Covered bond issuers continue to achieve solid execution

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The past week in European FIG primary capital markets was all about covered bonds. Issuers found robust demand and achieved keen execution into the bargain. Demand for EUR 4.85bn-equivalent supply reached around EUR 16bn.

Deutsche Hyp kicked off past week’s proceedings and took the primary covered bond market into a negative spread context, printing its small euro tap on May 6 at MS-1bp. Erste Bank, Santander UK and SpareBank 1 Boligkreditt stormed into the market the next day; Erste pricing its 15-year in territory typically reserved for German issuers. Nykredit Realkredit (euro tap) and Barclays in its home market were next up, with Lloyds also pricing in sterling on May 9. See pricing details below.

How low pricing can go remains a topic of discussion not just in covered bonds but across the FIG funding and capital spectrum. With zero or negative new-issue premiums already a market fixture, how far investors are prepared to continue buying in such size remains something of an open question.

Market technicals are strong, but there is a lot of latent geopolitical and economic event risk out there. For the time being, technicals are clearly winning out and cash-rich investors seem happy enough to continue buying in size as the market grinds tighter. Perhaps with an eye on the tights of early 2018, which the market is still some ways off.

Sell-side research output in the past week has suggested that the introduction of a tiered ECB deposit rate could take its toll on covered bond spreads, as parking cash for free at the central bank will be a much better option for banks than paying for the privilege of holding negative-yielding covered bonds. That’s an interesting thought. If the ECB moves, it’ll certainly be fascinating to see how the market dynamic plays out.

Thin and expensive secondary markets and an inability to secure large lines tends to make primary the only game in town these days. Syndicates continue to go out with optically wide initial price thoughts to build momentum, but the fact that books on sought-after deals are covered in minutes is a sign of exuberance.

Then again, given that something like half of outstanding covered bonds are marked at negative yields, the impetus to gain exposure to new paper above the zero-spread water mark is clear.

In single-name news, it looks like a State bailout of Banca Carige is back on the cards after BlackRock pulled out of its rescue deal. The US fund manager had been working in partnership with the Italian banks, via the Italian Deposit Protection Fund, that own Carige’s EUR 320m 16% convertible hybrid. Conversion of that bond would have given the banks a 43% stake, but control would have gone to BlackRock.

Boldly stating the obvious, perhaps, the bank said “assessments of alternative market solutions to ensure the stability and relaunch of Banca Carige are continuing”. Time is running out, however. The fall-back option is a precautionary recapitalisation; the government has allocated EUR 1bn.to fund the purchase of Carige shares if a private-sector solution fails to emerge.

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Summary of key bank issuance May 6 through May 10 (12:30)

Deutsche Hypo sold a EUR 250m tap of its EUR 500m due 29 June 2026 mortgage covered bond that was 4x covered at the final print of one basis point through mid-swaps. Initial guidance had been MS+2bp, revised to MS flat +/-1bp WPIR. The original deal priced in June 2018.

SpareBank 1 Boligkreditt sold EUR 1bn in seven-year covered bonds. Initial guidance of MS+7bp area was revised to MS+4bp area and the deal priced at MS+2bp at fair value, having amassed demand of EUR 2.5bn.

Erste Bank extended its curve with a no-grow EUR 500m 15-year soft-bullet mortgage covered bond on May 7 that was 6x covered and priced at or slightly through fair value at MS+7bp. Leads had gone out with +12bp area guidance.

Santander UK sold a 4x covered EUR 1bn five-year UK covered bond, picking up a solid bid on the back the relative scarcity of UK benchmark euro paper. Initial guidance of MS+16bp area was revised to MS+11bp +/- 1bp WPIR and the bond reportedly priced at a low single-digit premium to fair value of MS+10bp.

Nykredit Realkredit printed a EUR 100m no-grow tap of its EUR 500m due 1 January 2024 floating-rate SDO covered bond at 3mE+14bp, the middle of the 3mE+14bp area +/-1bp revised guidance range. Initial guidance had been 3mE+14bp-16bp area. The original deal came on 30 November 2018.

Barclays Bank UK, the group's ring-fenced unit, printed its debut SONIA covered bond, a heavily-oversubscribed GBP 500m four-year at fair value of SONIA+48bp. Heavy demand – books reached GBP 2.7bn from 70 accounts – enabled leads to pull in pricing from +55bp area initial guidance, revised to +50bp area +/-2bp WPIR.

Lloyds Bank's return to the SONIA covered bond format came via a GBP 1.25bn five-year trade at a spread of +57bp, flat to or a tad above fair value. The bank had initially gone out with guidance of +62bp and drew in over GBP 2.3bn in demand.

Abanca Corporación Bancaria mandated leads to arrange investor roadshows from 13 May ahead of its debut covered bond (intermediate to long maturity).

Bank of Queensland mandated banks for to arrange a European investor roadshow ahead of a possible intermediate-maturity euro-denominated benchmark CPT covered bond.

HSBC France was out marketing a EUR 1bn euro five-year senior preferred offering on May 10, pushing out MS+50bp area IPTs. Books had reached EUR 2bn by the time books closed at the end of the morning. Guidance came at MS+35bp +/- 3bp and the spread was set at MS+32bp, the tight end of guidance.

Away from financials **Asian Infrastructure Investment Bank**'s inaugural bond is worth noting. The multilateral development bank sold a USD 2.5bn five-year at MS+6bp, against IPTs of +8bp and guidance of +7bp. Demand was in the region of USD 4.5bn, arguably less than the issuer would have liked.

But a debut trade in US dollars from an organisation that only began operations in 2016, in which China has almost a third of the voting rights, is headquartered in Beijing and has no US involvement in the midst of US-China trade tensions was a big ask. Net-net, a decent-enough debut that the supranational will look to outdo in future forays.

Source for deal stats: Bond Radar (www.bondradar.com)

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