

## European Banks – Credit Update

- UBS and Credit Suisse resisted calls from the Swiss regulator to fully freeze dividend payments, highlighting the strength of their balance sheets and business models.
- Highlighting how some banks have actually benefited from the market volatility in March, UBS announced a 34% Y/Y net profit increase in the first quarter.
- Secondary spreads tightened significantly, on SNP/Sr HoldCo paper in particular, albeit liquidity remains reportedly reduced. Primary market activity remained subdued.

**Israel Da Costa, CFA**

Credit Analyst

+44 20 7597 8355

[Israel.DaCosta@uk.daiwacm.com](mailto:Israel.DaCosta@uk.daiwacm.com)

### Restrictions to capital redistribution (Part III)

After euro area, Nordic and UK banks agreed with their respective regulators to restrict capital redistributions, last week saw UBS and Credit Suisse finally reach a compromise with FINMA on dividend payments. Yet, in contrast to their European peers, both banks are going ahead with their YE19 dividend payments. They will, however, be split in half, with the first half to be paid now, the other to be paid at the end of the year. The ability of both banks to resist earlier calls from the usually strict local regulator for a freeze on dividend payments highlights the strength of their balance sheets and business models.

Accordingly, highlighting how some banks have actually benefited from the market volatility in March, UBS also announced last week that it expects 1Q20 net profit of \$1.5bn, up from \$1.1bn in 1Q19, and beating analysts' average estimate by 28%. The bank stated that it expects to report strong operating performance in all business divisions, even after accounting for credit loss expenses and own credit valuation adjustments. CET1 and leverage ratios remain in line with targets, and well above regulatory requirements, despite market conditions leading to a significant increase in credit and market risk RWAs. Earlier last month, Credit Suisse said it was on course to deliver strong results for the first quarter despite the market volatility. The strong trading performance of the Swiss banks bodes well for Barclays, BNPP, SocGen and Deutsche. In all, the lack of profit warnings and the encouraging comments point to a better 1Q20 than the decline in share prices indicates. The earnings season for European banks starts on 22 April with Svenska Handelsbanken, and Credit Suisse on 23 April. The American one starts today with JPMorgan.

### Regulatory changes

The ECB temporarily relaxed last week its collateral eligibility requirements, through three key measures: (i) valuation haircuts were lowered, meaning euro area banks will be allowed to draw more ECB liquidity (e.g. LTROs) from the same collateral pool; (ii) collateral eligibility was expanded, with lower rated and less liquid assets now also being allowed, which is of particular relevance for smaller southern European banks; and (iii) Greek sovereign bonds became eligible for ECB funding. The latter will indirectly support Italian govies, as a potential downgrade of the Italian sovereign rating to sub-investment grade will no longer necessarily render it ineligible as collateral. In turn, this is beneficial for all Italian banks, which held €387bn in Italian sovereign debt as at end-January 2020, making them meaningfully exposed to fluctuations in the price of government bonds, and to their eligibility as collateral for ECB funding. We also note that, despite the significant widening observed in early March, yields on Italian 10Y BTPs closed March at 1.52%, only slightly above December's closure of 1.41%. As a result, Italian banks' Q1 numbers should incur only a limited impact from the fluctuations in BTP prices over the past two months.

In Sweden, the financial regulator announced a postponement of the deadline for Swedish banks to meet their MREL requirements from 2022 to 2024. This will reduce the planned issuance of senior non-preferred debt by Swedish banks in 2020 and 2021.

### Primary and secondary markets

**Primary market** activity remained weak last week. Only Svenska Handelsbanken and Credit Suisse tapped the unsecured market, with final prices still substantially above pre-crisis levels, yet both deals closed significantly inside IPT. SHB was the first Scandinavian bank to tap the unsecured market since the crisis started, whilst the preference for the SP format, rather than SNP, was likely driven by the local regulator's postponement of MREL requirements by 2 years. The likelihood of a similar approach by other Swedish banks in the next few weeks is high. Euro area banks had less urgency to return to the markets, as funding needs have easily been covered by LTROs (total outstanding €890bn, +€20bn W/W) and deposits, whilst regulatory requirements seem to have become of secondary significance for the local supervisors. That, said, after 8 weeks of no activity, Credit Agricole and BNPP reopened the senior unsecured market for euro area banks this morning. With the earnings season for European banks starting next week, primary market activity is likely to remain somewhat subdued.

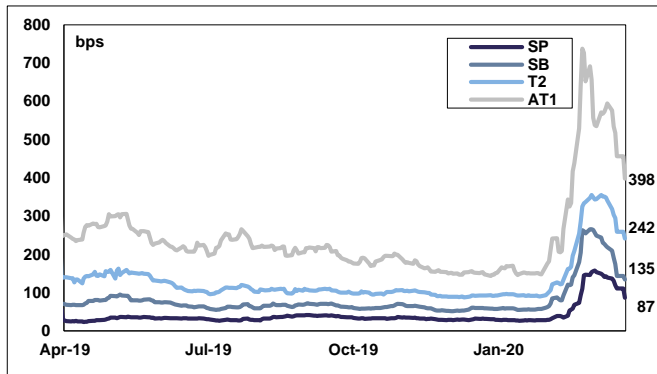
- SHB, SP, EUR1.25bn 5Y, priced at MS+135, IPT at MS+175bps, book orders of EUR8.5bn. In early February the bank priced a 10Y SNP bond at MS+58bps, whilst the last SP paper it placed was in June 2019, priced at MS+30.
- Credit Suisse, Sr OpCo, dual tranche 2Y/5Y, USD1.5bn/USD1.5bn, both priced at T+255bps, 55bps below IPT.

The **secondary** market saw a material tightening of spreads across the debt stack in both the EUR and USD markets last week, with the extent of the shift seemingly magnified by low liquidity. Indeed, EUR SP spreads remain on average 64bps above pre-crisis levels (+88bps for SNP paper), whilst those on USD SP/Sr OpCo debt remain 96bps above pre-crisis levels (+122bps for SNP/Sr HoldCo paper). Interestingly, SNP/Sr HoldCo debt, which recently traded at almost the same level as T2s, is now trading much closer to SP/Sr OpCo paper. In our view, this highlights that markets now view the risk of bail-in of senior debt as having reduced significantly, although a material deterioration of banks' credit profile is still - rightly - expected, reflected in the persistence of wide SP/Sr OpCo spreads.

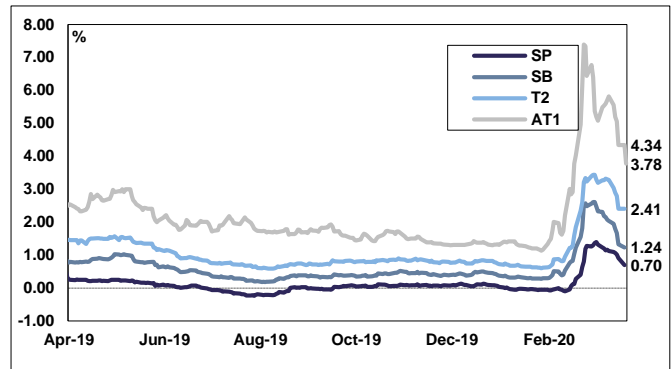
The following pages provide the LTM performance of EUR and USD Z-Spreads and Yields, as well as a breakdown of Z spreads by country and maturity.

### Western European Banks EUR Z spreads

Median Z-spread LTM (bps)



Median Yields LTM (%)



Median EUR SP/Senior OpCo Z-Spread Net Change (bps)

	YTDΔ	Last 5 Days Δ				
		All	1-3Y	3-5Y	5-7Y	> 7 Y
UK	80	-32	-39	-31	-31	-31
DENMARK	58	-28	-23	-34		
FINLAND	58	-33	-31	-35	-36	-26
FRANCE	56	-48	-44	-50	-51	-48
ITALY	76	-33	-26	-29	-35	-31
NETHERL.	153	-44	-30	-37	-45	-51
SPAIN	66	-34	-35	-32	-46	1
SWEDEN	109	-27	-27	-27	-25	
SWITZ.	52	-33		-33		

Median EUR SP/Senior OpCo Z-Spread Value (bps)

	All	Z Spread Curve			
		1-3Y	3-5Y	5-7Y	> 7 Y
UK	112	111	113	113	113
DENMARK	86	80	96		
FINLAND	86	83	87	91	100
FRANCE	84	82	82	89	94
ITALY	118	94	130	104	114
NETHERL.	231	209	223	244	262
SPAIN	93	83	119	88	206
SWEDEN	157	115	158	172	
SWITZ.	83		92	74	

Median EUR SNP/Senior HoldCo Z-Spread Net Change (bps)

	YTDΔ	Last 5 Days Δ				
		All	1-3Y	3-5Y	5-7Y	> 7 Y
UK	125	-96	-91	-96	-104	-82
DENMARK	114	-66	-69	-65	-70	
FINLAND	95	-66		-66		
FRANCE	61	-90	-88	-92	-91	-86
ITALY	187	-59	-58	1	-67	-59
NETHERL.	86	-75	-71	-77	-74	-76
SPAIN	121	-69	-63	-70	-67	-59
SWEDEN	85	-70		-69	-76	-70
SWITZ.	97	-96			-96	-98

Median EUR SNP/Senior HoldCo Z-Spread Value (bps)

	All	Z Spread Curve			
		1-3Y	3-5Y	5-7Y	> 7 Y
UK	186	160	186	192	186
DENMARK	178	162	183	195	
FINLAND	134		134		
FRANCE	113	109	104	114	124
ITALY	301	282	535	302	301
NETHERL.	132	117	109	138	141
SPAIN	179	143	207	175	200
SWEDEN	148		150	131	141
SWITZ.	161			165	161

Median EUR Tier 2 Z-Spread Net Change (bps)

	YTDΔ	5DΔ				
		All	1-3Y	3-5Y	5-7Y	> 7 Y
UK	250	-76	-50	-41	-123	-80
DENMARK	172	-63			-60	-65
FINLAND	211	-35	-21		-31	-90
FRANCE	122	-79	-33	-67	-66	-83
ITALY	204	-81	-113	-31	-78	-81
NETHERL.	163	-79	-98	-27	-188	-77
SPAIN	337	-75		-104	-100	-65
SWEDEN	152	-38			-38	-53

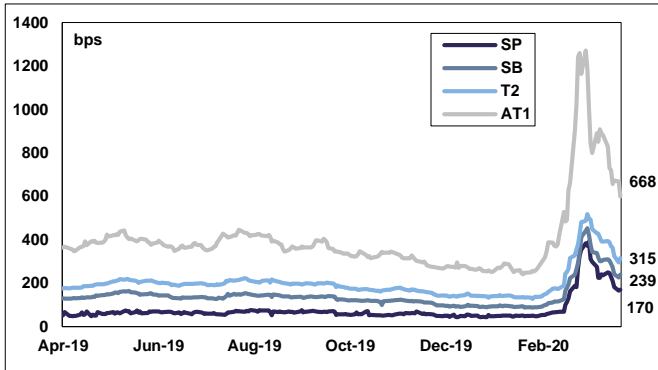
Median EUR Tier 2 Z-Spread Value (bps)

	All	Z Spread Curve			
		1-3Y	3-5Y	5-7Y	> 7 Y
UK	321	310	321		342
DENMARK	318			338	314
FINLAND	255	141		261	271
FRANCE	225	110	200	212	249
ITALY	483	391	307	340	537
NETHERL.	312	192	199	330	321
SPAIN	463		220	463	590
SWEDEN	273			261	287

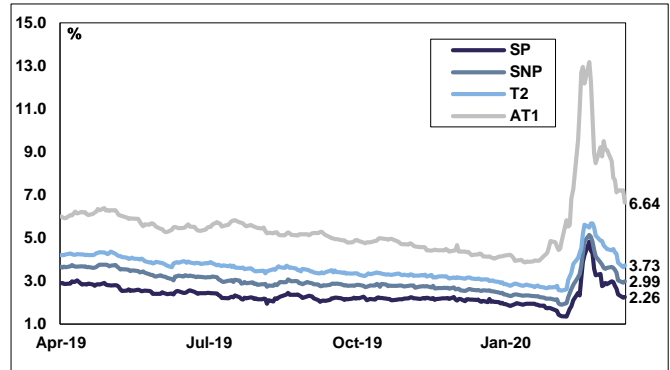
Source: Bloomberg, Daiwa Capital Markets Europe. SP = Senior Preferred/Senior OpCo; SNP = Senior Non-Preferred/Senior HoldCo; T2= Tier 2; AT1 = Additional Tier 1. All figures based on Z to worst spread of public benchmark issuances. Blank cells represent lack of statistically significant data. Figures may not be representative of the whole market.

### Western European Banks USD Z spreads

Z-spreads LTM performance (bps)



Yields LTM performance (%)



Median USD SP/Senior Opco Z-Spread Net Change (bps)

	YTDΔ		5DΔ			
	All	All	1-3Y	3-5Y	5-7Y	> 7 Y
UK	155	-18	-35	-66		
DENMARK	7					
FINLAND	6	-68	-68			
FRANCE	83	-14	-14			
ITALY	124	-6	-97	-81		
NETHERL.	148	-15	-18			
SPAIN	59	-70		-70		
SWEDEN	10	-56	-56			
SWITZ.	159	-27	-27			

Median USD SP/Senior OpCo Z-Spread Value (bps)

	All	Z Spread Curve			
		1-3Y	3-5Y	5-7Y	> 7 Y
UK	230	184	219	177	
DENMARK	201	176			
FINLAND	191	161			
FRANCE	183	142	196	163	
ITALY	356	289	369		
NETHERL.	161	143		174	
SPAIN	233		216		
SWEDEN	216	213			
SWITZ.	182	166	196		

Median USD SNP/Senior HoldCo Z-Spread Net Change (bps)

	YTDΔ		5DΔ			
	All	All	1-3Y	3-5Y	5-7Y	> 7 Y
UK	137	-60	-77	-66	-54	-58
DENMARK	206	-11	-6	92	-18	
FINLAND	179	-32		-32		
FRANCE	154	-53	-41	-35	-55	-57
ITALY	248	-88	-142	-34		
NETHERL.	153	-62	-29	-42	-67	-64
SPAIN	148	-68	-67		-74	-68
SWITZ.	177	-58	-84	-32		

Median USD SNP/Senior HoldCo Z-Spread Value (bps)

	All	Z Spread Curve			
		1-3Y	3-5Y	5-7Y	> 7 Y
UK	252	239	243	269	273
DENMARK	314	319	309	312	
FINLAND	248		248		
FRANCE	252	261	256	249	237
ITALY	383	369	397		
NETHERL.	223	201	215	234	236
SPAIN	277	248		290	294
SWITZ.	243	243	222		265

Median USD Tier 2 Z-Spread Net Change (bps)

	YTDΔ		5DΔ			
	All	All	1-3Y	3-5Y	5-7Y	> 7 Y
UK	194	-64	-83	-84	-74	-50
FINLAND	139	-27	-27			
FRANCE	204	-53		-50	-59	-53
ITALY	223	-44		0	-88	-49
NETHERL.	212	-48	-53	-66	-42	-44
SPAIN	190	-111			-111	

Median USD Tier 2 Z-Spread Value (bps)

	All	Z Spread Curve			
		1-3Y	3-5Y	5-7Y	> 7 Y
UK	352	342	348	315	339
FINLAND	301	243			340
FRANCE	334		335	329	376
ITALY	519		519	487	538
NETHERL.	320	262	240	307	416
SPAIN	333			333	

Source: Bloomberg, Daiwa Capital Markets Europe. SP = Senior Preferred/Senior OpCo; SNP = Senior Non-Preferred/Senior HoldCo; T2 = Tier 2; AT1 = Additional Tier 1. All figures based on Z to worst spread of public benchmark issuances. Blank cells represent lack of statistically significant data. Figures may not be representative of the whole market.

## Credit Research

### Key contacts

<i>London</i>		
<i>Head of Research</i>	<i>Chris Scicluna</i>	+44 20 7597 8326
<i>Financials, Supras/Sovereigns &amp; Agencies</i>	<i>Israel Da Costa, CFA</i>	+44 20 7597 8355
<i>Research Assistant</i>	<i>Katherine Ludlow</i>	+44 20 7597 8318
<i>Tokyo</i>		
<i>Domestic Credit</i>		
<i>Chief Credit Analyst</i>	<i>Toshiyasu Ohashi</i>	+81 3 5555 8753
<i>Electronics, Automobiles, Non-Banks, Real Estate, REIT</i>	<i>Takao Matsuzaka</i>	+81 3 5555 8763
<i>Chemicals, Iron &amp; Steel</i>	<i>Kazuaki Fujita</i>	+81 3 5555 8765
<i>International Credit</i>		
<i>Non-Japanese/Samurai, European Sovereigns</i>	<i>Hiroaki Fujioka</i>	+81 3 5555 8761
<i>Non-Japanese/Samurai</i>	<i>Fumio Taki</i>	+81 3 5555 8787
<i>Non-Japanese</i>	<i>Jiang Jiang</i>	+81 3 5555 8755
<i>London Translation</i>		
<i>Head of Translation, Economic and Credit</i>	<i>Mariko Humphris</i>	+44 20 7597 8327

## DAIR <GO>

All of the research published by the London and New York research teams is available on our Bloomberg page at DAIR <GO>.

### Access our research at:

<http://www.uk.daiwacm.com/ficc-research/research-reports>



Follow us  
[@DaiwaEurope](https://twitter.com/DaiwaEurope)

This document is produced by Daiwa Securities Co. Ltd and/or its affiliates and is distributed by Daiwa Capital Markets Europe Limited in the European Union, Iceland, Liechtenstein, Norway and Switzerland. Daiwa Capital Markets Europe Limited is authorised and regulated by The Financial Conduct Authority, is a member of the London Stock Exchange and an exchange participant of Eurex. Daiwa Capital Markets Europe Limited and its affiliates may, from time to time, to the extent permitted by law, participate or invest in, or be mandated in respect of, other transactions with the issuer(s) referred to herein, perform services for or solicit business from such issuer(s), and/or have a position or effect transactions in a particular issuer's securities or options thereof and/or may have acted as an underwriter during the past twelve months in respect of a particular issuer of its securities. In addition, employees of Daiwa Capital Markets Europe Limited and its affiliates may have positions and effect transactions in such securities or options and may serve as Directors of a particular issuer. Daiwa Capital Markets Europe Limited may, to the extent permitted by applicable UK law and other applicable law or regulation, effect transactions in securities of a particular issuer before this material is published to recipients.

This publication is intended for investors who are not Retail Clients in the United Kingdom within the meaning of the Rules of the FCA and should not therefore be distributed to such Retail Clients in the United Kingdom. Should you enter into investment business with Daiwa Capital Markets Europe's affiliates outside the United Kingdom, we are obliged to advise that the protection afforded by the United Kingdom regulatory system may not apply; in particular, the benefits of the Financial Services Compensation Scheme may not be available.

Daiwa Capital Markets Europe Limited is part of Daiwa Securities Group Inc. Daiwa Securities Group Inc., its subsidiaries or affiliates, or its or their respective directors, officers and employees from time to time have trades as principals, or have positions in, or have other interests in the securities of the company under research including market making activities, derivatives in respect of such securities or may have also performed investment banking and other services for the issuer of such securities. Daiwa Securities Group Inc., its subsidiaries or affiliates do and seek to do business with the company(s) covered in this research report. Therefore, investors should be aware that a conflict of interest may exist.

Daiwa Capital Markets Europe Limited has in place organisational arrangements for the prevention and avoidance of conflicts of interest. Our conflict management policy is available at <http://www.uk.daiwacm.com/about-us/corporate-governance-regulatory>. Regulatory disclosures of investment banking relationships are available at <http://www.us.daiwacm.com/>.

The statements in the preceding paragraphs are made as of April 2020.

## Explanatory Document of Unregistered Credit Ratings

In order to ensure the fairness and transparency in the markets, Credit Rating Agencies became subject to the Credit Rating Agencies' registration system based on the Financial Instruments and Exchange Act. In accordance with this Act, in soliciting customers, Financial Instruments Business Operators, etc. shall not use the credit ratings provided by unregistered Credit Rating Agencies without informing customers of the fact that those Credit Rating Agencies are not registered, and shall also inform customers of the significance and limitations of credit ratings, etc.

### ■ The Significance of Registration

Registered Credit Rating Agencies are subject to the following regulations:

- 1) Duty of good faith.
- 2) Establishment of control systems (fairness of the rating process, and prevention of conflicts of interest, etc.).
- 3) Prohibition of the ratings in cases where Credit Rating Agencies have a close relationship with the issuers of the financial instruments to be rated, etc.
- 4) Duty to disclose information (preparation and publication of rating policies, etc. and public disclosure of explanatory documents).

In addition to the above, Registered Credit Rating Agencies are subject to the supervision of the Financial Services Agency ("FSA"), and as such may be ordered to produce reports, be subject to on-site inspection, and be ordered to improve business operations, whereas unregistered Credit Rating Agencies are free from such regulations and supervision.

### ■ Credit Rating Agencies

#### [Standard & Poor's]

##### The Name of the Credit Rating Agencies group, etc

The name of the Credit Rating Agencies group: S&P Global Ratings ("Standard & Poor's")

The name and registration number of the Registered Credit Rating Agency in the group: S&P Global Ratings Japan Inc. (FSA commissioner (Rating) No.5)

##### How to acquire information related to an outline of the rating policies and methods adopted by the person who determines Credit Ratings

The information is posted under "Unregistered Rating Information" (<http://www.standardandpoors.co.jp/unregistered>) in the "Library and Regulations" section on the website of S&P Global Ratings Japan Inc. (<http://www.standardandpoors.co.jp>)

##### Assumptions, Significance and Limitations of Credit Ratings

Credit ratings assigned by Standard & Poor's are statements of opinion on the future credit quality of specific issuers or issues as of the date they are expressed and they are not indexes which show the probability of the occurrence of the failure to pay by the issuer or a specific debt and do not guarantee creditworthiness. Credit ratings are not a recommendation to purchase, sell or hold any securities, or a statement of market liquidity or prices in the secondary market of any issues.

Credit ratings may change depending on various factors, including issuers' performance, changes in external environment, performance of underlying assets, creditworthiness of counterparties and others. Standard & Poor's conducts rating analysis based on information it believes to be provided by the reliable source and assigns credit ratings only when it believes there is enough information in terms of quality and quantity to make a conclusion. However, Standard & Poor's does not perform an audit, due diligence or independent verification of any information it receives from the issuer or a third party, or guarantee its accuracy, completeness or timeliness of the results by using the information. Moreover, it needs to be noted that it may incur a potential risk due to the limitation of the historical data that are available for use depending on the rating.

This information is based on information Daiwa Securities Co. Ltd. has received from sources it believes to be reliable as of March 7th, 2017, but it does not guarantee accuracy or completeness of this information. For details, please refer to the website of S&P Global Ratings Japan Inc. (<http://www.standardandpoors.co.jp>)

#### [Moody's]

##### The Name of the Credit Rating Agencies Group, etc

The name of the Credit Rating Agencies group: Moody's Investors Service ("MIS")

The name and registration number of the Registered Credit Rating Agency in the group: Moody's Japan K.K. (FSA commissioner (Rating) No.2)

##### How to acquire information related to an outline of the rating policies and methods adopted by the person who determines Credit Ratings

The information is posted under "Unregistered Rating explanation" in the section on "The use of Ratings of Unregistered Agencies" on the website of Moody's Japan K.K. (The website can be viewed after clicking on "Credit Rating Business" on the Japanese version of Moody's website ([https://www.moody.com/pages/default\\_ja.aspx](https://www.moody.com/pages/default_ja.aspx)))

##### Assumptions, Significance and Limitations of Credit Ratings

Credit ratings are Moody's Investors Service's ("MIS") current opinions of the relative future credit risk of entities, credit commitments, or debt or debt-like securities. MIS defines credit risk as the risk that an entity may not meet its contractual, financial obligations as they come due and any estimated financial loss in the event of default. Credit ratings do not address any other risk, including but not limited to: liquidity risk, market value risk, or price volatility. Credit ratings do not constitute investment or financial advice, and credit ratings are not recommendations to purchase, sell, or hold particular securities. No warranty, express or implied, as to the accuracy, timeliness, completeness, merchantability or fitness for any particular purpose of any such rating or other opinion or information, is given or made by MIS in any form or manner whatsoever.

Based on the information received from issuers or from public sources, the credit risks of the issuers or obligations are assessed. MIS adopts all necessary measures so that the information it uses in assigning a credit rating is of sufficient quality and from sources MIS considers to be reliable. However, MIS is not an auditor and cannot in every instance independently verify or validate information received in the rating process.

This information is based on information Daiwa Securities Co. Ltd. has received from sources it believes to be reliable as of April 16th, 2018, but it does not guarantee accuracy or completeness of this information. For details, please refer to the website of Moody's Japan K.K. ([https://www.moody.com/pages/default\\_ja.aspx](https://www.moody.com/pages/default_ja.aspx))

#### [Fitch]

##### The Name of the Credit Rating Agencies group, etc

The name of the Credit Rating Agencies group: Fitch Ratings ("Fitch")

The name and registration number of the Registered Credit Rating Agency in the group: Fitch Ratings Japan Limited (FSA commissioner (Rating) No.7)

##### How to acquire information related to an outline of the rating policies and methods adopted by the person who determines Credit Ratings

The information is posted under "Outline of Rating Policies" in the section of "Regulatory Affairs" on the website of Fitch Ratings Japan Limited (<https://www.fitchratings.com/site/japan>)

##### Assumptions, Significance and Limitations of Credit Ratings

Ratings assigned by Fitch are opinions based on established criteria and methodologies. Ratings are not facts, and therefore cannot be described as being "accurate" or "inaccurate". Credit ratings do not directly address any risk other than credit risk. Credit ratings do not comment on the adequacy of market price or market liquidity for rated instruments. Ratings are relative measures of risk; as a result, the assignment of ratings in the same category to entities and obligations may not fully reflect small differences in the degrees of risk. Credit ratings, as opinions on relative ranking of vulnerability to default, do not imply or convey a specific statistical probability of default.

In issuing and maintaining its ratings, Fitch relies on factual information it receives from issuers and underwriters and from other sources Fitch believes to be credible. Fitch conducts a reasonable investigation of the factual information relied upon by it in accordance with its ratings methodology, and obtains reasonable verification of that information from independent sources, to the extent such sources are available for a given security or in a given jurisdiction. The assignment of a rating to any issuer or any security should not be viewed as a guarantee of the accuracy, completeness, or timeliness of the information relied on in connection with the rating or the results obtained from the use of such information. If any such information should turn out to contain misrepresentations or to be otherwise misleading, the rating associated with that information may not be appropriate. Despite any verification of current facts, ratings can be affected by future events or conditions that were not anticipated at the time a rating was issued or affirmed.

For the details of assumption, purpose and restriction of credit ratings, please refer to "Definitions of ratings and other forms of opinion" on the website of Fitch Rating Japan Limited.

This information is based on information Daiwa Securities Co. Ltd. has received from sources it believes to be reliable as of September 27th, 2019, but it does not guarantee accuracy or completeness of this information. For details, please refer to the website of Fitch Rating Japan Limited (<https://www.fitchratings.com/site/japan>)

February 2020