Covered Bond & SSA View

NORD/LB Markets Strategy & Floor Research

22 March 2023 ♦ 11/2023

Marketing communication (see disclaimer on the last pages)

NORD/LB

Agenda

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RESP NRDR <GO>

Market overview
Covered Bonds

Author: Stefan Rahaus

Primary market issuance activity brought to a halt

Due to the uncertainties on the financial markets and the volatility this has triggered for international trading centres, there has been a lull in issuance activity on the covered bond primary market for the past eight trading days. In addition, there were and are unknowns with regard to the interest rate decisions of the ECB last Thursday and the US central bank today (22.03). We deal with the impacts of the ECB decision in the article entitled "Covered bonds: Under the spell of the banking crisis and ECB hawks?" in this present edition of our weekly publication, and strive to provide an overview of the current risk landscape of the banking sector in the process. Even after the Russian invasion of Ukraine last year, we did not see an issuance pause of eight trading days (aside from the summer and winter recesses). After placing a deal on 23 February 2022, the Canadian CIBC (CM) brought the covered bond primary market back to life on 3 March 2022, before four issuers successfully approached investors with fresh supply on 8 March 2022. This helped to get the ball rolling again in the market for senior unsecured bonds. We would expect the current situation to develop in similar fashion when the financial markets calm down and volatility recedes. Even if the inverse swap curve is not quite as pronounced now, in the current environment short maturities are likely to be preferred by investors and deals of this kind should be the easiest to place as well. In view of the significantly higher funding levels of refinancing instruments compared with the beginning of March, which rank above covered bonds in the liability cascade, we are still comfortable with our updated issuance forecast of EUR 189.5bn despite the rather extended break from issuance activity.

Issuer	Country	Timing	ISIN	Maturity	Size	Spread	Rating	ESG
-	-	-	-	-	-	-	-	-

Source: Bloomberg, NORD/LB Markets Strategy & Floor Research (Rating: Fitch / Moody's / S&P)

Secondary market: covered bonds illiquid, moderate spread widening

High levels of volatility on the interest rate and swap markets have been making it difficult for traders to quote current trading prices adjusted to market events, which has resulted in an extremely illiquid market over the past few days. Compared with other asset classes, the widening of spreads in the covered bond segment can be described as very moderate at two to five basis points. However, it should hardly come as a surprise to learn that the outstanding EUR benchmark from Credit Suisse (CS; ISIN: CH1230759495) forms an exception here. At its peak, the ASW spread widened from just under 60bp to around 120bp. The ramifications of the CS takeover by UBS, which does not have any outstanding EUR benchmarks bonds of its own, are described in a separate paragraph below.

Malta implements Covered Bond Directive in national law

As the competent authority for the implementation of the EU Covered Bond Directive, the Malta Financial Services Authority (MFSA) announced in a newsletter dated 17 March 2023 that the provisions have now been implemented. Malta was the last EU member state to integrate these requirements in national law. In due course, the regulatory authority will flesh out the amended legislation with extra details. In our records of EUR benchmark and EUR sub-benchmark deals, Malta is conspicuous by its absence to date. Nevertheless, we welcome the fact that the chapter “Implementation of the EU Covered Bond Directive” can now be brought to a close. Deals in the “European Covered Bond” or “European Covered Bond (Premium)” format will then also be possible from Malta once the amendments to the implemented directive are finalised.

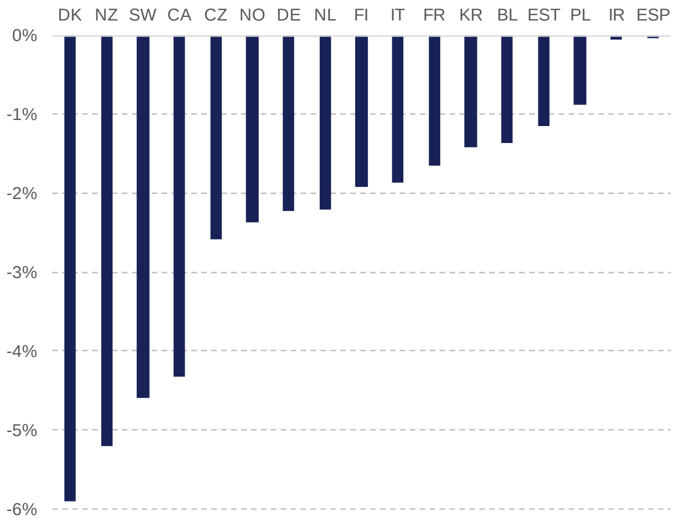
Statement of the European Supervisory Authorities and the ECB on the disclosure of information on the subject of climate change for structured finance products

The European Supervisory Authorities (ESA) and the ECB are working to improve disclosure standards for securitised assets. In a joint statement dated 13 March 2023, they are calling on EU-level issuers, sponsors and originators to proactively collect meaningful and comprehensive information on climate-related risks during the process of developing securitised assets. As the value of these underlying assets can be affected by climate-related events, reporting on existing climate-related metrics needs to be improved. Furthermore, additional indicators are required because a lack of climate-related data hinders the classification of products and services as sustainable under the EU Taxonomy Regulation and the Sustainable Finance Disclosure Regulation (SFDR). In addition, templates for the voluntary sustainability-related disclosures for "simple, transparent and standardized" (STS) securitisations were developed. As early as March 2022, the EBA also provided guidelines for the implementation of ESG standards in the context of securitisations, before the ECB additionally announced in July 2022 that it was taking further steps to include climate protection aspects in its asset purchase programmes and collateral framework. This is intended to take better account of climate-related financial risks when implementing monetary policy. Covered bonds are not directly subject to the SFDR, but are to be included in the disclosure requirements due to comparability requirements in order to ensure a level playing field for similar asset classes.

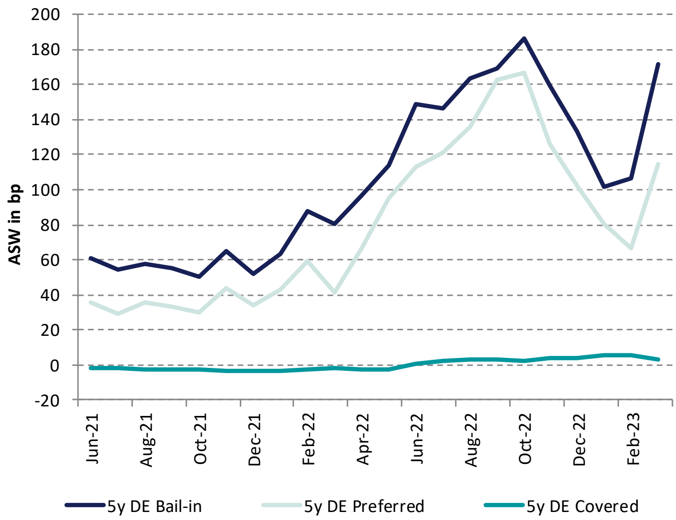
IMF: house prices fall further due to rising credit costs

According to data from the Organisation for Economic Co-operation and Development (OECD), the dynamics of the global real estate markets are weakening after years of steady growth. Overall, 31 of the 46 economies included in the OECD data set showed a decline in inflation-adjusted house prices (see chart below left) in comparison with the previous quarter. According to the IMF, this development is a reflection of the way in which the real estate market is reacting to rising interest rates. Key interest rates have risen by four percentage points on average in the major economies. An IMF conclusion, based on cross-country data, claims that for every one percentage point increase in real interest rates, house price growth slows by about two percentage points. As a result, house prices would be expected to stabilise if central banks are able to slow or suspend rate hikes. Due to the stable labour markets in the EUR benchmark jurisdictions, among other aspects, we currently see no risk to the credit quality in the covered bond cover pools.

Development of house prices in selected countries (Q/Q; inflation-adjusted)



ASW spreads DE covereds / preferred / bail-in (5y; generic)



Source: OECD, IMF, market data, NORD/LB Markets Strategy & Floor Research

UBS acquires Credit Suisse and Switzerland's only EUR benchmark programme

Last Sunday, UBS announced a takeover of Credit Suisse (CS), after CS credit spreads widened hugely (cf. ad hoc announcements here and here). ASW spreads in other banking markets were also impaired. The chart on the right-hand side above depicts the generic ASW spread movements of senior unsecured bonds and covered bonds of German issuers. Similar to the spread developments seen in past crises, a clear outperformance was again recorded for covered bonds. The announcement that UBS had agreed a takeover of CS is also likely to have an impact on CS's outstanding covered bonds. At present, we can only identify the ISIN CH1230759495 (EUR 750m; issued on 01 December 2022, at ms +73bp; residual term to maturity 2.7y) in the EUR benchmark segment. According to our understanding, with the takeover, the corresponding covered bond programme will also be transferred to UBS, with the result that this covered bond will in turn become a UBS covered bond. We currently do not see any change in the regulatory treatment of the affected covered bonds (20% risk weight, no LCR eligibility and no ECB repo eligibility).

Market overview SSA/Public Issuers

Authors: Dr Norman Rudschuck, CIIA // Jan-Phillipp Hensing // Valentin Jansen

ECB Governing Council sticks with +50bp: imprudence, ignorance or backbone?

The market turbulence has by no means left the ECB Governing Council cold. Nevertheless, the central bankers stuck to their "forward guidance", which should actually no longer exist. But regardless of this, a pure focus on data dependence would not have justified turning away from the 50 basis point step (cf. Fixed Income Special). However, irrespective of this, even focusing purely on the data would not have justified a departure from the 50bp hike, because the upward pressure on prices in the euro area remains considerable. All three key ECB interest rates were raised accordingly. The ECB Governing Council by no means ignored the latest developments in the banking sector and concerns in relation to the stability of banks – which is why we would not speak of imprudence. As expected, opinions on the Governing Council varied. It is our view that the ECB, in its role as banking supervisor, can certainly rely on a banking sector that is soundly capitalised and in an adequate liquidity position overall. However, the monetary authority will have to deal more intensively with the consequences of the steep interest rate course potentially having an uneven effect on the earnings and liquidity situation of banks going forward. It may also be necessary to focus on individual banks while avoiding contagion effects. Following this logic, the “stress” in the banking sector remains for the time being. In line with expectations, there was no new information relating to reinvestments in the context of the APP and PEPP purchase programmes. The pace of purchases in the APP will remain at an average of EUR 15bn per month until June 2023, and “its subsequent pace will be determined over time”. As concerns the PEPP, principal payments from maturing securities purchased under the programme will be reinvested in full until at least the end of 2024. Looking at the impact of yesterday’s decision on the SSA segment, it is still our assertion that while supras are by no means operating in a vacuum space, if order books are oversubscribed many times over then it will be in this subsegment. The primary market for SSA issuers was also comparatively open compared to other segments last week: tap issues were placed by KfW in the German agency market on Tuesday (EUR 1.0bn) and by the State of Lower Saxony on Wednesday (EUR 0.5bn). However, the ECB’s slow but steady progress in ending its asset purchase programmes could shake up spread variance in the medium term and return the focus to fundamental differences.

ECB projections: inflation remains high for the time being – “soft landing” ahead?

The adjusted ECB Staff Projections speak a clear language here. For 2023, the central bank's experts still expect an average inflation rate of 5.3% (previously: 6.3%). For 2024, according to the projections, 2.9% (previously: 3.4%) would still be on the books, while for 2025 a further decline to 2.1% (previously: 2.3%) is painted on the wall. Inflation excluding energy and food, on the other hand, is seen by the ECB at 4.6% in 2023, before "coming down" in 2024 (2.5%) and 2025 (2.2%). We can see clearly a disinflationary trend here. With regard to economic activity, the "soft landing" scenario remains in our view. After all, the central bank experts adjusted their projection for 2023 to 1.0% (previously: 0.5%). For the following years 2024 and 2025 the central bank communicated a growth rate in the common currency area of 1.6% (2024 previously: 1.9%; 2025 previously: 1.8%). There is almost no better way to describe a soft landing in figures.

Nordic Investment Bank: 2022 promotional business shaped by long-term loans

The Nordic Investment Bank (ticker: NIB) reported a significant increase in demand for long-term financing in promotional financing last year. New lending in this segment amounted to EUR 4.1bn in 2022, compared with EUR 1.9bn in the previous year. As at year-end 2022, the loan portfolio amounted to EUR 22.3bn, with total assets rising from EUR 37.5bn in 2021 to EUR 39.3bn. To meet the growing demand for financing, NIB placed a record volume of EUR 9.6bn through 111 transactions. For the first time in the bank's history, the issuance of NIB Environmental Bonds (NEB) for the year surpassed EUR 1bn. The mission of NIB is currently defined as providing financing to promote sustainable growth in its eight member countries that are its owners (namely, Denmark, Estonia, Finland, Iceland, Latvia, Lithuania, Norway and Sweden). "Our mandate to finance projects that improve productivity and benefit the environment is more important than ever," NIB President and CEO André Küüsvek said in a press release discussing the 2022 funding statement. NIB plays an important stabilising role in the energy crisis and market turbulences, which have not least been brought about by Russia's war of aggression in Ukraine. The promotional bank also started implementing resolutions from the business strategy review, which had been concluded by the Board of Directors at the end of 2021. This included expanding its lending in the area of sustainability-linked loans. In terms of a sectoral breakdown, lending in the area of energy generation amounted to 10% of all new commitments, while the energy infrastructure segment (e.g., expanding electricity networks) accounted for a share of 16%. The Nordic Investment Bank will continue to play an important role as the international financial institution for the Nordic-Baltic region, helping it to stay in the forefront of the technology and the green transformation, as Küüsvek explained in the press release.

Baden-Wuerttemberg adopts new law for sustainable financial investments

As we previously reported in our weekly edition on 22 February, the State of Baden-Wuerttemberg (ticker: BADWUR) has adopted a new Climate Protection Act, which includes an amendment to the Landeshaushaltsordnung (regional budget regulation) and firmly anchors sustainability in the state budget as a mandatory criterion. Building on this, the state parliament further resolved a law on 2 March relating to sustainable financial investments, which currently make up a volume of EUR 17bn. Sustainability is therefore being established as a basic principle of investment that must no longer conflict with the own sustainability goals going forward. This is also intended to help incentivise companies to make greater investment in sustainability and climate protection in future. In addition to orientation towards the Paris Agreement target of 1.5°C, the new regulations essentially also include alignment with the EU taxonomy. In future, investments will no longer conform if they hinder or impair one or more of the six environmental objectives of the EU taxonomy. Furthermore, preference should be explicitly given to companies that achieve a particularly high share of their sales through environmentally sustainable economic activities pursuant to the EU taxonomy, as soon as a realistic assessment can be made from the data. "As a public investor, our financial investments must correspond to the values we represent elsewhere," said Dr Danyal Bayaz, Minister of Finance for Baden-Wuerttemberg, explaining the decision. Against the backdrop of strong momentum in the field of sustainable finance, the aim is to report to the state parliament every two years and carry out a comprehensive evaluation as well as any necessary adjustments every four years.

NRW.BANK 2022 promotional financing: new commitments up +13% (Y/Y)
Over the past year, NRW.BANK (ticker: NRWBK) once again supported the State of North Rhine-Westphalia and its municipal authorities in fulfilling their public duties. Overall, promotional financing of EUR 13.6bn was awarded in 2022. By comparison, the volume of new commitments in the previous year was around EUR 12.0bn, so this represents an increase of +13%. In terms of themes, the promotional bank of North Rhine-Westphalia divides its new business into the following fields: I. special programmes for ad hoc needs (EUR 1.7bn; +55% Y/Y), II. energy transition/environmental protection (EUR 3.1bn; -9%) and III. other promotional financing (EUR 8.8bn; +17%). In relation to the considerable rise in ad hoc needs for financing, the bank highlights the promotion of transformation-related financing as well as supporting the Federal State in acute special situations such as coping with the current multiple crises. In total, around EUR 4.8bn was invested in the promotional area of "energy transition/environmental protection" with various special programmes, in order to alleviate the effects of the war in Ukraine and the floods in 2021, for example. This represents over half of the promotional business in 2022. "We live in times of upheaval and multiple crises. The need for transformation is huge and particularly high demands are being made on promotional banks right now," said Eckhard Forst, Chairman of the Managing Board of NRW.BANK, at the annual press conference. The Bank intends to continue supporting North Rhine-Westphalia in coping with these challenges and to provide effective promotional impulses to accelerate the transformation processes – for a sustainable and digital North Rhine-Westphalia. This commitment can also be observed on the funding side: according to the Bank, 25% of funding is now based on the issuance of green and social bonds. In 2022, NRW.BANK appeared on the capital markets three times in these segments, raising a total of EUR 2.5bn via two green bonds and one social bond, all in EUR benchmark format, with maturities of up to 15 years. NRW.BANK has been issuing green bonds since 2013 – Europe's first regional promotional bank doing so at the time. To date, it has issued 13 green bonds overall with a total volume of around EUR 7bn.

Moody's raises rating of Council of Europe Development Bank to Aaa (outlook stable)
After placing the Aa1 rating of the Council of Europe Development Bank (CEB; ticker: COE) on review for upgrade in December 2022, the rating agency Moody's upgraded its assessment for the multilateral development bank to its highest rating of Aaa (stable outlook) following the approval of its new Strategic Framework 2023-2027 and a capital increase. The rating report published on 10 March 2023 shows a material improvement of the CEB's creditworthiness due to the new Strategic Framework and capital increase. The rating agency highlights that the magnitude of the capital increase (EUR 1.2bn) is a testament to the strong support for the CEB from the 42 member states. This was the first direct paid-in capital contribution from its member states in the 65-year history of the institution. According to Moody's risk experts, the CEB also has enhanced relevance in tackling key social challenges in Europe. The stable outlook reflects Moody's perspective that the risk resulting from the CEB's operations in Ukraine with loans totalling EUR 465m will be absorbed by its capital increase. Alongside Moody's, CEB also has ratings from Standard & Poor's (AAA, stable outlook) and Fitch (AA+, positive outlook).

Primary market

Even after last week's ECB meeting, the current market turbulence continues to inspire a wait-and-see approach from many issuers. However, the market was not completely idle, so we can at least comment on a few – albeit not many – transactions. Let's proceed in chronological order, as usual: one day before the ECB key interest rate meeting, the State of Lower Saxony (ticker: NIESA) found a funding window and consequently increased NIESA 2 ¾ 02/17/31 by EUR 500m to bring the total volume to EUR 1.25bn. It was priced at ms -2bp, with no narrowing versus the guidance. The order book of the deal amounted to EUR 800m. In our last issue we drew your attention to the EU bond auction on 20 March and can now comment on the results this week. Two bonds were topped up, though this again did not include a green bond. The total volume of the "shorter" EU 2 10/04/27 was increased by EUR 1.85bn to EUR 12.915bn. The bid-to-cover ratio at auction was 1.91x. The "longer" EU 1 07/06/32 was increased by a slightly smaller amount (EUR 1.746bn) to bring the current outstanding volume to EUR 19.007bn. At 1.45x, the bid-to-cover ratio was also slightly lower. Nevertheless, the EU – which is also its ticker – raised a total of almost EUR 3.6bn during the auction. We are expecting the next transaction from the EU to follow shortly: RfPs were already sent to the relevant banking group last week and, according to the funding plan published on a half-yearly basis, a syndicated transaction is scheduled for the coming week. Yesterday, on Tuesday, the State of Saxony also ventured onto the trading floor with its first new bond since the beginning of the turmoil. A total of EUR 500m WNG was sought for a term of five years. The pricing was at ms -9bp, with no narrowing versus the same guidance achieved. The order book of EUR 500m is proof of a precision landing for this deal, with a coupon for the bond of 2.875%. This was the first EUR benchmark issue from the State of Saxony in 2023, which had last placed a bond in December 2021. Taking into account the gross credit authorisation for Saxony in the amount of EUR 0.28bn, no further EUR benchmark issue is expected this year, although this should only be regarded as a funding target in the broadest sense.

Issuer	Country	Timing	ISIN	Maturity	Size	Spread	Rating	ESG
SAXONY	DE	21.03.	DE0001789352	5.0y	0.50bn	ms -9bp	- / - / AAA	-

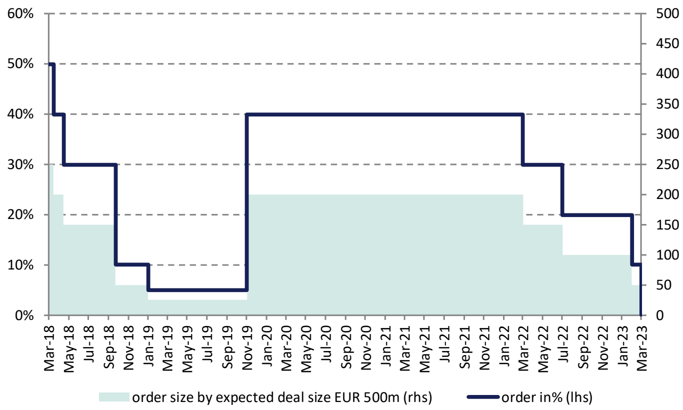
Source: Bloomberg, NORD/LB Markets Strategy & Floor Research (Rating: Fitch / Moody's / S&P)

Covered Bonds
Covered Bonds: Under the spell of the banking crisis and ECB hawks?
Author: Dr Frederik Kunze

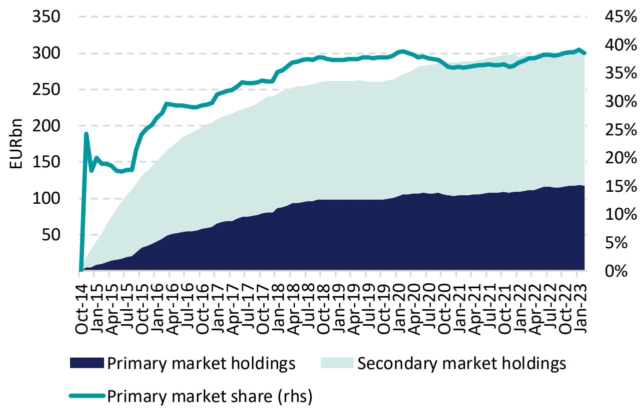
The ECB is holding its course: what does this mean for the covered bond market?
The ECB Governing Council held the scheduled monetary policy meeting under extremely difficult conditions last week. The monetary authorities also had to evaluate what signals a departure from its planned interest rate hike (+50bp for all three key interest rates) would send to capital market players (see NORD/LB Fixed Income Special dated 16 March). Unsurprisingly, general sentiment was and continues to also be reflected in the covered bond segment. As in the periods of crisis or uncertainty in recent years, this was apparent in a suspension of primary market activity and a perceptible wait-and-see approach in secondary trading. A widening of the spreads on covered bonds was also observed, although these movements can be described as modest by and large compared with other asset classes. In this article we shall provide a brief assessment of the ECB's decision from the perspective of the covered bond market and, in doing so, also refer to the current risk landscape in the banking sector.

ECB interest rate decision: focus on interest rate turnaround and risk position
At the most recent monetary policy meeting and the subsequent press conference, the focus was clearly on continuing the turnaround in interest rates and the general risk position. With regard to the ECB's APP purchase programme, which has been a major driver for the covered bond segment over the years, the information available is largely unchanged. In this respect, the question as to what extent the ECB will be actively involved in the covered bond secondary market in the second half of the year remains unanswered. In our opinion, repayment of the APP portfolios has already been priced in to a very significant degree. Accordingly, there were no longer any signs of spreads widening dramatically in the course of the Eurosystem's withdrawal from the covered bond primary market. The fact that the ECB now reinvests solely via the secondary market, does, however, provide it with additional liquidity. In principle, however, we no longer see any critical market size in the purchases although the reduction in reinvestments may still lead to a modest widening in spreads. Should the ECB's Governing Council still decide to suspend reinvestments entirely in the first half (we discussed possible scenarios within our ECB Preview), this is definitely likely to go hand in hand with significantly wider spreads. Admittedly, this should be due more to general sentiment and should not be the consequence of a sustained change in the technical market or fundamental assessment of the situation in the covered bond segment. The latest ECB statement and subsequent comments in the course of the press conference do not therefore persuade us to adjust our expectations as far as spreads are concerned, although the current market phase is leading to increased volatility in spreads. In actual fact, however, this viewpoint should not be confused with the fact that the decision on interest rates or question marks and concerns with regard to the situation on the banking market leave this sub-segment untouched. In fact, in terms of the financial institutions affected by the latest crisis so far, it is their own liquidity that has ultimately proved to be their Achilles' heel. It is therefore not really surprising that this topic area was taken up in the closing passage of the ECB's statement.

ECB: primary market purchasing behaviour (CBPP3)



ECB: CBPP3 volume

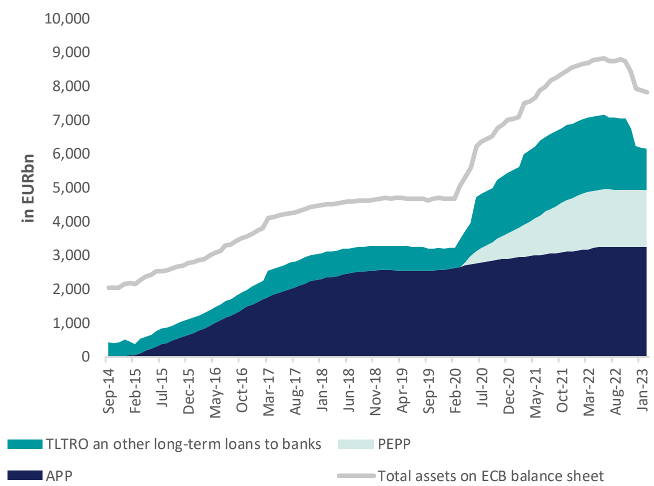


Source: ECB, market data, Bloomberg, NORD/LB Markets Strategy & Floor Research

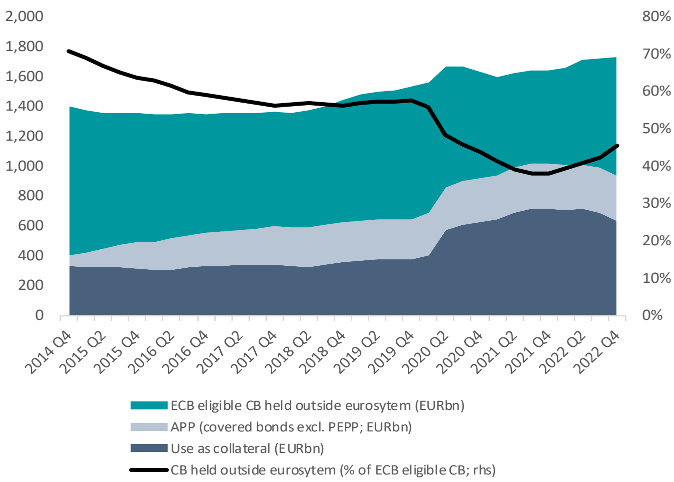
CBPP3, TLTRO III and ECB balance sheet: game changer for the covered bond market?

The liquidity of banks is also being significantly affected by the less accommodating monetary policy. Here, too, TLTRO III repayments (cf. [CB&SSA View dated 1 March]) and the general reduction in the ECB's balance sheet are already largely priced in in our opinion. Nevertheless, this monetary policy course now raises the question as to the liquidity situation of banks. Referring to the EBA's database, we have repeatedly pointed to the largely sound capitalisation and liquidity of banks in the EEA and would continue to share this view. However, the ECB's explicit reference to possible liquidity support also shows the potential dangers that can emerge from even an "irrational" crisis of confidence. In this environment, however, the central bank must maintain its course and, at the same time, create framework conditions that offer as little scope as possible for a loss of confidence. In our opinion, the recent past has shown that the reduction in the ECB's balance sheet can take place without significant collateral damage, and it cannot be an option either to abandon this course. Liquidity support (if it must come to this) should only be provided in isolated cases.

ECB balance sheet: TLTRO, APP and PEPP

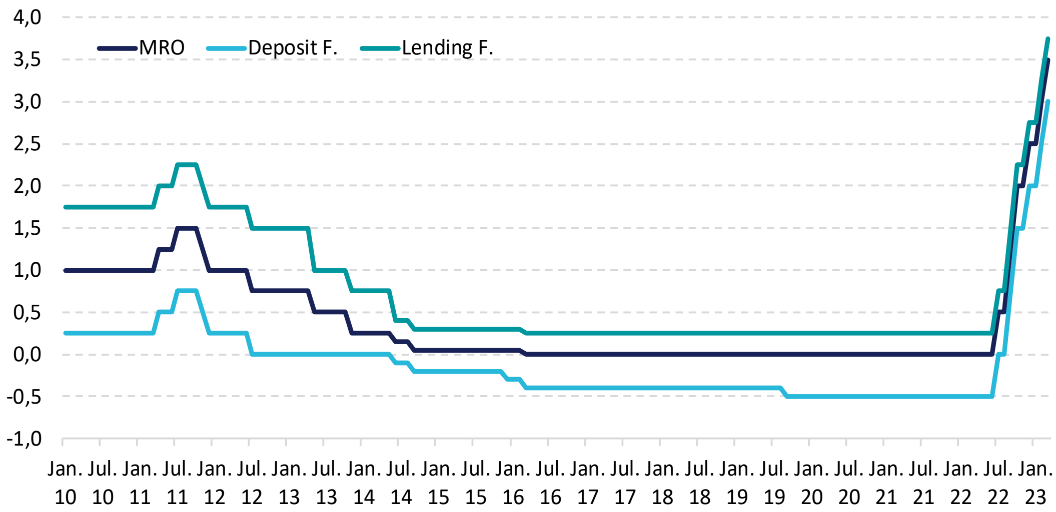


ECB share of the covered bond market



Source: ECB, Moody's, Bloomberg, NORD/LB Markets Strategy & Floor Research

ECB key interest rates (in %; incl. decision on interest rates on 16 March 2023)



Source: ECB, Bloomberg, NORD/LB Markets Strategy & Floor Research

A new world for interest rates: what might this mean for covered bonds?

In addition to the market-related shift on the covered bond market, which was triggered by the change of course in monetary policy and which has been expressed so far by a reduction in demand from the ECB and an increase in the supply of covered bonds, respectively, attention must be focused on possible fundamental changes. Within our ECB Preview, we had already discussed the fact that the "soft landing" scenario for economic activity, generally allows central banks to adopt a "more hawkish" course (cf. "ECB Preview – soft landing lets ECB play hard ball with key rates"). Fundamental factors that are of relevance for the covered bond market actually include the economic situation of the relevant economies. For example, the employment market is paramount for us with regard to the mortgage loans in the cover pools being serviced without any problems. Not only because of the soft landing for economic activity signalled by the ECB's forecasts, we continue to view the crisis scenario of a dramatic rise in unemployment as extremely unlikely. However, in actual fact, the interest rate reversal is affecting the covered bond market through another means. High interest rates are ultimately thwarting new property financing business more and more. This inertia affecting new loan production will also affect cover pools in future and could, in our opinion, markedly curb future issuance potential on the covered bond market moving forwards. The link between interest rates and loan volume should materialise to varying degrees of intensity in the covered bond jurisdictions covered by us. Accordingly, reactions are likely to be faster in countries where the majority of loans are agreed at variable rates – including premature repayments – while jurisdictions where the majority of interest rates are fixed over several years are likely to be characterised by a "welcome" rigidity. On balance, we certainly also see the possibility of weaker issuance years even for EUR benchmarks, but this is a topic for subsequent years. In 2023, issuers are still likely to have a sufficient amount of cover assets and can in part still have significant recourse to cover assets that are being released as soon as the "own use" covered bonds are repaid.

Conclusion and outlook

As is the case for other sub-markets, the assessment of the situation on the covered bond market definitely requires an adjustment in the wake of recent developments. General uncer-tainty must be taken into consideration just as much as the specific concerns about the bank-ing sector. On top of this, there is the course already adopted by the ECB with regard to the interest rate turnaround but also the reduction in its own balance sheet. In our opinion, the credit quality of the covered bond asset class is not threatened even in the current market environment. In this respect, the fact that the ECB's Governing Council is maintaining its course is definitely to be welcomed. More clarity must now be provided with regard to the specific features of its withdrawal from securities purchases under the APP or CBPP3. In this context, we would assign less event risk to repayments of the TLTRO III tenders, although in the current market landscape the refinancing of the tender volumes could become a more major challenge for some banks. In our opinion, the fact that, as a funding tool, covered bonds allow market access in periods of crisis even in phases of increased uncertainty or volatility should provide support here. While the general level of interest rates is generally depressing new property financing business and loan volumes – and consequently the supply of assets as a whole – the "soft landing" scenario and the more than just robust situation on the labour market suggest that the credit quality of cover assets will remain strong. From the perspective of the covered bond market, the ECB should, in our opinion, stick to its course. In this context, we are thinking first of the TLTRO III tenders and the APP. With regard to fur-ther possible rate hikes, we would, however, finally like to see a more pronounced integrity with respect to the meeting-by-meeting approach and consequently a move away from pre-determination. The current risk situation could in extremis also make the previously men-tioned "liquidity support" a necessity in the single currency area. However, this must still be deployed and understood as emergency measures for isolated cases.

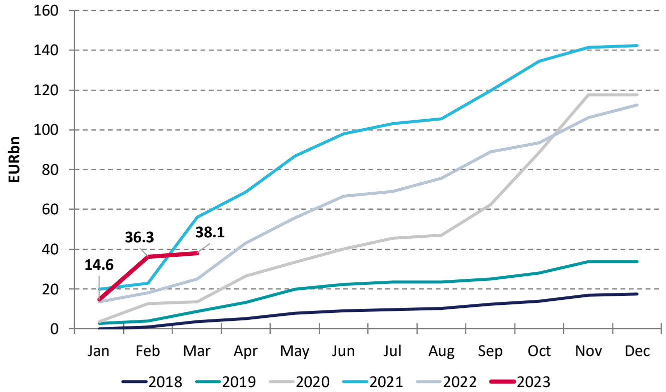
SSA/Public Issuers
ESG: EUR-benchmarks 2023 in the SSA segment (ytd)

Authors: Dr Norman Rudschuck, CIIA // Jan-Phillipp Hensing

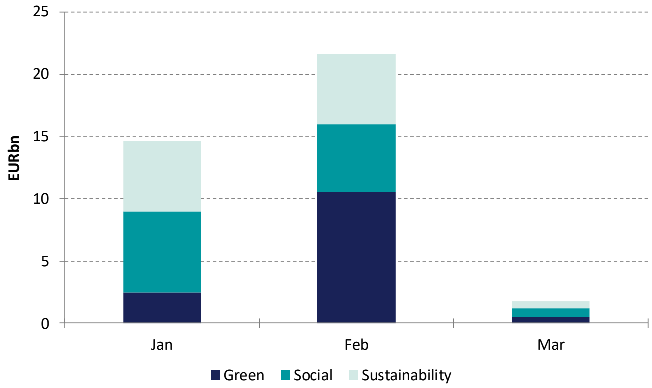
Introduction

As was the case last year, we are again focusing on the ESG segment over the course of the year to date in the SSA segment (as we define it - i.e., excluding sovereigns) as part of this publication. We published a report relating to the global ESG bond market in March 2022 (cf. NORD/LB Fixed Income Special – ESG Update; an update for this year is also planned). The data that forms the basis for this issue come from our in-house database in which we record each new EUR BMK issue from the SSA segment. To identify ESG bonds, we have recourse to data fields supplied by the financial data provider Bloomberg, which also allow us to make a distinction between green, social and sustainability bonds. As at the reference date of 21 March 2023, we recorded a figure of EUR 38.1bn for EUR BMK issues of an ESG nature since the beginning of the year. If this figure is compared with issuance trends from previous years, it is admittedly below the previous record year of 2021, but well above the years 2017 to 2020 and 2022. There was one reason for the record year in 2021: the European Union alone issued EUR 46.1bn worth of social bonds under the SURE programme between February and May. With the help of the programme, EU Member States received financial support to cope with the social and civic consequences of the coronavirus pandemic (such as by financing short time working programmes). At the end of 2022, the ESG volume issued stood at a level of EUR 112.6bn, while in the record year of 2021 the figure at year-end came in at EUR 142.3bn. Compared with 2019 (EUR 33.7bn), 2022 represents more than a tripling of the amount issued, which illustrates the significance and relevance of the ESG segment both for issuers and investors. In this year, February especially set a very high bar: at EUR 21.7bn, the issuance volume of ESG bonds was more than twice as high as the second strongest February in 2020 (EUR 9.0bn). In total, 15 new ESG issues were placed, of which CADES carried out the largest in terms of volume (EUR 4bn). The proceeds of this deal are to be used for social purposes in line with the issuer's role.

Primary market: EUR ESG BMK issuance trajectory

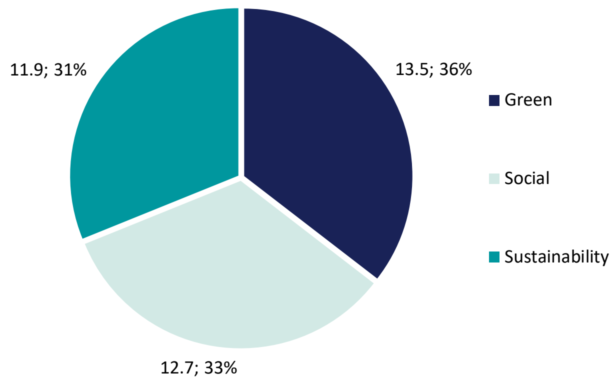


Primary market: EUR ESG BMK issues in 2023

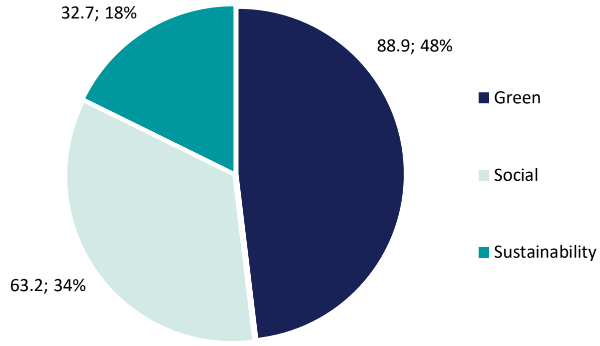


Source: Bloomberg, NORD/LB Markets Strategy & Floor Research

Breakdown by ESG category (ytd; EURbn)



Order books by ESG category (ytd; EURbn)



Source: Bloomberg, NORD/LB Markets Strategy & Floor Research

Balanced distribution of volume, green bonds boast highest order books

It is worth taking a look at the ESG issuance volumes to date in greater detail: of the volume of EUR 38.1bn issued up to 21 March, the proportion of green bonds amounted to 36% or EUR 13.5bn, while social bonds accounted for a slightly smaller share of 33% (EUR 12.7bn). Sustainability bonds amounted to EUR 11.9bn (31%) to date. Over the course of the year, green bonds are therefore slightly ahead at present, but the issuance dynamics are such that shifts at the top are possible at any time. With regard to issuers, CADES stands out in the social segment; it has issued EUR 9bn worth of new social bonds since the beginning of the year and therefore accounts for over 70% of the social segment. If one looks at demand in the form of aggregate order books, however, a markedly different picture emerges. In this context, green bonds come first, at EUR 88.9bn (48%), followed by social bonds (EUR 63.2bn). To date, sustainability bonds have achieved an aggregate volume of EUR 32.7bn (18%). However, we should not forget to point out that the comparison of order books is of course also driven by ratings and the general popularity of the issuers and is therefore difficult to assess. The substantial aggregate order book volume of green bonds is, for example, largely attributable to two issues: both KfW and the EIB, which in any case have the capacity to generate substantial oversubscription rates for bonds without ESG characteristics, each issued a green bond where the order books totalled EUR 34bn and EUR 30.5bn respectively. The situation is similar for social bonds: of the aggregate EUR 63.2bn under consideration, EUR 57bn ended up in the books of the two CADES transactions.

EU as a mega issuer of green and social bonds

We would like to deal with the European Union separately as an ESG issuer. Social bonds worth EUR 98.4bn were issued under the SURE programme, which was capped at EUR 100bn, until the programme ended in 2022. The situation is different for the NextGenerationEU (NGEU) programme. Up to the end of 2026, the EU plans an average annual funding target of EUR 150bn under this programme, which has a total volume of over EUR 800bn. The intention is to raise around 30% of the funding using green bonds (up to EUR 250bn in total). This would make the EU the world's largest green bond issuer. So far this year, the European Union has not issued a green bond – so there is certainly still upside potential here!

Overview of the top 10 benchmark issuers by ESG category and EUR volume (ytd)

Issuer	Green (EURbn)	Issuer	Social (EURbn)	Issuer	Sustainability (EURbn)
EIB	5.0	CADES	9.0	IBRD	3.0
KFW	3.0	BNG	1.5	AGFRNC	1.5
KUNTA	1.0	WALLOO	1.5	AIIB	1.5
SOGRPR	1.0	LCFB	0.7	ALSFR	1.2
IDFMOB	1.0			MADRID	1.0
NIB	0.5			BERGER	0.8
CDEP	0.5			BASQUE	0.7
JFM	0.5			ANDAL	0.6
KOMINS	0.5			IDF	0.6
ICO	0.5			NEDWBK	0.5

Source: Bloomberg, NORD/LB Markets Strategy & Floor Research

Taps of previously issued ESG bonds: nothing to report

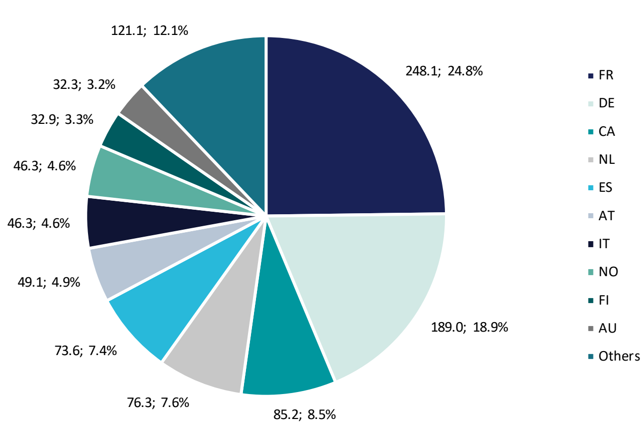
Taps are not included in the data up to now since we consciously differentiate between new issues and taps. But even if we did consider taps, this would not lead to any difference: of the 14 taps carried out to date in the SSA universe that we cover, none related to ESG bonds.

Conclusion and outlook

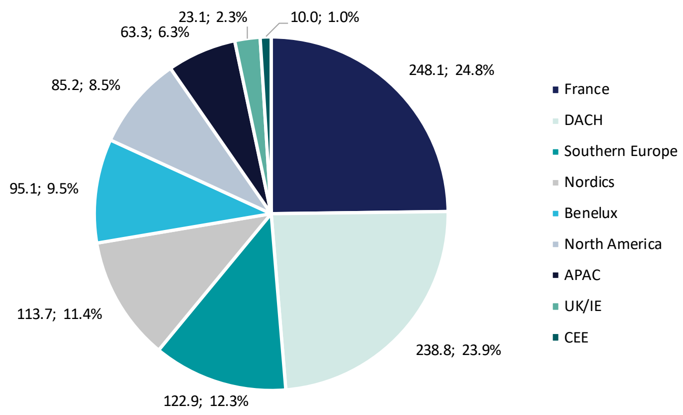
ESG bonds in the SSA segment as we define it are still heavily driven by individual issuers, although the number increases year by year. In our opinion, there is still upside potential here as far as the diversity of EUR issues is concerned, since it is not even possible, for example, to produce a list of the top 10 social bond issuers to date in 2023 yet. Nonetheless, the volume to date is impressive although we doubt whether it can exceed the record year of 2021. The SURE issues were too large, even if the EU's self-imposed 30% quota for green bonds in the NGEU funding volume was complied with, this would account for EUR 45bn with an average annual funding target of EUR 150bn. Something very surprising would have to occur to outdo 2021. However, considered over the years, we assume that there will be a long-term increase in the proportion of ESG bonds in the funding of our SSA coverage. Environmental protection, sustainability and social added value are not merely highly relevant but are also popular with investors. But before we get carried away, we would also like to point out that an increase in the issuance of ESG bonds does not necessarily mean that more green, social or even sustainable projects will be carried out. Issuers would almost certainly have carried these out even without an ESG label for their funding, as was the case for CADES. However, by implication this also means that issuers that have not issued ESG bonds to date can also promote social and sustainable projects and doubtless carry them out too. Especially for smaller issuers, the high reporting requirements continue to be a challenge. We therefore welcome the fact that a fourth German Bundesland, namely Berlin, has developed an ESG framework and several German regional promotional banks joined forces for the first time under the ticker LFIESG in 2022.

Charts & Figures
Covered Bonds

EUR benchmark volume by country (in EURbn)



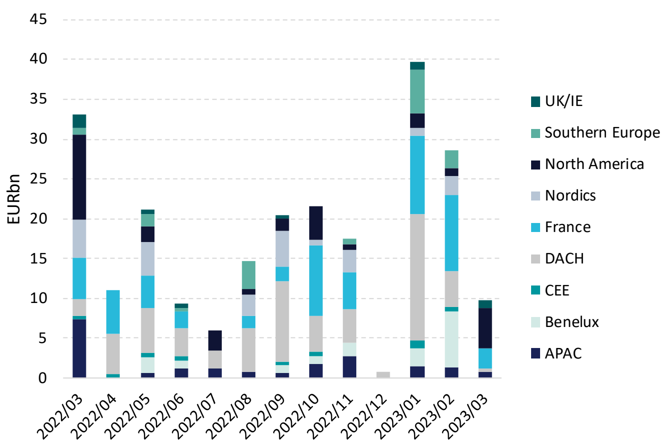
EUR benchmark volume by region (in EURbn)



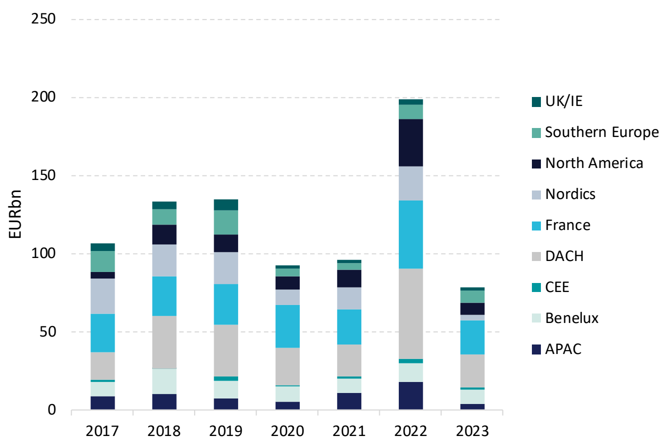
Top-10 jurisdictions

Rank	Country	Amount outst. (EURbn)	No. of BMKs	There of ESG BMKs	Avg. issue size (EURbn)	Avg. initial maturity (in years)	Avg. mod. Duration (in years)	Avg. coupon (in %)
1	FR	248.1	239	16	0.96	9.6	5.3	1.12
2	DE	189.0	270	31	0.65	8.1	4.3	0.88
3	CA	85.2	64	0	1.30	5.6	2.9	0.74
4	NL	76.3	76	2	0.94	10.9	6.7	0.98
5	ES	73.6	59	6	1.14	11.1	3.8	1.93
6	AT	49.1	84	4	0.58	8.7	5.4	1.09
7	IT	46.3	57	2	0.79	9.2	3.6	1.24
8	NO	46.3	55	11	0.84	7.3	3.8	0.51
9	FI	32.9	35	3	0.93	7.4	3.8	0.90
10	AU	32.3	32	0	1.01	7.6	3.8	1.19

EUR benchmark issue volume by month

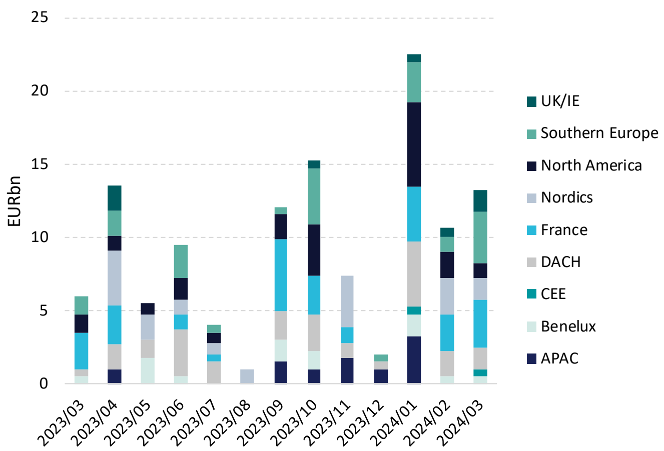


EUR benchmark issue volume by year

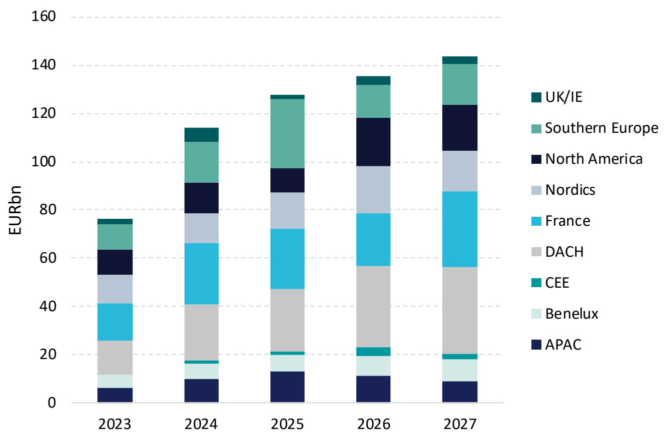


Source: market data, Bloomberg, NORD/LB Markets Strategy & Floor Research

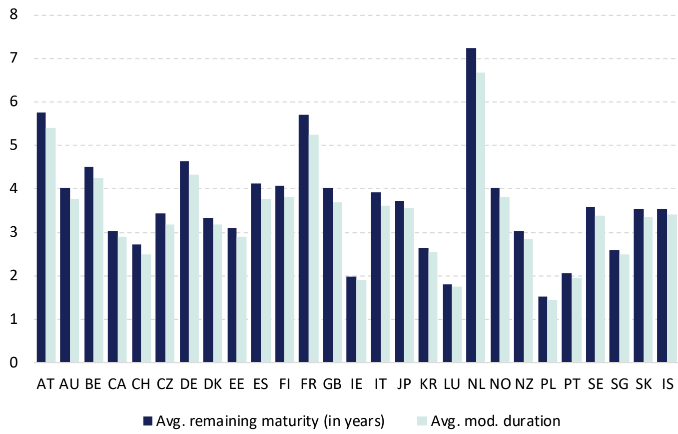
EUR benchmark maturities by month



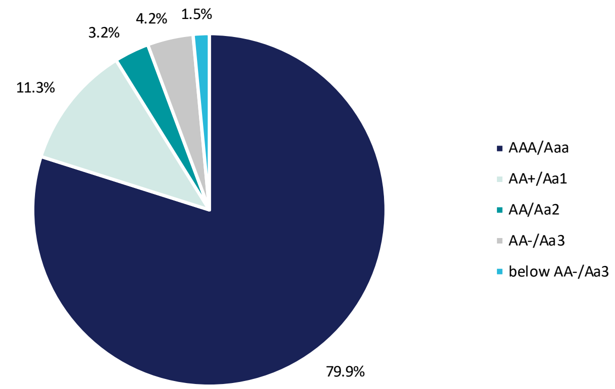
EUR benchmark maturities by year



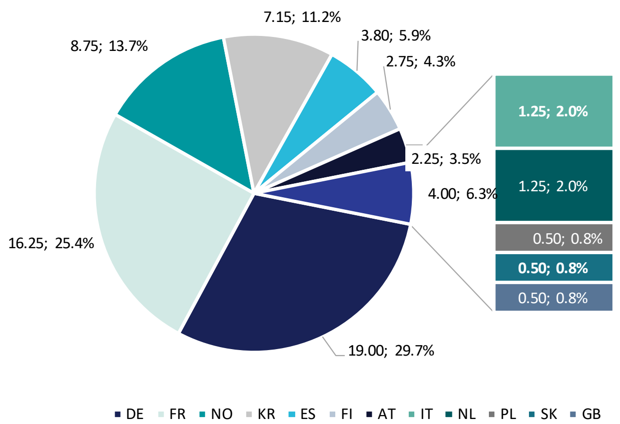
Modified duration and time to maturity by country



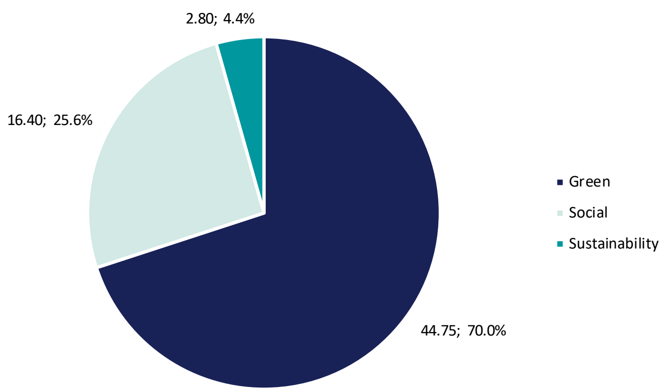
Rating distribution (volume weighted)



EUR benchmark volume (ESG) by country (in EURbn)



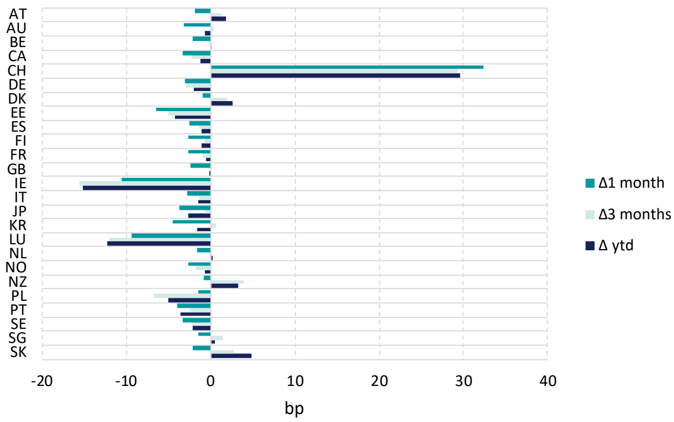
EUR benchmark volume (ESG) by type (in EURbn)



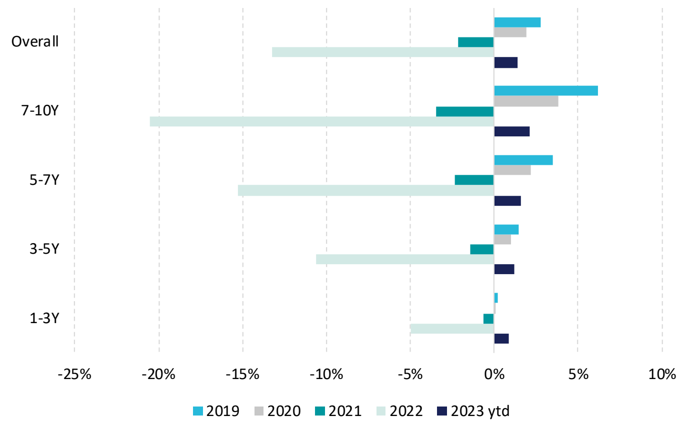
Source: market data, Bloomberg, NORD/LB Markets Strategy & Floor Research

NORD/LB

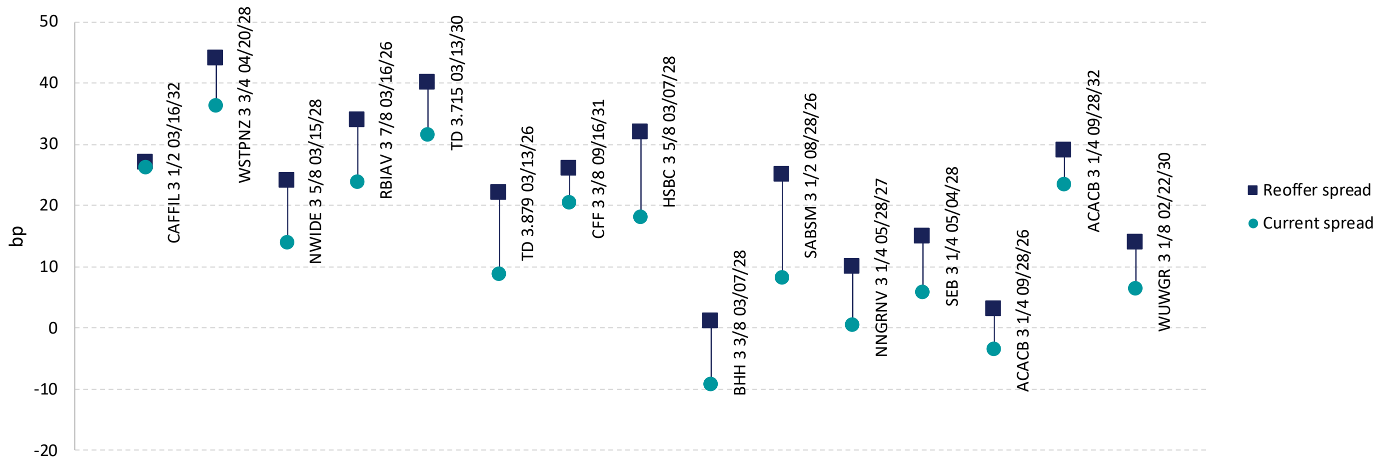
Spread development by country



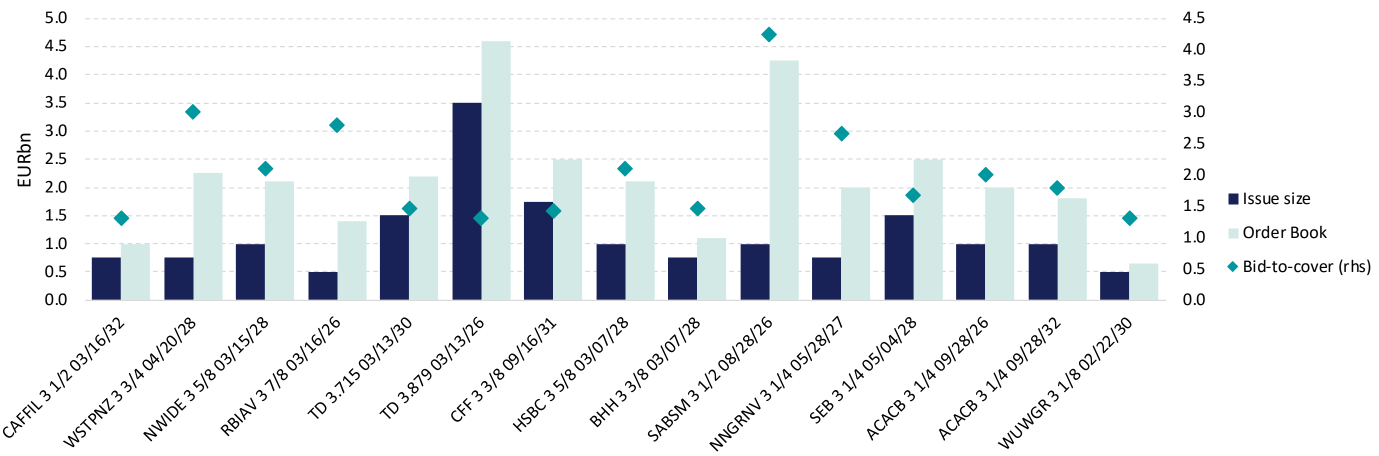
Covered bond performance (Total return)



Spread development (last 15 issues)



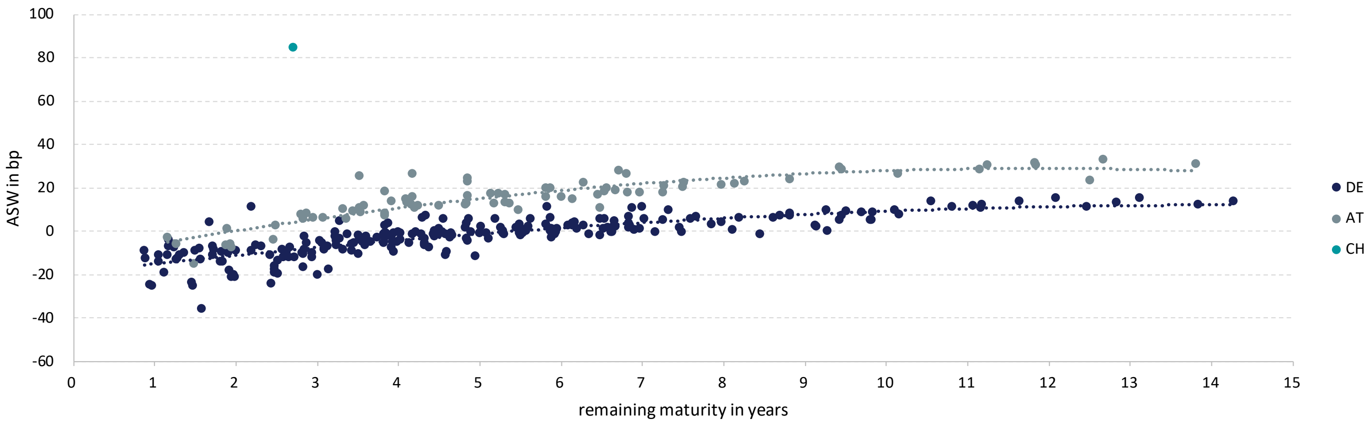
Order books (last 15 issues)



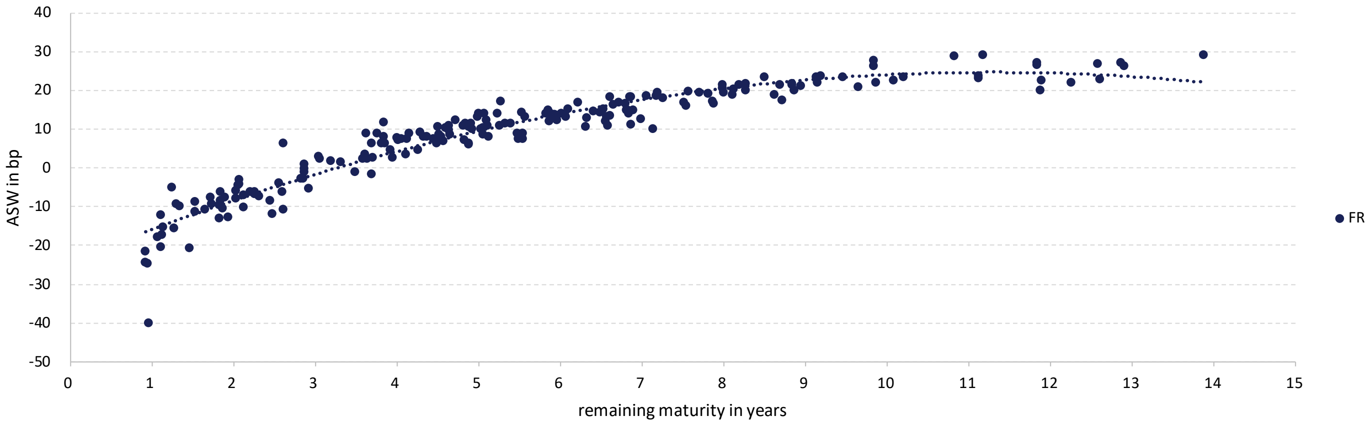
Source: market data, Bloomberg, NORD/LB Markets Strategy & Floor Research

Spread overview[1]

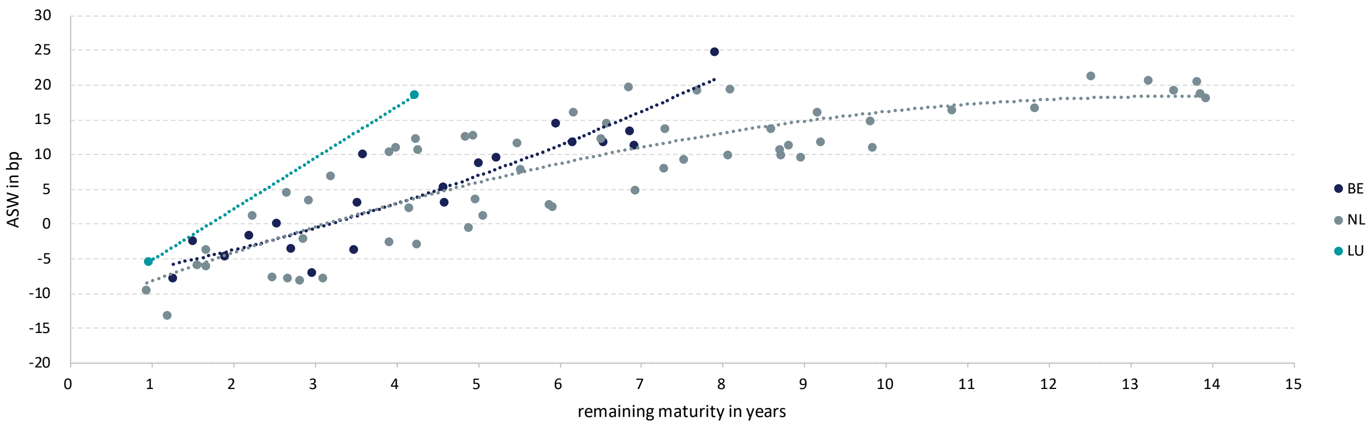
DACH



France

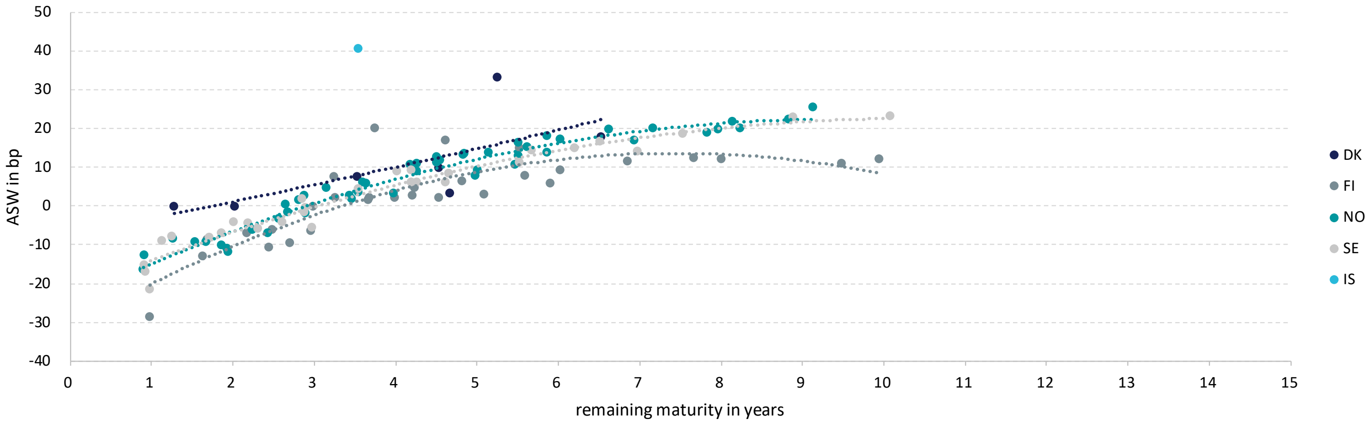


Benelux

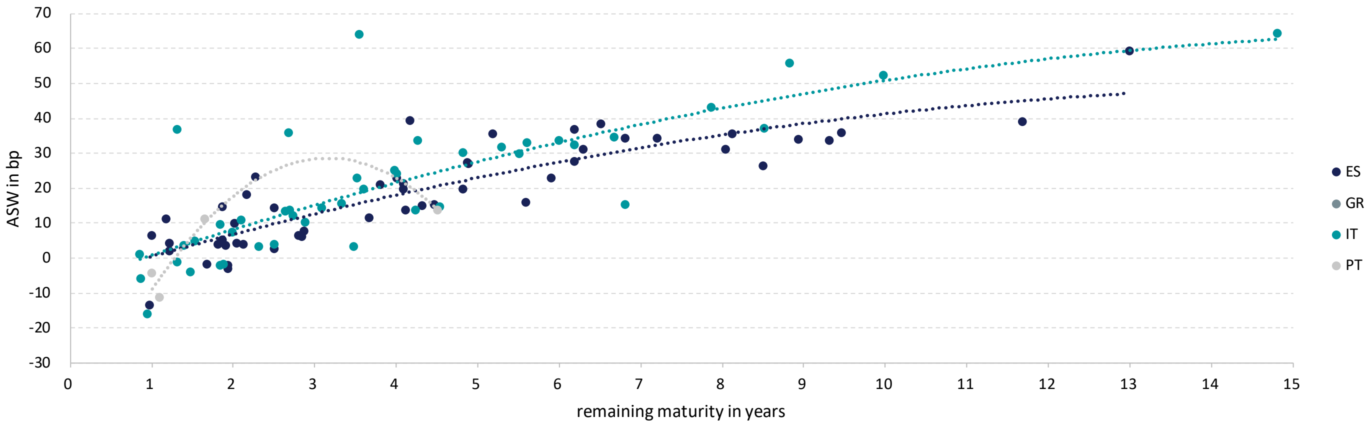


Source: market data, Bloomberg, NORD/LB Markets Strategy & Floor Research [1]Time to maturity 1 ≤ y ≤ 15

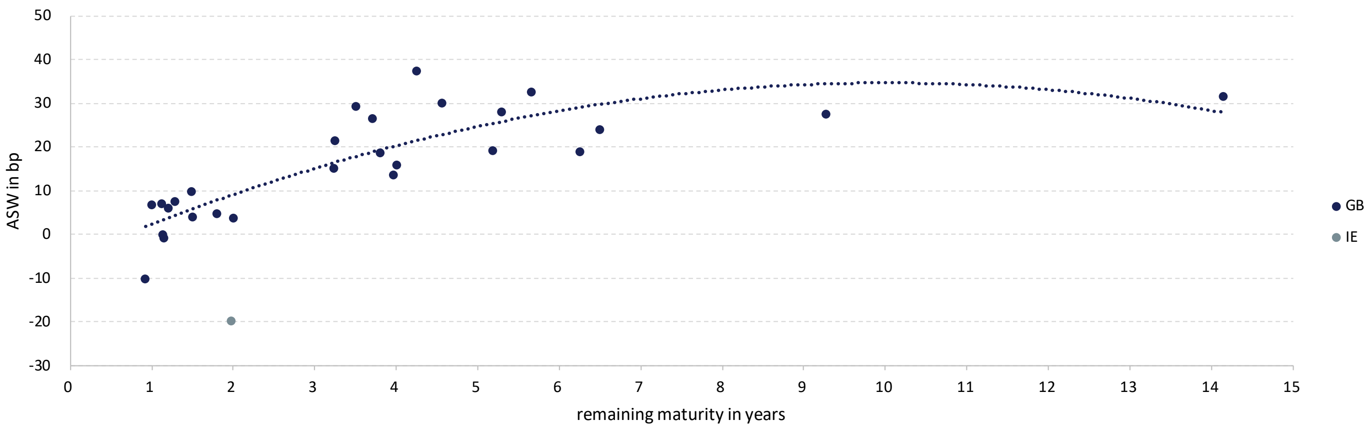
Nordics



Southern Europe

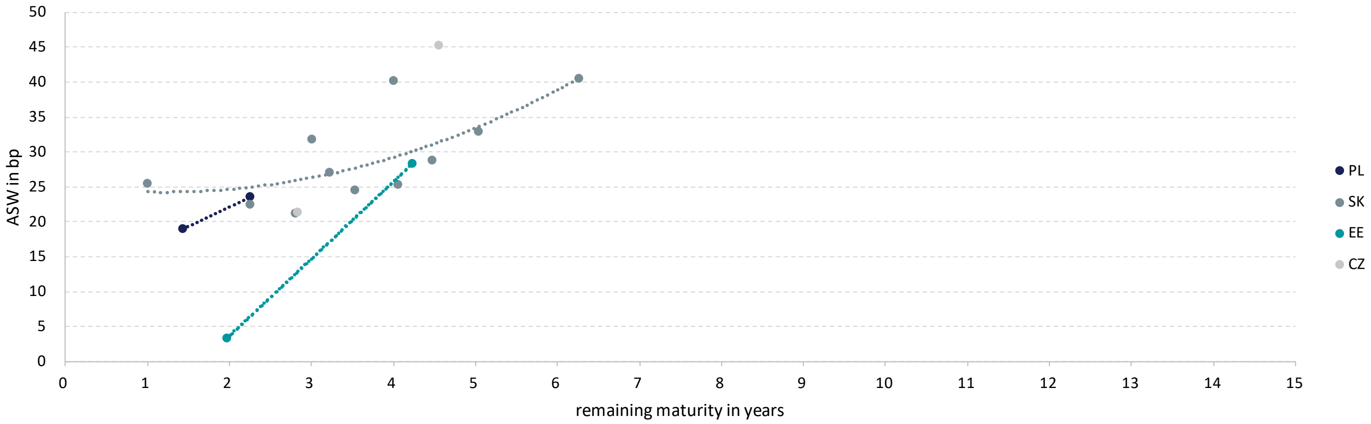


UK/IE

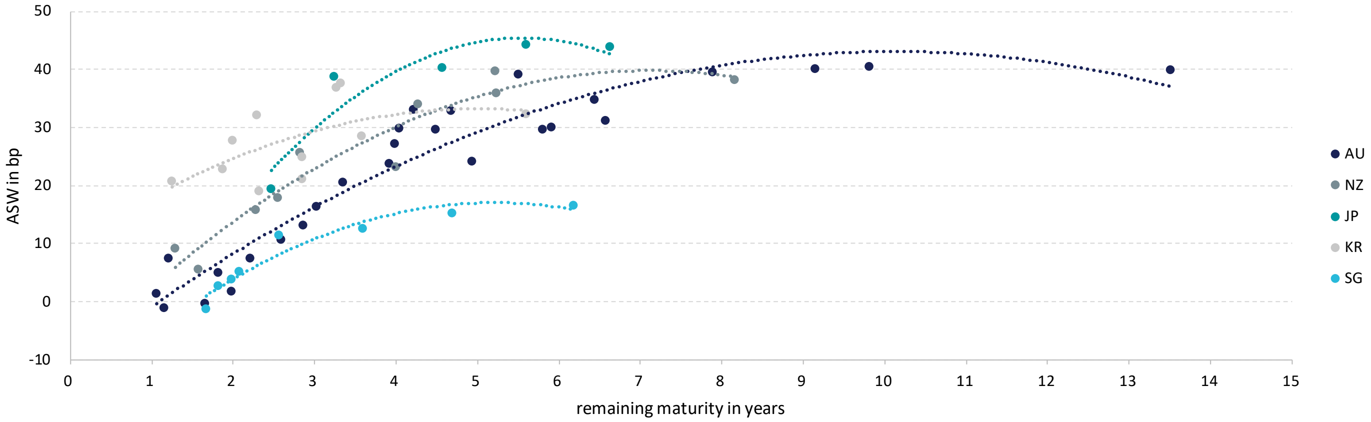


Source: market data, Bloomberg, NORD/LB Markets Strategy & Floor Research

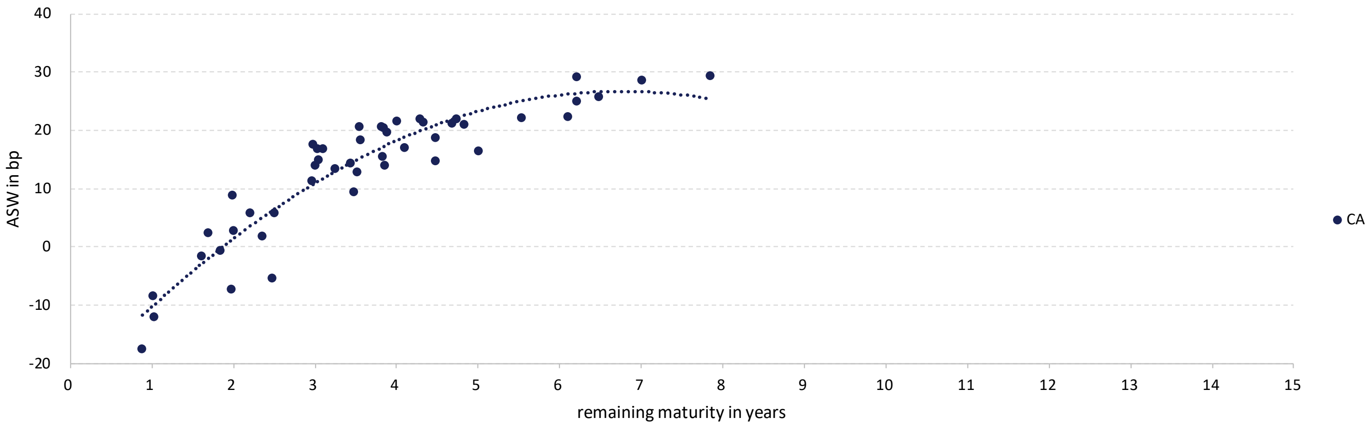
CEE



APAC



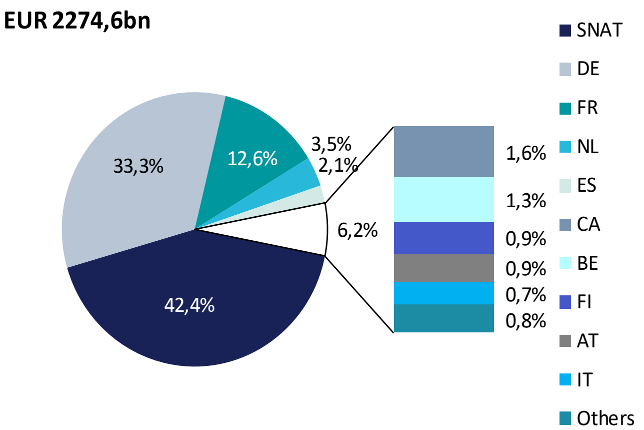
North America



Source: market data, Bloomberg, NORD/LB Markets Strategy & Floor Research

Charts & Figures
SSA/Public Issuers

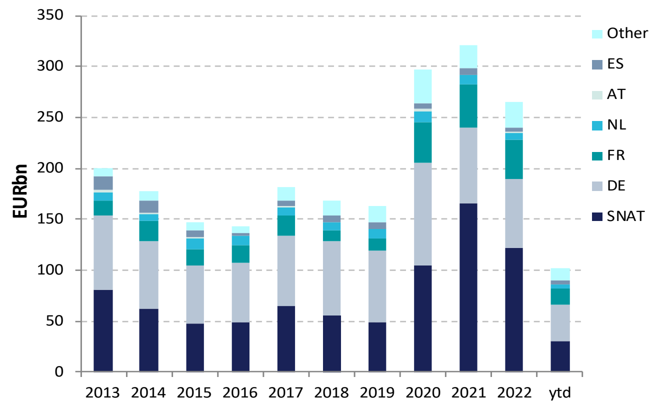
Outstanding volume (bmk)



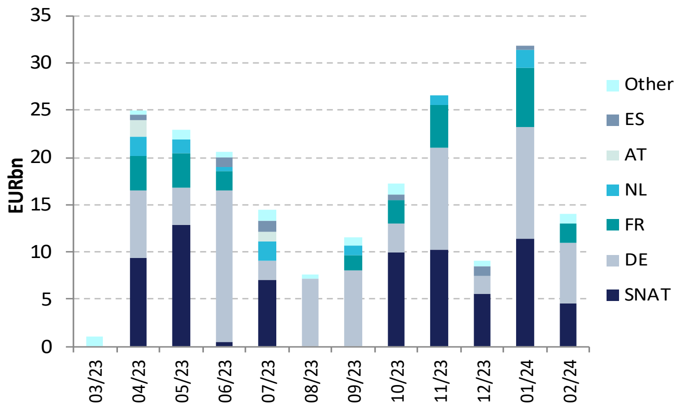
Top 10 countries (bmk)

Country	Vol. (€bn)	No. of bonds	ØVol. (€bn)	Vol. weight. ØMod. Dur.
SNAT	964,1	225	4,3	8,1
DE	756,7	564	1,3	6,4
FR	285,9	188	1,5	6,2
NL	79,5	70	1,1	6,5
ES	47,4	64	0,7	4,8
CA	35,5	25	1,4	4,5
BE	30,2	34	0,9	11,5
FI	21,4	24	0,9	5,2
AT	19,6	22	0,9	4,3
IT	15,5	20	0,8	4,7

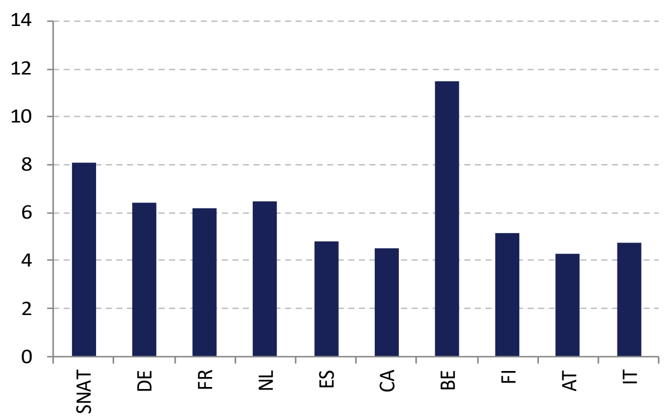
Issue volume by year (bmk)



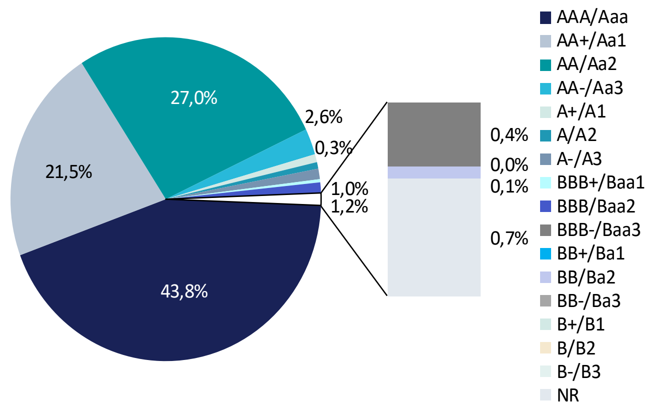
Maturities next 12 months (bmk)



Avg. mod. duration by country (vol. weighted)



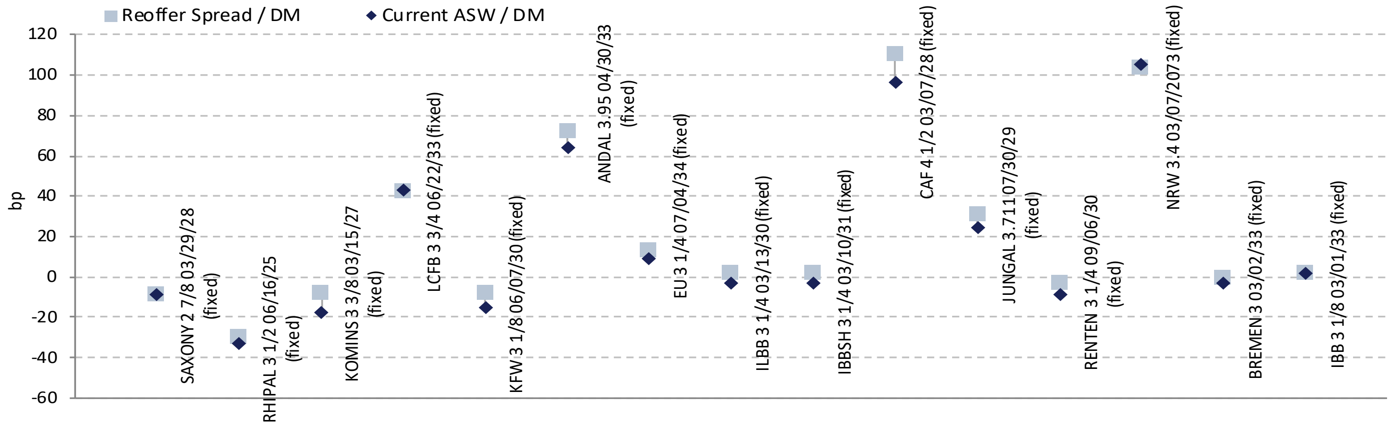
Rating distribution (vol. weighted)



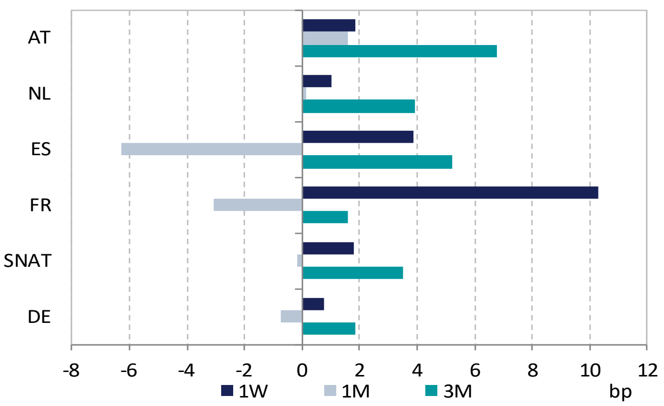
Source: Bloomberg, NORD/LB Markets Strategy & Floor Research

NORD/LB

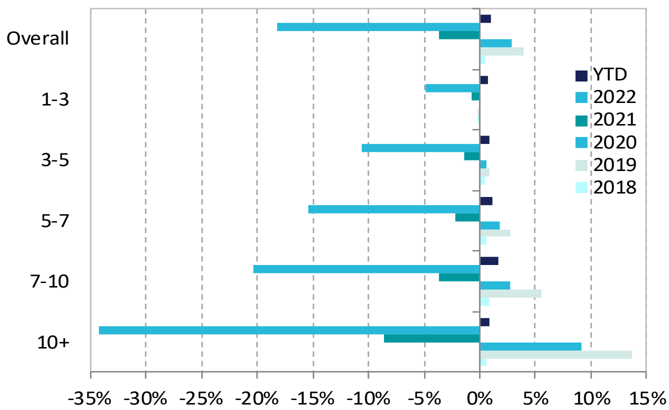
Spread development (last 15 issues)



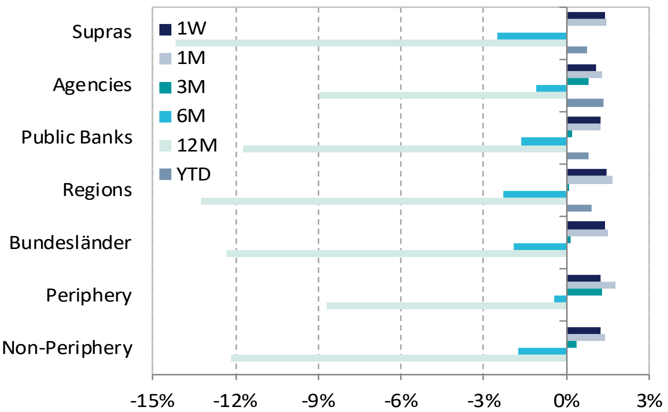
Spread development by country



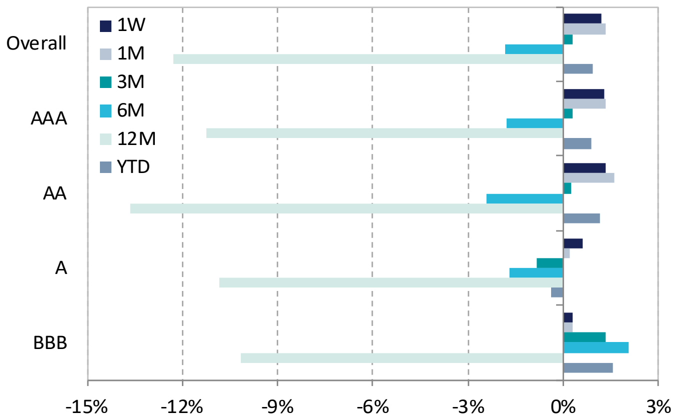
Performance (total return)



Performance (total return) by segments

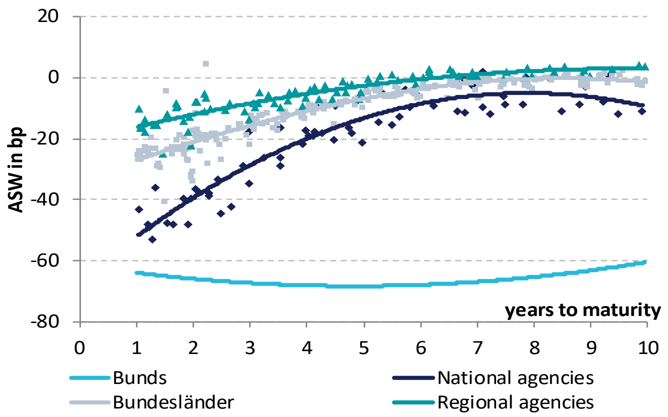


Performance (total return) by rating

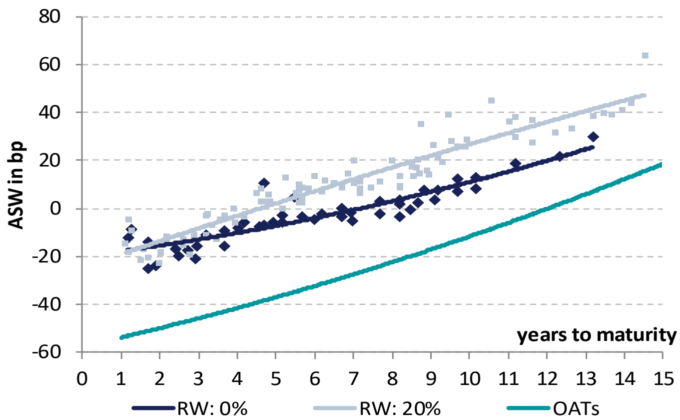


Source: Bloomberg, NORD/LB Markets Strategy & Floor Research

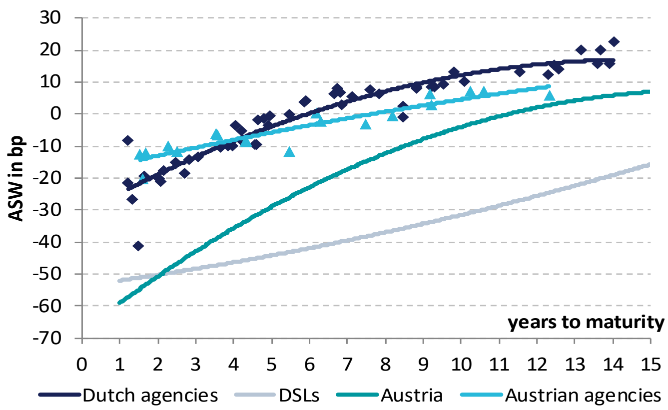
Germany (by segments)



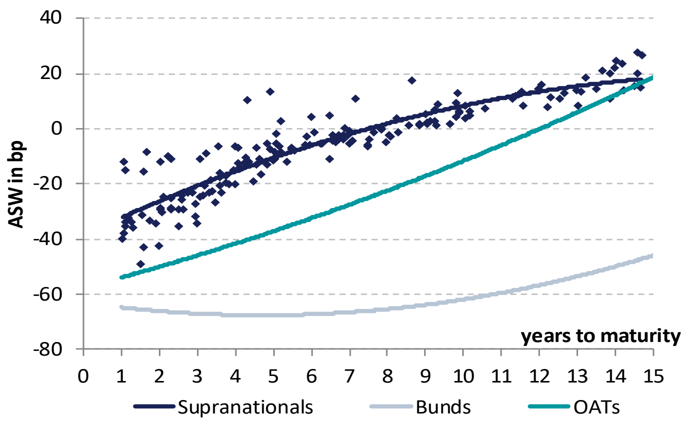
France (by risk weight)



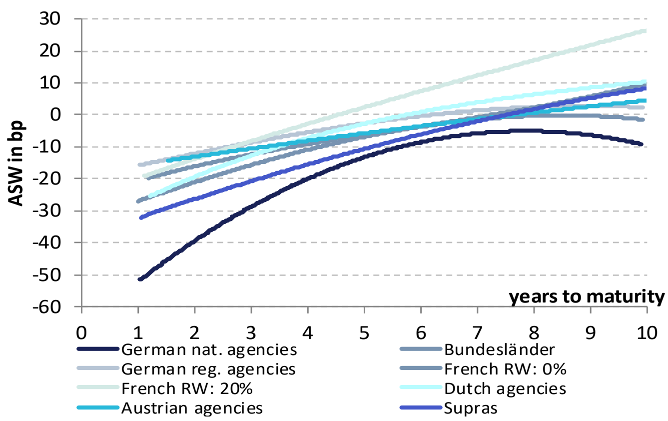
Netherlands & Austria



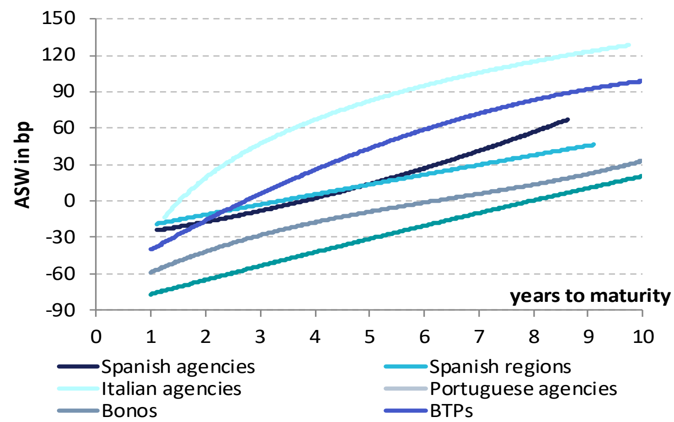
Supranationals



Core



Periphery



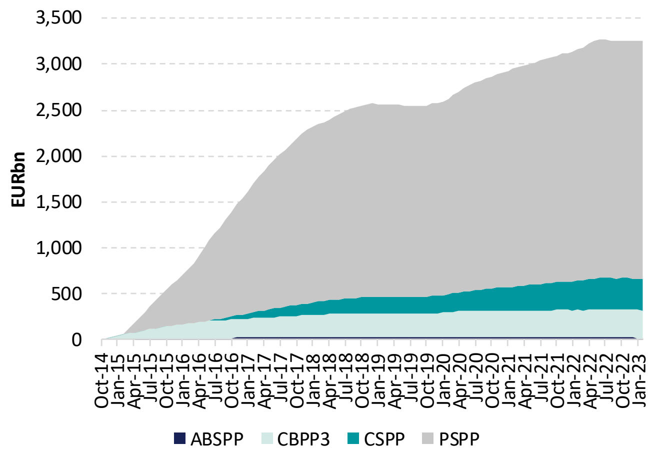
Source: Bloomberg, NORD/LB Markets Strategy & Floor Research

ECB tracker

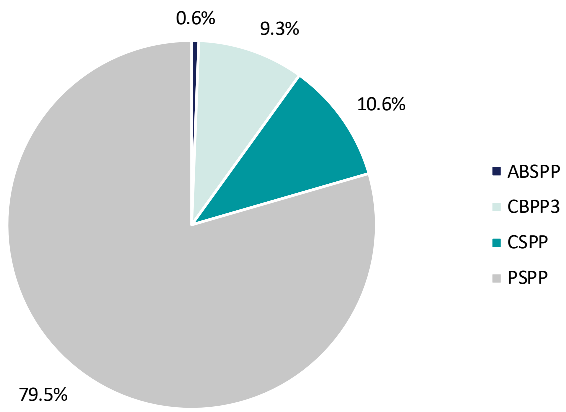
Asset Purchase Programme (APP)

	ABSPP	CBPP3	CSPP	PSPP	APP
Jan-23	20,829	303,269	344,010	2,584,798	3,252,906
Feb-23	20,191	302,677	344,102	2,584,935	3,251,905
Δ	-638	-592	+92	+137	-1,001

Portfolio development

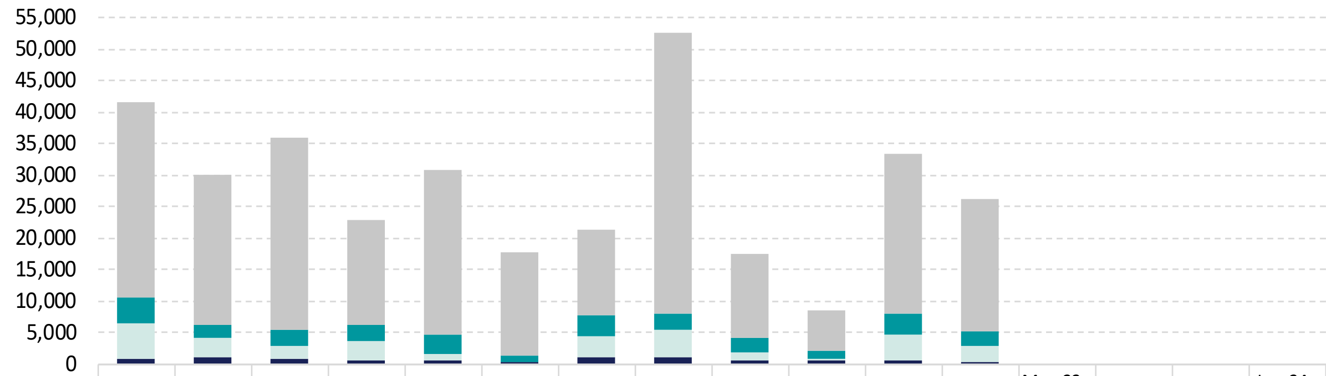


Portfolio structure



Source: ECB, NORD/LB Markets Strategy & Floor Research

Expected monthly redemptions (in EURm)

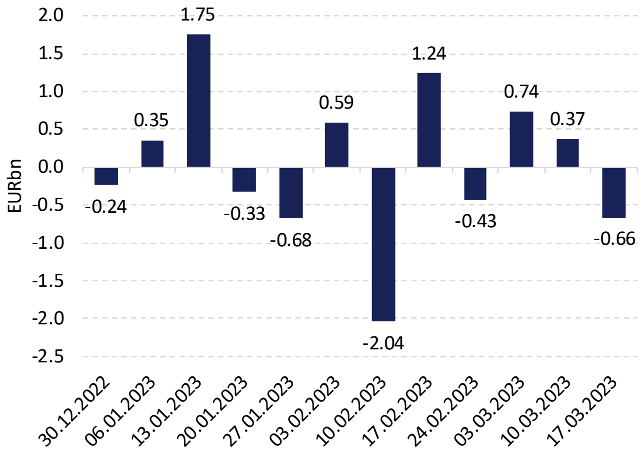


	Mar-23	Apr-23	May-23	Jun-23	Jul-23	Aug-23	Sep-23	Oct-23	Nov-23	Dec-23	Jan-24	Feb-24	Mar-23 - Feb-24	2022	2023	Jan-24 - Feb-24
APP	41,620	29,968	35,912	22,863	30,887	17,856	21,217	52,596	17,507	8,556	33,467	26,100	338,549	299,142	331,104	331,104
PSPP	31,061	23,858	30,558	16,619	26,130	16,445	13,351	44,559	13,255	6,336	25,524	21,013	268,709	228,585	255,266	255,266
CSPP	4,219	1,965	2,579	2,557	3,038	986	3,377	2,616	2,393	1,336	3,357	2,282	30,705	17,670	30,428	30,428
CBPP3	5,631	2,937	1,874	3,112	1,170	0	3,346	4,465	1,351	408	4,109	2,447	30,850	41,244	35,145	35,145
ABSPP	709	1,208	901	575	549	425	1,143	956	508	476	477	358	8,285	11,643	10,265	10,265

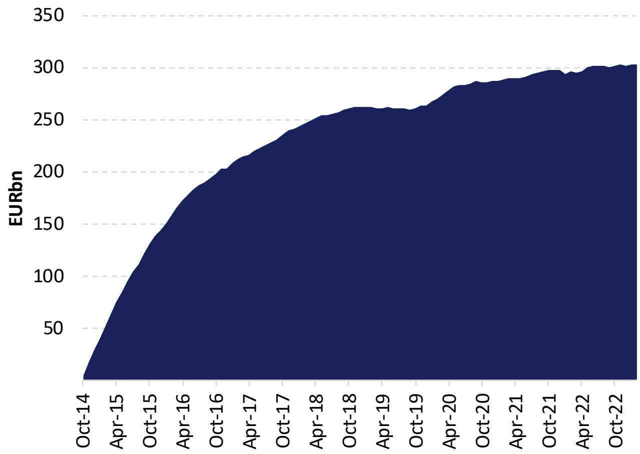
Source: ECB, Bloomberg, NORD/LB Markets Strategy & Floor Research

Covered Bond Purchase Programme 3 (CBPP3)

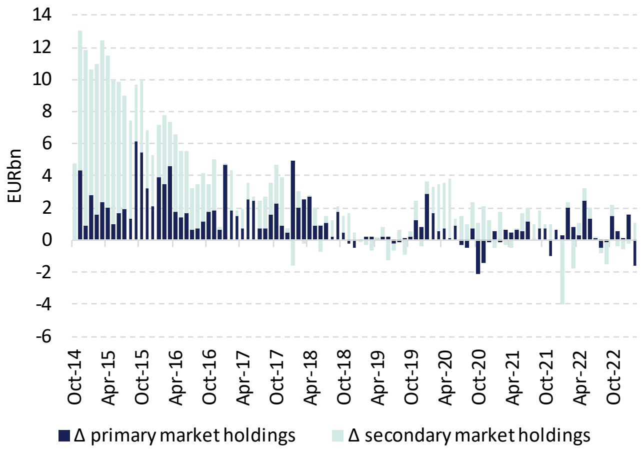
Weekly purchases



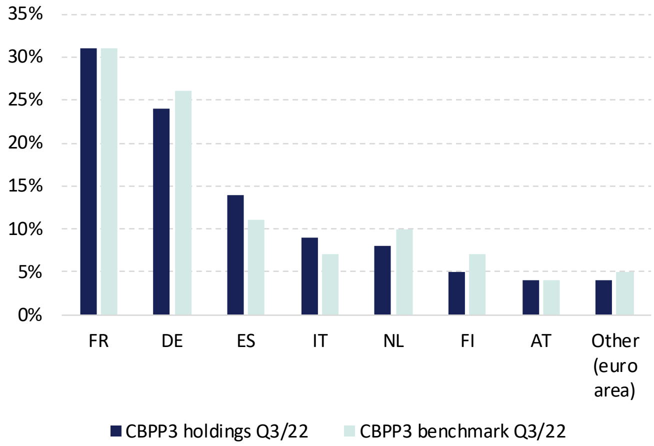
Development of CBPP3 volume



Change of primary and secondary market holdings

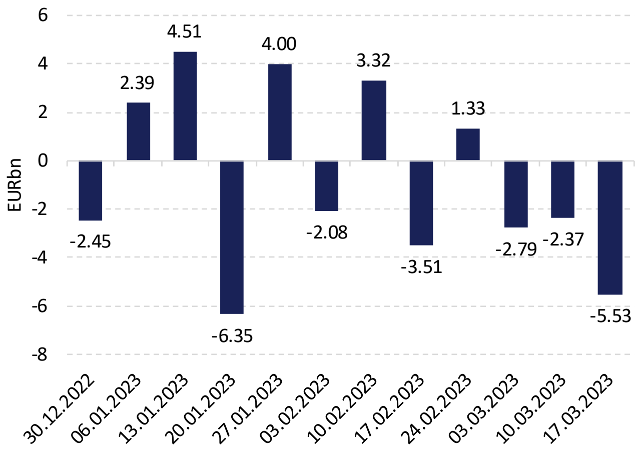


Distribution of CBPP3 by country of risk

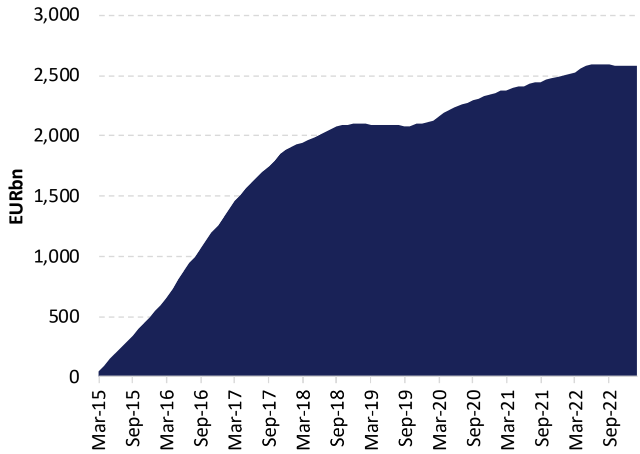


Public Sector Purchase Programme (PSPP)

Weekly purchases



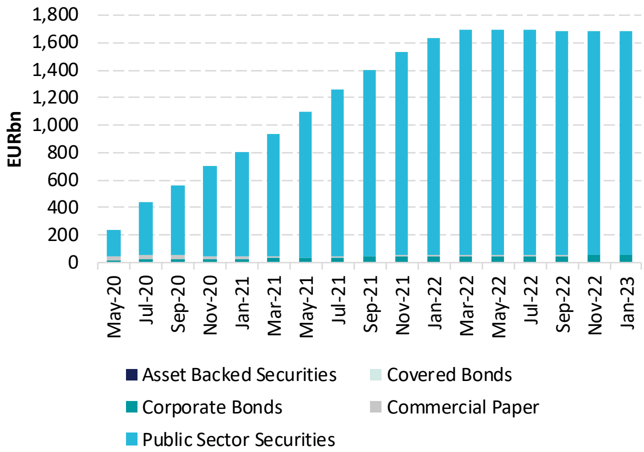
Development of PSPP volume



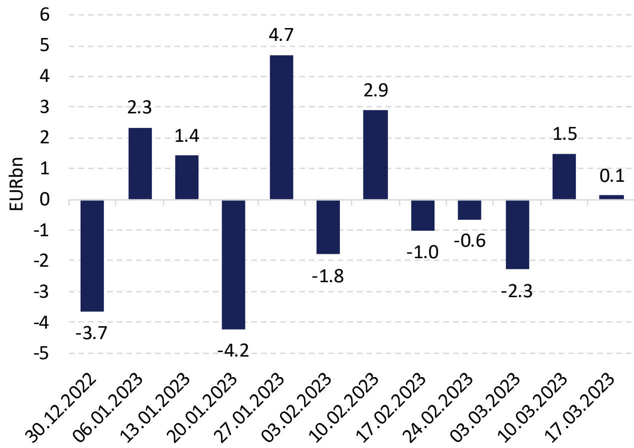
Source: ECB, Bloomberg, NORD/LB Markets Strategy & Floor Research

Pandemic Emergency Purchase Programme (PEPP)

Portfolio development



Weekly purchases



Breakdown of public sector securities under the PEPP

Jurisdiction	Holdings (in EURm)	Δ Holdings previous period	Adj. distribution key[1]	PEPP share	Deviations from the adj. distribution key[2]	Current WAM[3] (in years)	WAM of eligible universe[4] (in years)
AT	44,037	-671	2.6%	2.7%	0.0%	7.5	7.4
BE	55,795	-698	3.3%	3.4%	0.1%	6.3	9.3
CY	2,493	4	0.2%	0.2%	0.0%	8.3	8.1
DE	398,297	2,551	23.7%	24.0%	0.3%	6.7	6.9
EE	256	0	0.3%	0.0%	-0.2%	7.4	8.0
ES	193,376	-1,418	10.7%	11.6%	0.9%	7.4	7.3
FI	26,953	-173	1.7%	1.6%	0.0%	7.4	7.5
FR	301,844	14	18.4%	18.2%	-0.2%	7.6	7.8
GR	37,760	729	2.2%	2.3%	0.0%	8.5	9.4
IE	25,998	-503	1.5%	1.6%	0.0%	8.8	10.2
IT	287,658	-794	15.3%	17.3%	2.0%	7.2	6.9
LT	3,256	14	0.5%	0.2%	-0.3%	9.5	9.1
LU	1,922	19	0.3%	0.1%	-0.2%	5.9	6.5
LV	1,911	0	0.4%	0.1%	-0.2%	7.9	7.4
MT	607	1	0.1%	0.0%	-0.1%	10.4	8.6
NL	83,388	1,689	5.3%	5.0%	-0.3%	7.7	8.7
PT	33,909	-1,068	2.1%	2.0%	-0.1%	6.8	7.3
SI	6,627	19	0.4%	0.4%	0.0%	8.5	9.4
SK	8,031	0	1.0%	0.5%	-0.5%	8.1	8.2
SNAT	147,088	0	10.0%	8.9%	-1.1%	10.2	8.8
Total / Avg.	**1,661,205**	**-281**	**100.0%**	**100.0%**	**0.0%**	**7.5**	**7.6**

[1] Based on the ECB capital key, adjusted to include supras [2] Based on the adjusted distribution key
[3] Current WAM of public sector securities holdings under the PEPP [4] WAM of eligible universe of public sector securities holdings under the PEPP
Source: ECB, Bloomberg, NORD/LB Markets Strategy & Floor Research

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Appendix
Overview of latest Covered Bond & SSA View editions

Publication	Topics
10/2023 ♦ 15 March	▪ Transparency requirements §28 PfandBG Q4/2022 ▪ Credit authorisations of the German Laender for 2023
09/2023 ♦ 08 March	▪ ECB preview: Soft landing lets ECB play hard ball with key rates ▪ Where does the Pfandbrief stand within the covered bond universe?
08/2023 ♦ 01 March	▪ The covered bond market and the ECB: a gradual farewell? ▪ Beyond Bundeslaender: Focus on Greater Paris (IDF and VDP)
07/2023 ♦ 22 February	▪ The Italian market for EUR benchmark covered bonds ▪ European supranationals – an overview
06/2023 ♦ 15 February	▪ Maturity premiums on covered bonds ▪ Development of the German property market ▪ Spotlight on the EU: a mega issuer spawned by the crisis
05/2023 ♦ 08 February	▪ January 2023: record start to the new covered bond year ▪ SSA monthly review: dynamic issuance activity to kick off the new year
04/2023 ♦ 01 February	▪ Focus on covered bond jurisdictions: Canada in the spotlight ▪ Focus on covered bond jurisdictions: Slovakia and Czech Republic in the spotlight ▪ 26th meeting of the Stability Council (December 2022)
03/2023 ♦ 25 January	▪ ECB preview: all eyes and ears on the press conference ▪ Successful start to the year for EUR sub-benchmarks as well ▪ ESG covered bonds from France: La Banque Postale SFH issues inaugural social covered bond
02/2023 ♦ 18 January	▪ Focus on covered bond jurisdictions: Belgium in the spotlight ▪ The Moody's covered bond universe: an overview ▪ Beyond Bundeslaender: focus on Belgian issuers
01/2023 ♦ 11 January	▪ ECB review: 2022 entailed all manner of monetary policy action ▪ Covered Bonds Annual Review 2022 ▪ SSA: Annual review of 2022
39/2022 ♦ 14 December	▪ Our view of the covered bond market heading into 2023 ▪ SSA outlook 2023: ECB, NGEU and the debt brake in Germany
38/2022 ♦ 07 December	▪ ECB preview – next hike but total assets (finally) reduced?! ▪ Covered bond jurisdictions in the spotlight: a look at Spain
37/2022 ♦ 30 November	▪ Transparency requirements §28 PfandBG Q3 2022 ▪ ECB repo collateral rules and their implications for Supranationals & Agencies
36/2022 ♦ 23 November	▪ ESG covered bonds - another record year ▪ Current LCR classifications for our SSA coverage

NORD/LB: Markets Strategy & Floor Research

NORD/LB: Covered Bond Research

NORD/LB: SSA/Public Issuer Research

Bloomberg: RESP NRDR <GO>

Appendix
Publication overview

Covered Bonds:

Issuer Guide Covered Bonds 2022

Covered Bond Directive: Impact on risk weights and LCR levels

Risk weights and LCR levels of covered bonds (updated semi-annually)

Transparency requirements §28 PfandBG Q4/2022 (quarterly update)

Covered bonds as eligible collateral for central banks

SSA/Public Issuers:

Issuer Guide – German Laender 2022

Issuer Guide – German Agencies 2022

Issuer Guide – Dutch Agencies 2022

Beyond Bundeslaender: Belgium

Beyond Bundeslaender: Greater Paris (IDF/VDP)

Spotlight on Spanish regions (Update planned in 2023)

Fixed Income Specials:

ESG-Update 2022

ECB interest rate decision: Roadmap to QT

ECB: The Wishing-Table, the Gold-Ass, and the Cudgel in the Sack

ECB interest rate decision: delivered as expected?

ECB acts as the 'House of Hikes' – or: Winter is coming!

Appendix
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Time of going to press: Wednesday, 22 March 2023 (08:58)