

Covered Bond Strategy

Alert: BBVA buys Catalunya Banc - spread convergence ahead

Last night, the Spanish Fondo de Reestructuración Ordenada Bancaria (FROB) confirmed that Catalunya Banc will be sold to BBVA, according to Bloomberg. In the beginning of June, the official auction process started for the bank, which was nationalized at the end of 2011 and recapitalized at the end of 2012 (capital injection of €9bn). Moreover, Catalunya Banc benefitted from the asset transfer to SAREB which increased the overall credit quality while junior bondholders had to bear a loss. However, such measures were not enough to find interest for the lender. The first attempts to sell Catalunya Banc via auction were suspended in June 2012 and March 2013, as there was a lack of international and domestic demand for the lender. This might have been driven by the fact that FROB refused to provide an asset protection scheme for Catalunya Banc to potential buyers. Thereafter, FROB decided to "slice and dice" the bank's asset portfolio. This increased investors' specific interests.

Nevertheless, the lender's risk profile continued to deteriorate in the past few years, according to Moody's. With a problem loans ratio of 22.3% the lender is at the lower credit range in Spain, which saw Moody's place the long-term debt rating of B3 on review for downgrade one month ago. Accordingly, the Ba1 covered bond rating is also under review for downgrade now. One main driver was that FROB was unsuccessful in selling a €6.4bn bad loan portfolio, which represented around 20% of the total loan book. However, yesterday, Moody's noted that the portfolio was sold to Blackstone Group last week, which is credit positive as this eases the bank's capital (decrease in risk weighted assets) and liquidity (cash for illiquid assets) position. The sale of this loan portfolio has been crucial for the sale of the whole bank to a peer, in our view.

With the latest acquisition, which has been confirmed by BBVA and FROB via Bloomberg, BBVA is not a first-time buyer of FROB-supported banks. In 2012, the lender acquired Unnim Banc. We think the latest transaction should be positive for Catalunya Banc's issuer and covered bond rating. Moody's acknowledged a month ago when it put both ratings on review for downgrade that the prospect of an acquisition of the lender by a stronger peer could have upward rating implications.

What consequences could this acquisition have? In the secondary market there are still two single-cédulas outstanding in the 2-3yr area. The bonds have been trading around 40 to 60bp above BBVA covered bonds yesterday. We would expect this spread to vanish over the near to medium-term. Investors should also expect to see repercussions in the multi-cédula market, as Catalunya Banc has been active in many structures. Below you can find the bonds where Catalunya Banc has a share of more than 15% and which should be more positively affected.

Michael Spies

+49-69-1366-8403

michael.spies@citi.com

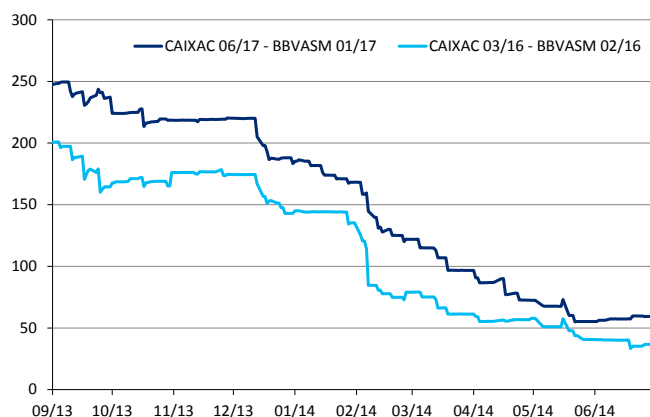
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One other consequence could be the merger of the balance sheet and consequently of both cover pools. It is too early to say what the final acquisition will eventually look like and how this translates into the cover pool composition, especially after the sale of the of the loan portfolio last week. In the past, the acquisition of a bank mostly led to a merger of balance sheets and cover pools. However, this has not always been the case in the Spanish consolidation process.

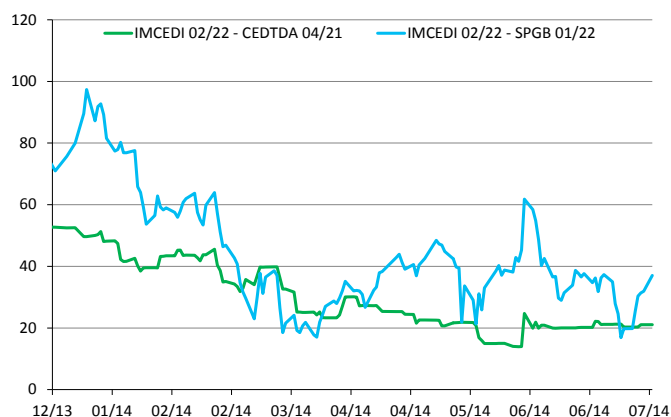
In general, we think that this potential sale is credit positive for covered bondholders of Catalunya Banc covered bonds as well as the multi-cédula market where the lender played a relatively big role (please see Citi's [The Multi-Cédula Road Map](#) for the bank's participation in all structures). Within the multi-cedula market, three bonds have a share of more than 15% of Catalunya Banc: AYTCE 05/15 (41% share), IMCEDI 02/22 (16%), CEDTDA 12/14 (43%). We think that IMCEDI looks relatively attractive, especially compared to equally rated peers like CEDTDA 04/21. The bond is rated Baa1*- and BBB by Moody's and Fitch, respectively.

Figure 1. ASW-Spread of CAIXAC to BBVASM, bp



Source: Citi Research

Figure 2. IMCEDI 02/22 vs multi-cédula peers and SPGB, asw, bp



Source: Citi Research

Appendix A-1

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