

## 2013 IG Corporate Supply Outlook

### More gross, less net

- We forecast \$1,030bn of high grade new issuance in 2013, an increase of 5% from the \$978bn issued so far in 2012.
- Net supply will likely decline by 14% YoY to \$450bn. In addition to the \$480bn of debt maturing next year, we expect to see roughly \$100bn of additional roll-offs as a result of liability management exercises and prefunding activity.
- Nonfinancials should contribute roughly \$400bn to net supply next year as M&A and shareholder-friendly activity drive releveraging. Financial net supply will likely decline to \$55bn.
- Although not incorporated in our forecasts, the possibility of new FDIC requirements on bank holdco capital poses a risk of heavier supply in 2013. Few details on these regulations exist at the moment.
- We forecast Yankee supply to drop by 14% to \$155bn, driven largely by EM and European financials. Our expectations for higher net European nonfinancials partially offset this.

**Sonam T Pokwal**

+1-212-723-3807  
sonam.t.pokwal@citi.com

**Jason Shoup**

+1-212-723-6147  
jason.b.shoup@citi.com

Figure 1. Citi 2013 investment grade supply forecasts, in \$bn

	Gross	2012 Maturities	Net	Gross	2013 Maturities	Net
<b>High Grade</b>	<b>978</b>	<b>617 (455)</b>	<b>361 (523)</b>	<b>1,029</b>	<b>479</b>	<b>450*</b>
<b>Financials</b>	<b>363</b>	<b>450 (288)</b>	<b>-87 (75)</b>	<b>304</b>	<b>249</b>	<b>55</b>
Domestic	246	339 (177)	-93 (69)	231	171	60
Yankee	116	110	6	73	78	-5
<b>Non-financials</b>	<b>615</b>	<b>167</b>	<b>448</b>	<b>725</b>	<b>230</b>	<b>395*</b>
Domestic	418	144	274	507	172	335
Yankee	198	24	174	218	58	160
<b>Domestic</b>	<b>664</b>	<b>483 (321)</b>	<b>181 (343)</b>	<b>739</b>	<b>344</b>	<b>395</b>
<b>Yankee</b>	<b>314</b>	<b>134</b>	<b>180</b>	<b>291</b>	<b>136</b>	<b>155</b>

Source: Citi Research, Dealogic

Numbers in parenthesis denote supply figures ex-TLGP debt.

\* These net figures are adjusted for our expectation of \$100bn in prefunding predominantly in US nonfinancials

See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

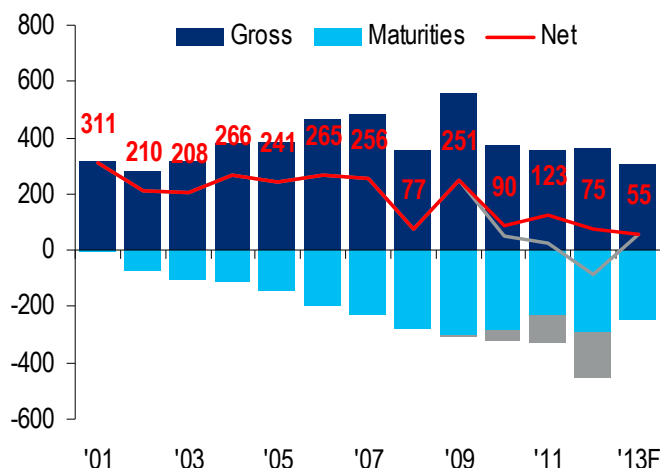
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## More gross, less net

We forecast \$1,030bn of high grade new issuance in 2013, an increase of 5% from the \$978bn issued so far in 2012. Nearly \$480bn of debt matures next year, which we expect to be refinanced. In addition, we expect to see roughly \$100bn of supply as a result of liability management exercises and prefunding activity.

On the other hand, net supply will likely decline next year by 14% YoY to \$450bn as nonfinancial EBITDA growth slows (we remove maturing TLGP from last years calculation of net supply). At an earnings growth rate of 5% for 2013, we see roughly \$125bn of net new issuance from nonfinancials, assuming balance sheet leverage remains unchanged.

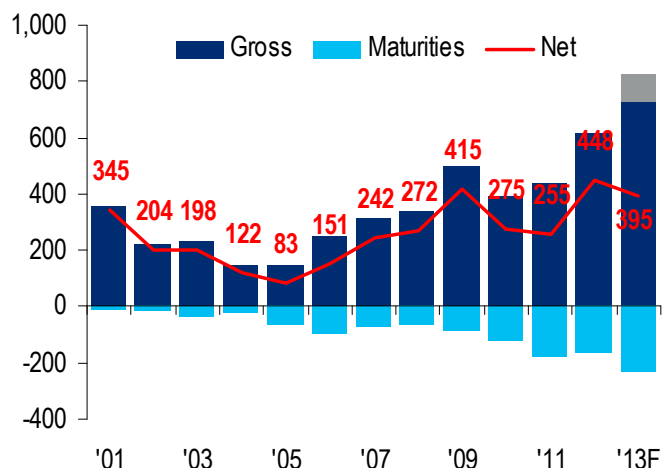
Figure 2. Financial issuance\*, in \$bn



Source: Citi Research, Dealogic

\*the grey bar denotes the TLGP maturities expiring in 2012. The grey line denotes the impact to net supply of this debt.

Figure 3. Nonfinancial issuance, in \$bn



Source: Citi Research, Dealogic

\*the grey bar denotes our estimated LME and prefunding activity.

## Releveraging to continue

In reality, we believe leverage will actually increase in 2013. Fed data implies that net leverage has increased by 0.25x since 2009, and we foresee an additional 0.25x increase over the next 12 months.

Of course, net leverage need not increase through the addition of debt. Indeed, we expect at least half of the increase in leverage to come as a result of lower cash balances, which have been growing at a slower rate than both EBITDA and total debt during the last two years.

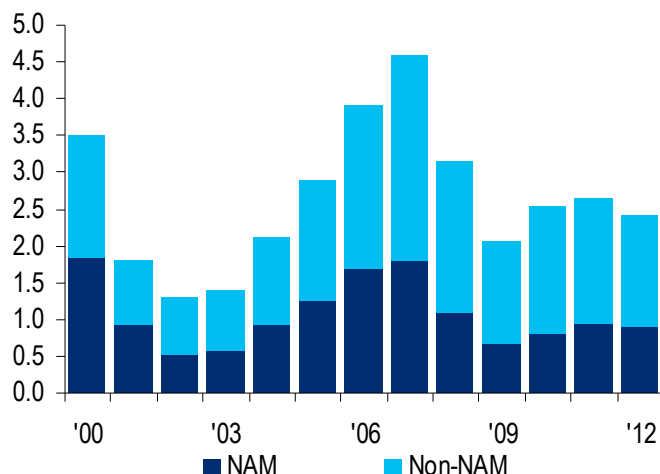
But that still leaves another 0.125x of releveraging that's likely to be debt funded. Applied to the entire high grade nonfinancial universe, that eighth-of-a-turn is likely to result in \$135bn of new debt next year.

We expect debt-funded releveraging to come in two forms: straight share buybacks/dividend deals, and M&A.

In that respect, shareholder friendly activity should continue to be a key driver of net supply in 2013. Although the recent flurry of tax-averting debt-funded dividend deals has undoubtedly pulled forward some releveraging activity from 2013 (perhaps \$25bn or so), it's likely that management teams will continue to be under intense pressure to return cash to shareholders in 2013, especially if margins come under pressure.

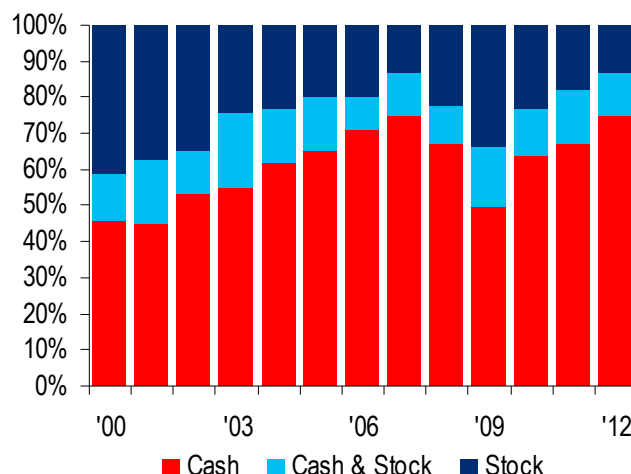
Likewise, we expect to see more M&A activity next year, as companies look to take out costs and boost shareholder value. Indeed, the pickup in 4Q activity suggests to us that 2013 is likely to be more active than 2012. A deal to avert the fiscal cliff, a reduction in global macroeconomic uncertainty, and an extended period of lower volatility, would go a long way toward supporting a long-awaited uptick in M&A.

Figure 4. Annualized global M&A activity, in \$tn



Source: Citi Research, Dealogic  
As of October 31, 2012

Figure 5. How deals are funded, as a % of all M&A



Source: Citi Research, Dealogic  
As of October 31, 2012

## The financial wildcard

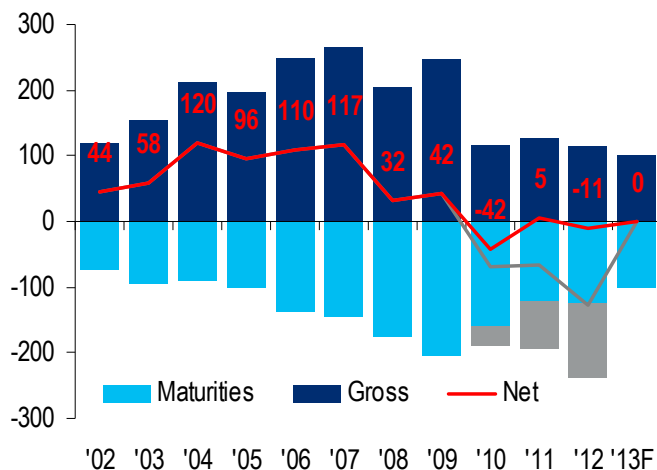
In contrast to nonfinancial corporates, the US banking sector will likely continue to delever. Nevertheless, net supply should rebound materially from last year, as TLGP distortions to maturities come to an end. In total, we expect net USD issuance to come in near zero for the US banking sector in 2013, continuing the trend of the last two years (adjusted for maturing TLGP debt). While not of consequence to the USD supply outlook, we expect US banks to continue to reduce the outstanding amount of their EUR denominated debt.

There is the possibility that US Bank net supply grows significantly over the next few years as a result of new FDIC regulations, although we don't incorporate this risk into the supply outlook. As part of Dodd-Frank, the FDIC has been directed to act as a receiver for large systemically important financial institutions, and in that capacity, has been floating plans to require banks to hold significantly more loss absorbent holdco debt. While details are scarce, recent comments by [Fed Governor Tarullo](#) suggest that other regulators are on board<sup>1</sup>.

Away from the US Banks, we expect financial net issuance to stay steady next year. Net supply for the sector was roughly \$60bn in 2012, corrected for maturing TLGP debt, and we expect roughly the same amount in 2013.

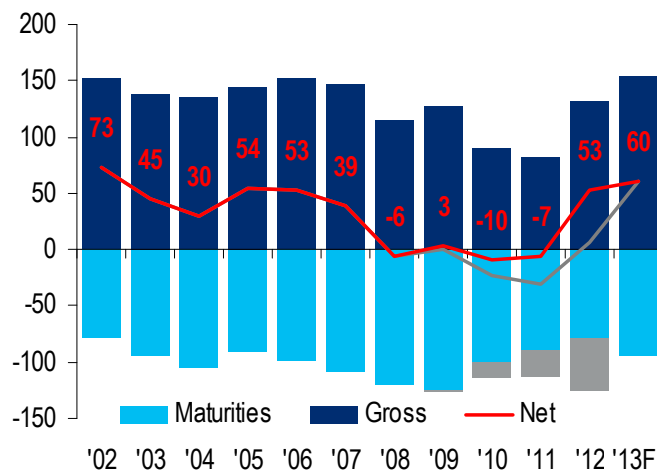
<sup>1</sup> "US Banks: Still Something to Worry About", Keith Horowitz et al, 5 December 2012

Figure 6. US bank debt, in \$bn



Source: Citi Research, Dealogic

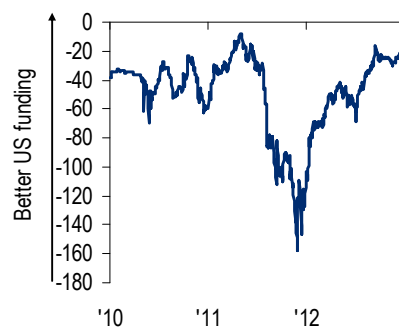
Figure 7. Other US financial debt, in \$bn



Source: Citi Research, Dealogic

## Yankees here to stay

Figure 8. EUR-USD 3mo Basis, in bp



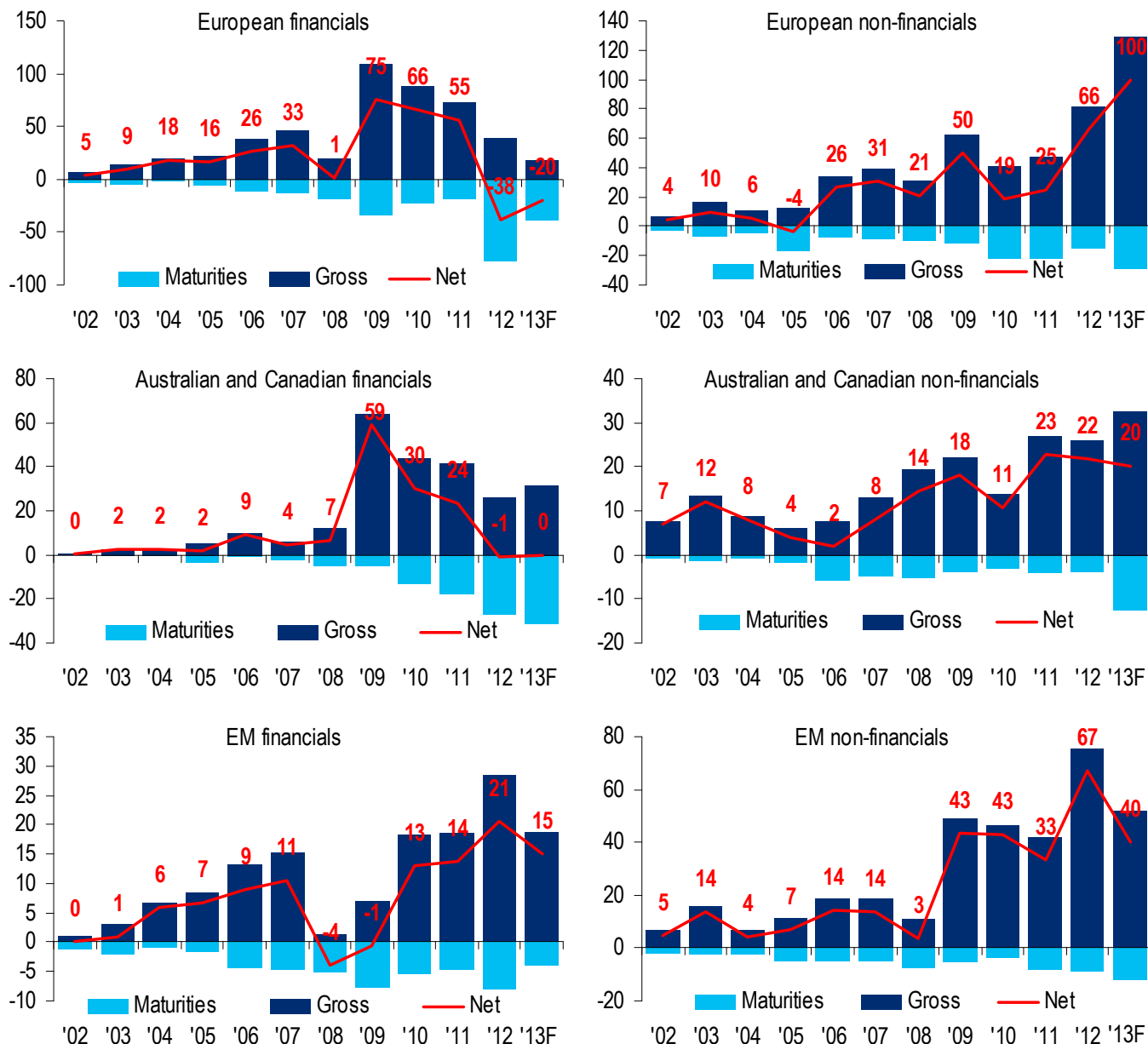
Source: Citi Research, Bloomberg

At least one portion of Yankee issuance should continue to be a large source of supply for US markets: European nonfinancials. Low yields, stable demand, and a relatively small premium to issue in dollars (as expressed by the cross-currency basis swap markets), make the US an attractive market from which to raise funds. Indeed, we see quite a bit of scope for IG rated European nonfinancials to decrease their dependence on bank loans in favor of bonds, as the continent moves to a banking model more similar to the US. As such, we expect net supply to grow to \$100bn in 2013.

By comparison, other Yankee nonfinancial issuance should stay steady or decline. We forecast net USD supply from EM issuers to drop to \$40bn, and net USD supply from Australian, Kiwi, and Canadian issuers to remain unchanged at \$20bn.

Net supply from Yankee financials will most likely be negative. We think European banks will contribute a negative net USD supply of \$20bn in 2013, as peripheral-based banks continue to find the US markets expensive and many European banks scale back US operations. Financials in Australia, New Zealand and Canada are unlikely to do much more than refinance debt coming due. And EM financials may add just \$15bn of net supply to the market.

Figure 9. Yankee supply, in \$bn



Source: Citi Research, Dealogic

## Appendix A-1

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