr> <td>Crédit Agricole Bank</td> <td>5.125%</td> <td>2.755%</td> <td>7.88%</td> </tr> <tr> <td>Crédit Agricole Group</td> <td>7.000%</td> <td>0%</td> <td>7.000%</td> </tr> <tr> <td>Barclays Group</td> <td>7.000%</td> <td>0%</td> <td>7.000%</td> </tr> <tr> <td>Société Générale Group</td> <td>5.125%</td> <td>0.563%</td> <td>5.688%</td> </tr> <tr> <td>BBVA Bank</td> <td>5.125%</td> <td>2.355%</td> <td>7.48%</td> </tr> <tr> <td>BBVA Group</td> <td>5.125%</td> <td>0.553%</td> <td>5.678%</td> </tr> </tbody> </table>											Bank/Group	Base Buffer (%)	Additional Buffer (%)	Total Buffer (%)	UniCredit Group	5.125%	0%	5.125%	UniCredit Bank	5.28%	21.50%	26.78%	KBC Group	5.125%	3.475%	8.60%	Danske Bank Bank	7.000%	4.900%	11.90%	Danske Bank Group	7.000%	0.700%	7.70%	Santander Bank	5.125%	2.025%	7.14%	Santander Group	5.125%	0.208%	5.333%	Crédit Agricole Bank	5.125%	2.755%	7.88%	Crédit Agricole Group	7.000%	0%	7.000%	Barclays Group	7.000%	0%	7.000%	Société Générale Group	5.125%	0.563%	5.688%	BBVA Bank	5.125%	2.355%	7.48%	BBVA Group	5.125%	0.553%	5.678%
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Source: Transaction documentation, Bloomberg, IFR; according to Issuer presentations as understood

\*Transitional CET1 means Basel 3 CET 1 phased-in capital definition in the European Union. Fully-loaded CET1 means that all measures used shall be calculated on a fully loaded basis.

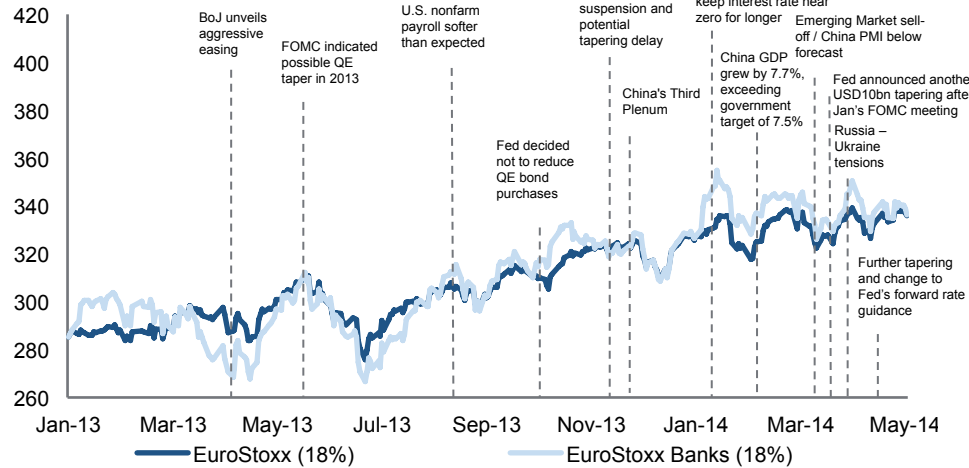
\*\* Acknowledgement of UK bail in powers in terms and conditions required by PRA for foreign law governed notes

\*\*\* Buffer is as disclosed at time of most recent available AT1 roadshow presentation

# Equity Issuance – Strong Volumes and Performance

## EMEA equity markets are back towards highs

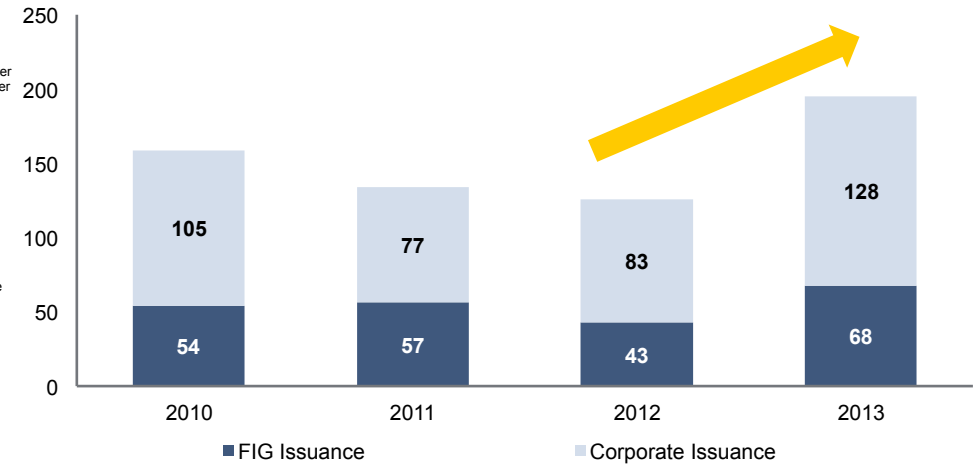
Rebased to EuroStoxx



Source: Bloomberg

## FIG equity issuance is gaining traction

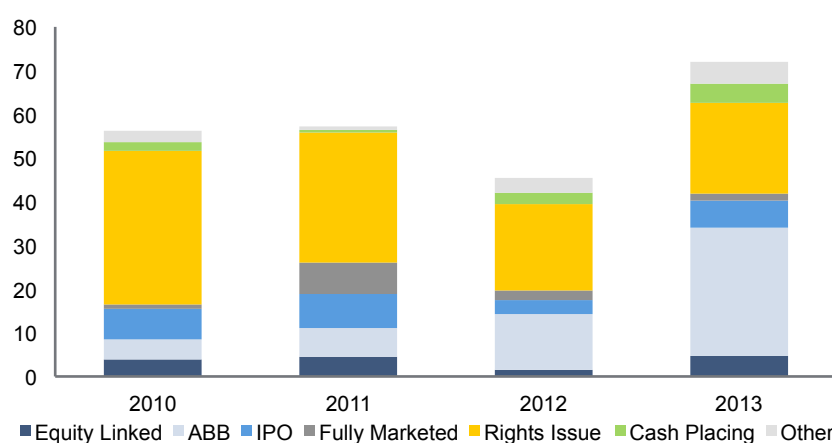
EURbn



Source: Dealogic

## With capital increases representing the bulk of FIG deals

EURbn



Source: Dealogic

## And strong investor response to recent peripheral European financial deals – bellwether of the wider market health

Date	Name	Country	Deal type	Value (EURm)	Demand
Ongoing		GR	FMO	c.2,500	• Strong investor response during pre-marketing
Ongoing		IT	Rights issue	c.5,000	• Resolved the issue regarding foundation participation • Wider international investor base to support the capital call
29-Apr-14		GR	FMO	2,864	• Several times covered books; covered within 3 hours • Strong participation from both foreign and domestic investors
24-Apr-14		IT	Rights issue	1,498	• High take-up of 99.14% for the €1.5bn issue
26-Mar-14		GR	ABB	1,750	• Far greater deal size than that required by the central bank • Heavily subscribed attracting demand worth c.€3bn
25-Mar-14		GR	ABB	1,200	• Books covered within couple of hours of opening • Multiple times covered attracting more than 150 accounts
19-Mar-14		IT	ABB	335	• Strong foreign investor participation • Blackrock and BTG major contributors
04-Mar-14		IE	ABB	681	• Wilbur Ross tripled his invested money with the 6.4% stake sale • Stock appreciation and current premium valuation invited strong demand including North American anchor investors
28-Feb-14		ES	ABB	1,304	• 7.5% stake sale generated net gain of €301m for the state • Multiple subscription with total demand of c.€2.5bn

# Equity vs Hybrid Capital Instruments

What are the main actors thinking about?

## Issuers

### Equity

- Generation of return hurdle rates
- Dividend pay-outs

### Hybrid Capital

- Timing and cost
- Role and magnitude of AT1 and Tier 2 within capital structure

## Regulations

## Regulators

### Equity

- Higher Minimums and Base Buffers – Largely done
- Domestic SiFi, Pillar II and Countercyclical Buffers – Still work in progress in many Countries
- Approval of capital and dividend plans

### Hybrid Capital

- Recovery and Resolution – minimum stock of bail-in eligible instruments while avoiding contagion
- New Applications for Hybrid Capital – E.g. stress test eligibility based on trigger attachment points
- Monitoring of new features and Q&A

- Leverage Ratio

- Asset Quality and Stress Tests

## Investors

### Equity

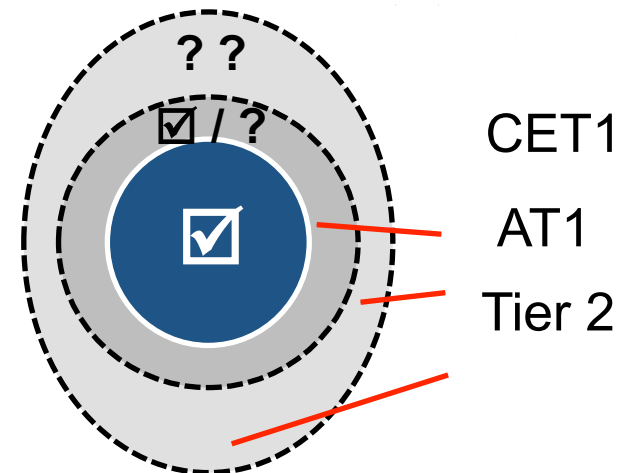
- Price gain and dividend return
- Earnings and fundamental outlook

### Hybrid Capital

- Yield/spread return, and potential price gain during non-call period
- Instrument features and interaction with issuer and regulator approach (e.g. distance to MDA)

## Regulations

→ Views on Layers of Bank Capital Still Evolving !!



# Examples of New Regulatory Applications of AT1

## UK Pillar 2A

- Ability to fill part of the Pillar 2 requirements with AT1 and T2
- Same proportion applied as to minimum capital requirements (56% CET1 / 19% AT1 / 25% T2)
- **BUT** Pillar 2B must be all equity

## European Stress Tests

- Ability to fill Part of the stress test requirement with AT1
- **BUT** very specific triggers required (5.5 / 6.0 / 7.0% CET1) and maximum recognition 1.0% of RWA

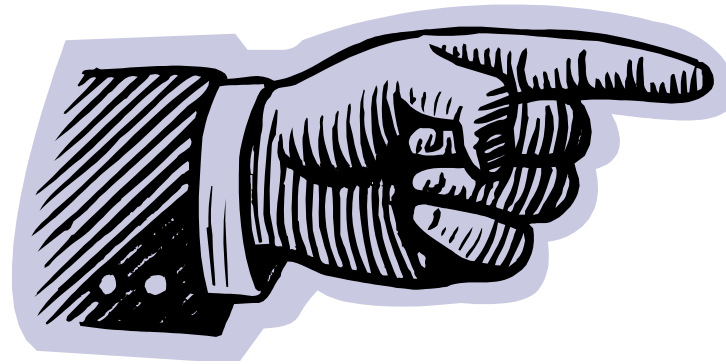
## Leverage Ratios

- AT1 likely eligible in many countries without specific limitations
- **BUT** some regulators require higher triggers or CET1 only

**→ Equity and AT1 likely continue to co-exist but applications of AT1 more specific**



# Conclusions and Discussion



**OVER TO  
YOU !**

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