European Banks – Quarterly ESG Update (3Q24)

- ESG volumes decelerate from record levels. Higher-for-long rates, uncertain operating environments, market volatility, political risk as well as payback for front-loading issuance all curtailed activity
- New SLB guidelines and structural improvements aim to mitigate shortcomings of the segment
- EU misses out on sovereign status for now, while ECB confirms steady decarbonisation of holdings
- Fewer debut ESG trades in primary market and previous front-loading hamper quarterly volumes
- Secondary market spreads widen late in 2Q24 in response to event risk. Higher volatility sees greeniums erode but risk indicators and spreads have largely recovered in the ensuing months

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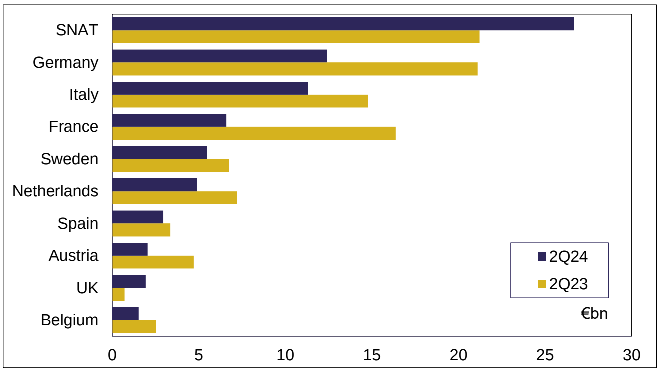
Overview: Deceleration in 2Q24 issuance activity may persists for the rest of the year

In 2Q24, global ESG bond issuance across all sectors – comprising green, social, sustainable and SLB bonds as well as ESG-labelled securitisations – fell to EUR273bn. This was 7.4% lower than the same period last year and only just above the 2Q22 level of EUR264bn. This reduction was in part due to issuers having front-loaded much of their funding requirements to earlier in the year, with ESG issuance in 1H24 still slightly up yoy. Nevertheless, volumes in 2Q24 were lower across most categories, notably SLBs (-32% yoy), social (-29% yoy), as well as green bonds (-3% yoy). Sustainability bonds, combining green and social elements, were the only labelled category that grew during the quarter (+11% yoy).

In Europe, ESG-linked bond sales from SSAs and FIGs reached EUR85bn in 2Q24 according to Bloomberg data, down 19% yoy. Of that total, green bond sales stood at EUR48bn (-27% yoy), sustainable bond volumes were EUR27bn (+29% yoy) and social bonds accounted for EUR10bn (-45% yoy). Entities from Germany, Italy, France and Sweden led European ESG debt issuance in 2Q24 alongside Supranationals. ESG-themed bonds issued by European financial institutions fell by EUR10bn from a year earlier to EUR23bn (-30% yoy). SSAs also experienced weaker activity as volumes declined by EUR10bn to EUR62bn (-14% yoy). Euro themed bond issuance by FIGs and SSAs accounted for 9.6% of the overall bond market volume (2Q23: 11%), down from the record level of 18.2% registered in 3Q22. The declining share of ESG stands in contrast to the expansion of the overall euro bond market that grew +4% yoy in 2Q24.

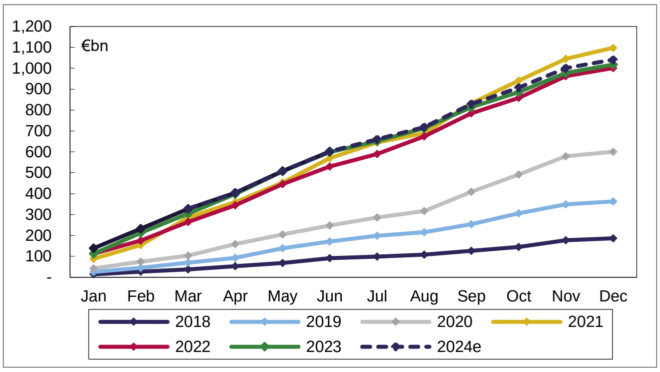
After the record quarterly volume registered in 1Q24, the drop-off from these levels in 2Q24 was unsurprising. Current amounts correspond more to the norm and are in line with averages observed over recent years. Looking ahead, events will likely put downward pressure on activity and volumes. The hoped-for quick series of interest rate cuts by major central banks has not yet materialised with policy remaining data dependent. Further, political headwinds from key events such as the U.S. election are mounting and have the potential to generate significant market volatility, as was the case of the French snap election in June and July. As many issuers are already well advanced in their funding programmes, we expect near-term activity to be more opportunistic in a bid to mitigate potential volatility and event risk.

European ESG Bond Issuance by Country



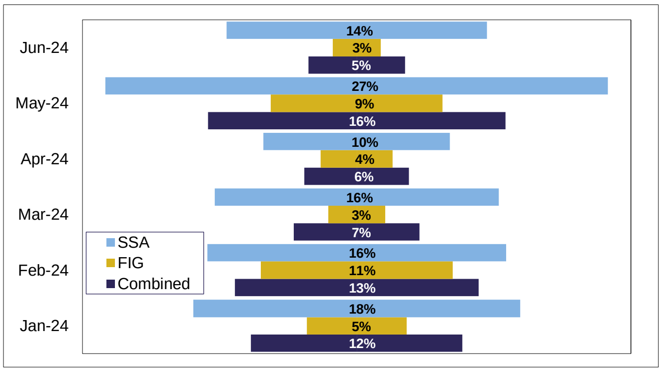
Source: Bloomberg; includes FIGs & SSAs; Daiwa Capital Markets Europe

Cumulative annual sustainable debt transactions*



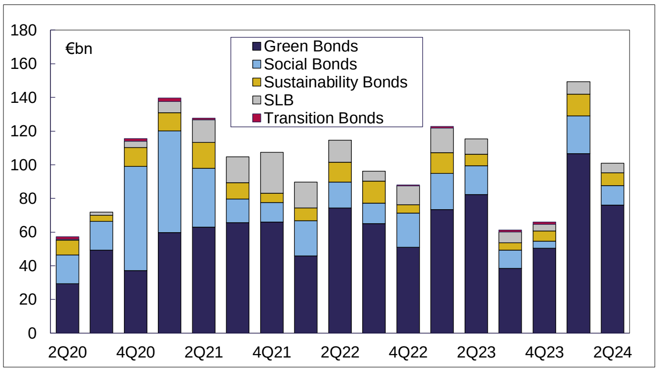
Source: Bloomberg; FIG, SSA & Corporates; *excl. green, social and sustainability-linked loans; Daiwa Capital Markets Europe

Proportion of ESG-themed debt to total issuance*



Source: Bloomberg; *EUR by European issuers; Daiwa Capital Markets Europe

Quarterly European ESG Bond Issuance by Type

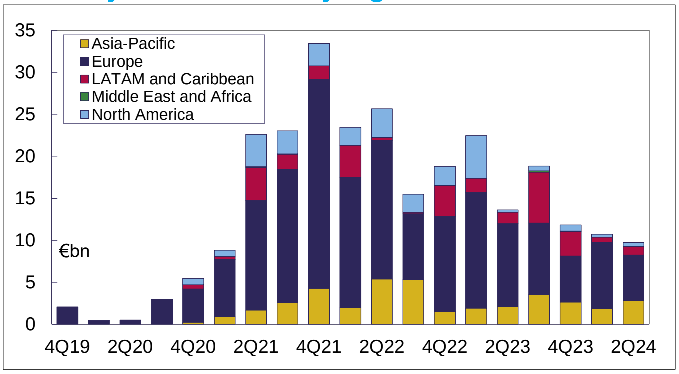


Source: Bloomberg; FIG, SSA & Corporates; Daiwa Capital Markets Europe

Structural changes to SLB market raise hopes of segment recovery in coming years

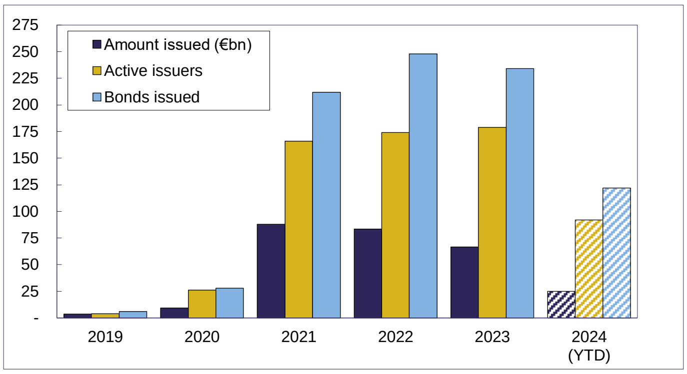
In the second quarter, global sustainability-linked bond (SLB) volumes dropped to EUR9.7bn, a 29% decline from last year, marking the lowest level since 1Q21. Volumes have been dwindling for a number of quarters for several reasons. Investors have raised concerns for some time about unambitious sustainability targets underpinning issuer key performance indicators (KPI), thus limiting the incentive for genuine impact. A considerable portion of older SLBs in particular have KPIs that are not progressing as planned, and many are linked to only one KPI, often not relevant to the sector. This has contributed to scepticism towards the label from investors amid greenwashing concerns. The more limited scope for and prevalence of greenwashing in the use-of-proceeds bond market stands in contrast to SLBs. However, an ICMA report last year also evidenced a significantly declining trend in reported SLB controversies (-80%) based on a representative sample of issuances over the observation period 1Q22-3Q23. Nevertheless, rising financial burdens associated with participating in the SLB space are likely contributing to the subdued appetite for the label. Reviewing bonds is a labour-intensive task, due to the lack of standardised data, making the analysis somewhat bespoke. The vast majority of structures are dominated by penalty-based mechanisms, like coupon step-ups, and pricing of coupon optionality means asymmetry of information often limits the value of the structure. Consequently, SLBs have not experienced broad based adoption so far, they remain concentrated in Europe, and are mostly issued by corporates (70% of issuers).

Quarterly SLB volumes by region



Source: Bloomberg; Daiwa Capital Markets Europe

SLB bonds in issue fall in 2023

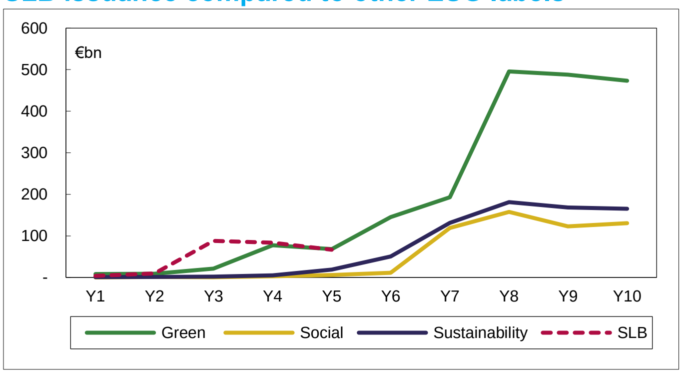


Source: Bloomberg; Daiwa Capital Markets Europe; as of 20.08.2024

SLB coupon features need to evolve to restore investor confidence

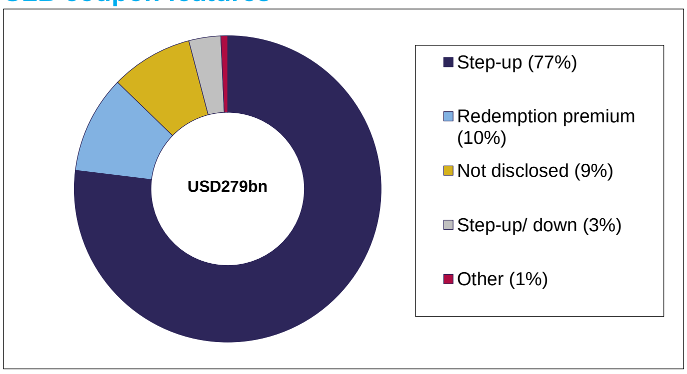
As the SLB market is evolving from novelty to maturity there is arguably the need for SLB structures to evolve with it. Currently, the most common financial mechanism is the coupon step-up (77% of total), whereby penalty premiums are applied if certain sustainability KPI are not achieved. These are followed by redemption premiums (10%) that require the issuer to pay a pre-determined premium at the time of redemption. This penalty-focused approach has only gradually given way to more incentive-based mechanisms (step-downs) that reward issuers for achieving their KPI, thus fostering positive impact. However, these currently only make up a small portion of coupon features. Most coupon penalties average 25bps and appear to be arbitrarily set, with no clear rationale for this clustering. They are more effective if the coupon is set at a low percentage but less so when the level approaches double digits. Additionally, issuers with weaker credit ratings are more likely to be impeded from setting higher coupon step-ups in order to retain their ability to service their debt. Nevertheless, there has been a shift towards higher step-up levels being adopted in more recent sustainability-linked bond structures, which we believe should restore confidence in the label.

SLB issuance compared to other ESG labels



Source: Bloomberg; SLB Year1=2019; Rest Year1=2014; Daiwa Capital Markets Europe

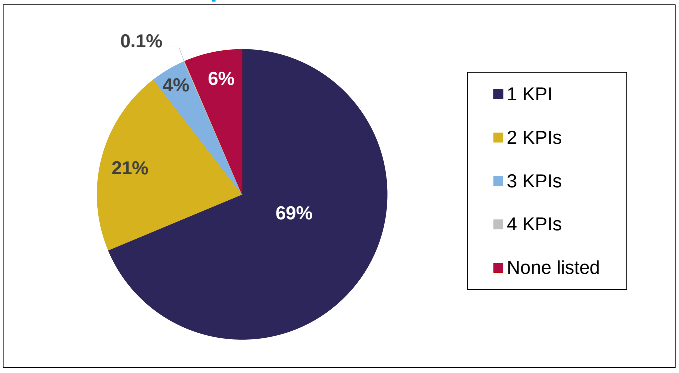
SLB coupon features



Source: Climate Bond Initiative as of 30.11.2023

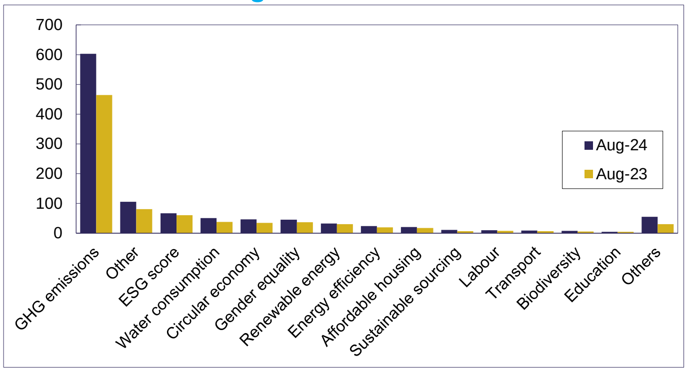
Recognising the aforementioned challenges, the market is shifting towards more detailed guidance, with ICMA having introduced new SLB Principles in June. These primarily aim at improved disclosures and clarifications around KPI selection, which should be consistent with the issuer's overall sustainability strategy. Updates to ICMA's KPI registry now also include themes around biodiversity, the circular economy and water, with additional KPIs for sovereigns. These steps continue to enhance the toolkit and guidance offered to issuers, and should be supportive of future issuance. In this context, we note that SLB instruments only started to emerge from 2019 onwards, at a time when the ESG environment started to become more regulated and structured. Despite the late entry and additional scrutiny, SLB growth rates since inception have been comparable, if not higher, to that of other categories. The compound annual growth rate (CAGR) of SLBs stands at 107% since 2019, ahead of social and sustainability bonds, which started to appear around 2014.

Number of KPIs per SLB



Source: Bloomberg; EUR276bn issuance volume across 850 bonds as of 20.08.2024; Daiwa Capital Markets Europe

Number of KPI categories and distribution



Source: Bloomberg; Daiwa Capital Markets Europe; as of 20.08.2024

Higher KPI count and credible redemption narrative valued by investors

Key performance indicators form an integral part of SLB structures and their specifics and calibration are highly dependent on the type of issuer. We found that SLBs in issue utilise between one and four KPI, with one being the most common (69% of total number of SLB in issue). There is a slight tendency for larger bonds from larger issuers to have more KPI, which may reflect a more holistic approach applied by these issuers, lending more credibility to their product. According to a report by the Climate Bonds Initiative (CBI) published in March, out of 50 sampled SLBs, 96% report on their KPI progress, yet issuers often fail to provide comprehensive reasons when there are changes in performance. Such data restatements are almost always linked to changes in greenhouse-gas (GHG) emissions, which in turn are mostly due to changes in the GHG accounting methodology. Despite some bonds having been structured with unambitious targets, the CBI found that 31% of its sample showed that all listed KPIs were currently off track. Taking the above into consideration, issuers' capacity to articulate the reasons behind missing their SLB targets and present a dedicated plan to address these challenges could be crucial in transforming a negative target performance into a positive sustainability narrative for investors. For instance, Enel, an early adopter of SLBs, is the most prominent case of a missed SLB target thus far. Enel's apparent ability to deliver a convincing sustainability story, even after failing to meet its target, was reflected in a positive reception by investors when the company re-entered the market.

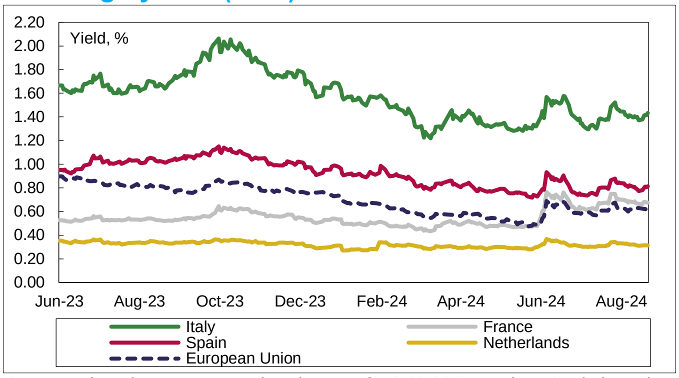
Structural loopholes and how to mitigate them

As mentioned above, greenwashing concerns have arguably played a large role in dulling the reputation of the SLB format and subduing issuance. A World Bank report titled 'Structural Loopholes in Sustainability-Linked Bonds', identifies key weaknesses in SLB structures that can be exploited for greenwashing. These include, among other things, (i) low penalties for failing targets; (ii) scope to minimise the impact of penalties by pushing target dates closer to maturity date; and (iii) options to call an SLB before maturity to avoid or minimise penalties. For issuers wishing to avoid these pitfalls, one of the easiest ways to mitigate investor concerns is by adhering and adopting standardised principles, such as those published by ICMA. Additionally, SLBs ideally require independent third-party verification of KPIs. For instance, the Global Reporting Initiative (GRI) offers verification services for sustainability reporting, which can be leveraged. Lastly, alignment with the Science Based Targets Initiative (SBTi), which defines and promotes best practice in science-based target setting, is a widely accepted way for issuers to test the adequacy of their sustainability targets. Ultimately, we expect the SLB segment to make the same inroad with the wider ESG investor base as other labels in the past. Being one of the most recent formats to appear, it needs to be given time to embrace these changes and best practices.

EU experiences set-back in effort to appeal to wider investor base

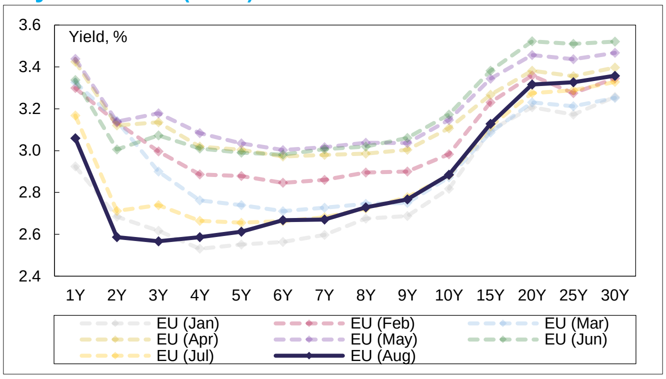
In our last quarterly issue, we wrote about the possibility of EU bonds positioning themselves as euro area public "safe assets" and the importance a potential inclusion in sovereign bond indices could play for this development. However, against general expectations, index providers MSCI and ICE both decided against such a move. Following a market consultation, in June MSCI cited diverging opinions on the matter, but the company plans to re-evaluate the issue again in 2Q25. In the case of ICE, which reached its verdict in early August, a consensus appears to have been even further out of reach. Respondents to ICE's consultation stated that changing the definition to include the EU also raised questions about similar issuers such as the Council of Europe Development Bank (CEB), the European Stability Mechanism (ESM) or the European Financial Stability Facility (EFSF). A major challenge for the EU regarding index inclusion remains the temporary nature of its pandemic borrowing programs, which have come under increasing scrutiny by EU-sceptic political factions that have made gains in recent parliamentary elections and generally oppose further fiscal integration. Ultimately, we expect one of the critical factors for the consideration of EU debt alongside that of sovereigns to be the continuation of fiscal integration efforts. For the time being, these uncertainties have dented the perception of the EU as a governing entity and EU bond yields widened against reference benchmarks such as Bunds. Yields on EU bonds have traded below those of French OATs, which increased sharply in late June in response to the snap French election. If this trend were to persist well into next year, the narrative of supporters of EU bond index-inclusion could strengthen.

Sovereign yields (YTM) over German Bunds*



*Source: Bloomberg; *10-year bonds; As of 30.08.2024; Daiwa Capital Markets Europe*

EU yield curve (YTM) at month-end in 2024



Source: Bloomberg; As of 30.08.2024; Daiwa Capital Markets Europe

New ECB disclosures show steady decarbonisation of purchase programmes

In late June, the ECB released its second report on the carbon footprint of its financial portfolios. Compared with the inaugural report, which exclusively focused on corporate bond holdings, the current one expanded the scope of the disclosures to the Eurosystem's holdings of public sector (PSPP) and covered bonds (CBPP) under the asset purchase programme (APP) and the pandemic emergency purchase programme (PEPP). As such, it covers almost EUR4.5tr in financial assets, almost all the assets held for monetary policy purposes. The report outlines the ECB's emission reduction process and confirmed that continued progress was being made, with greater issuer carbon efficiency being the strongest driver. As at end-2023, the carbon intensity of the EUR367bn Eurosystem corporate sector holdings had declined by 37% since 2021. Most of the exposures (88% of the total) were concentrated in the corporate sector purchase programme (CSPP), with the remainder held in the PEPP. The ECB noted that most of the emissions reduction was due to issuers becoming more carbon-efficient, while capital reallocation effects were only responsible for about 20% of the reduction over the same period. Despite the end of reinvestments under the APP from July 2023, the green tilting policy towards issuers with better climate performance affected EUR23.7bn in assets.

Share of green bonds among sovereign holdings has gradually increased

Inaugural disclosures show that the share of green bonds among the ECB's sovereign holdings has gradually increased over the years. Overall, sovereign bonds account for 86% of public sector holdings and the green portion therein accounted for roughly 1.9% of the PSPP and PEPP as at end-2023. While in the preceding three years the green share in the portfolio grew in line with the expansion of the market, in 2023 the share could not increase to the same degree due to limited reinvestment volumes and the lower secondary market liquidity of green bonds. Nevertheless, the decarbonisation of the portfolio displayed strong progress between 2018-2023, with the weighted average carbon intensity dropping by 55% during that period. This was partially driven by pandemic-related effects. Looking ahead, the Governing Council agreed to set interim emission reduction targets for the corporate portfolios in the APP and PEPP, reflecting guidelines set forth by the EU Benchmarks regulation. For now, the targets will only be used internally to monitor the emission reduction trajectory of the portfolios and help guide potential remedial action should deviations from the desired path be identified.

European primary markets in 2Q24

SSA ESG issuance volumes in 2Q24 reached EUR62bn, down 14% on the previous year, of which 47% had a green bond indicator, 40% were sustainability bonds, and 13% social bonds. SLB issuance continued to be almost irrelevant during the quarter, with just one small trade. We observed falling volumes across most ESG categories, with social bonds declining the most to EUR8bn (-41% yoy). This was due to some of the segment's largest issuers, such as CADES, being absent from the market. For comparison, during the same quarter last year, CADES issued almost EUR6bn in social bonds. However, as we noted in our previous publication, CADES has front-loaded much of its 2024 funding activity and therefore this was not entirely surprising. Nevertheless, social bonds haven't managed to reclaim the heights they achieved during the pandemic era and due to the rather limited issuer and investor base, any recovery is likely to be gradual in nature. Green bonds were also down, at EUR29bn (-25% yoy), while sustainability bonds were the only segment that saw an increase in volumes to EUR25bn (+25% yoy). The IBRD was the single largest issuer of sustainability bonds in 2Q24, with over EUR11bn, followed by the IDA with EUR4.7bn.

SSA - Top 10 European ESG Issuers 1H24

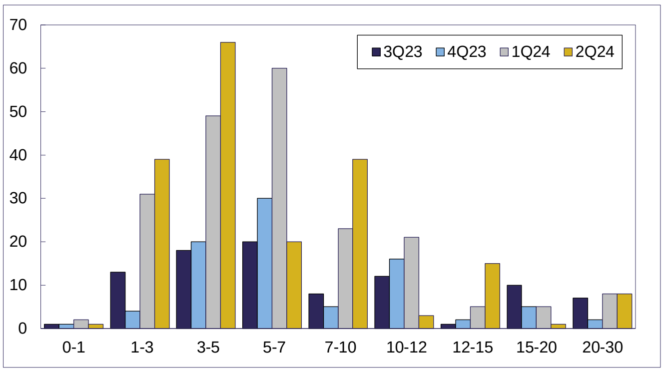
Issuers	Total Issued (€m)*	Average Tenor (years)
IBRD	27,871	6.4
CADES	11,668	3.9
Italy	9,000	13.4
EIB	8,341	6.7
France	8,000	25.4
AIIB	7,411	4.7
KfW	7,196	6.3
European Union	7,000	25.9
IADB	6,730	6.2
IDA	6,497	11.2

*Source: Bloomberg; *Cumulative*

Weaker outlook due to event risk and market volatility

Despite the average deal size falling in 2Q24 to EUR333m (-37.6% yoy), the overall number of registered trades increased substantially to 192, up from 136. Bid-to-cover ratios were only slightly lower than during the previous quarter but elevated compared to last year. 2Q24 SSA supply was skewed somewhat towards the shorter and medium section of the curve with the majority of deals carrying 3-5 year tenors (34%) followed by 1-3 years (20%) and 7-10 years (20%). Looking at indicative 3Q24 issuance data, we see that volumes are trailing by -3% yoy as at mid-August, which in turn was likely due to market volatility caused by the snap French election as well as weaker than expected U.S. CPI and labour data, BoJ policy tightening and the unwinding of the yen carry trade. Although the indicative decline in volumes appears modest, we note that last year's third quarter was already one of the weakest in our series. However, with new-found market stability, we expect some increased September activity as issuer may be looking to avoid a potentially tumultuous end of the year with the U.S. election looming.

Number of SSA transactions per tenor bucket

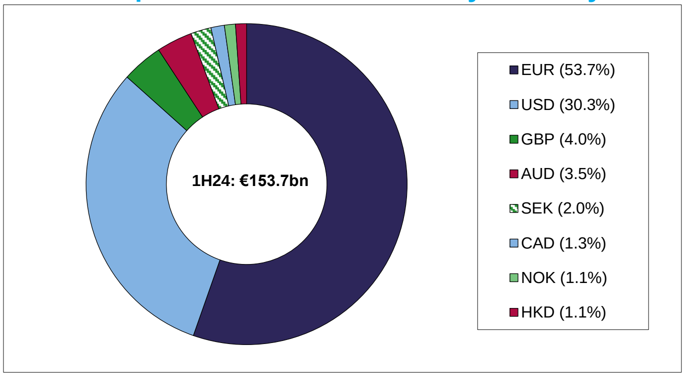


Source: Bloomberg; Daiwa Capital Markets Europe

SSAs buck the trend and continue to consistently produce debut themed bonds

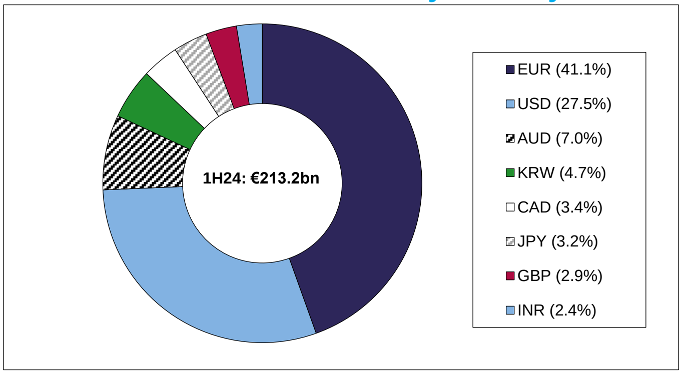
Debut ESG issuance across sectors has generally been down-trending as markets are maturing. However, this development does not appear to apply to the SSA space where debut ESG debt issuance in 1H24 reached the highest level (13) since 1H21. For instance, **Iceland** (A+/A/A2) placed the [world's first sovereign gender bond] in June to fund housing, elder care, and parental leave policies. The small, 3-year private placement carries a 3.4% fixed rate coupon and comes off the back of its inaugural green bond from March. The deal was issued based on an annex to Iceland's sustainable finance framework dealing with [financing for gender equality]. Also noteworthy was a transaction by **Société des grands projets (SGP)**, formerly Société du Grand Paris, from earlier this year. The issuer's [updated green financing framework] from January is one of the first to fully align with two of the six EU-taxonomy environmental objectives. The inaugural bond under the issuer's new framework and name was a EUR1bn green bond with a 25-year maturity, achieving an order book of EUR17bn, the largest in its history. Since 2018 SGP issued EUR21bn in green bonds to fund the Grand Paris Express, a major metro network project to offer urban, social and environmentally development to Paris.

1H24 European ESG SSA issuance by currency



Source: Bloomberg; Daiwa Capital Markets Europe

1H24 Global ESG SSA issuance by currency



Source: Bloomberg; Daiwa Capital Markets Europe

Total **FIG ESG** volumes in 2Q24 reached EUR23bn (-30% yoy), with market activity somewhat skewed to the beginning of the quarter. May accounted for most deals (41%), followed by April (37%) and June (22%). The slowdown in June activity is in part due to lower ESG loan demand from corporates since 2H23, which feeds through to bank balance sheets and funding requirements with a lag. Furthermore, market conditions deteriorated in the wake of the surprise French parliamentary elections, and once issuance did resume at the end of the quarter new deals initially priced at a premium. In terms of different labelled categories, green bonds by far made up the largest proportion with EUR19bn (-30% yoy), followed by EUR2bn in social bonds (-56% yoy). Sustainability bonds of EUR1.6bn (+156% yoy) were the only segment that experienced volume growth, while modest SLB volumes stood at EUR142m compared with no issuance during the same period last year. As market uncertainty gradually crept up throughout the quarter, investors were increasingly looking to moderate duration risk, focusing on medium- and shorter-dated trades. Bond maturities were concentrated in the 3-5 year maturity bucket (39% of total), followed by 1-3 years (19%) and 5-7 years (18%).

FIG - Top 10 European ESG Issuers 1H24

Issurs	Total Issued (€m)*	Average Tenor (years)
Intesa	2,030	5.0
LBBW	1,670	3.9
CaixaBank	1,561	7.0
BPCE SFH	1,500	10.0
Münchener Hyp	1,269	6.0
Generali	1,250	7.5
Crédit Agricole SFH	1,250	10.0
ING Groep	1,250	11.0
DNB Bolingkredit	1,131	3.7
Berlin Hyp	1,123	3.1

*Source: Bloomberg; *Cumulative*

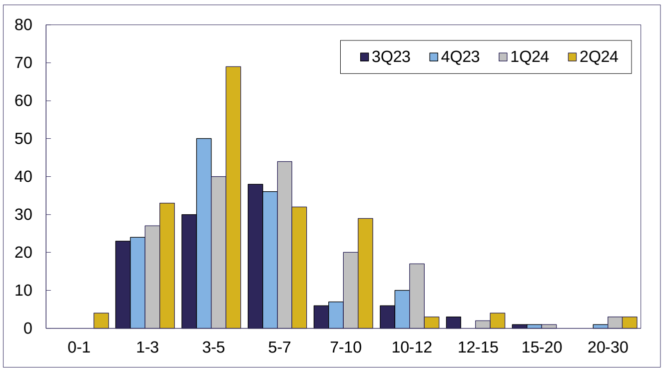
Solid credit fundamentals accompanied by improving outlooks likely conductive for ESG activity

Looking ahead, the FIG sector appears to be recovering some lost ground following the strong decline of the past quarter. Indicative 3Q24 numbers look encouraging compared to the same period of 2023. Based on mid-August data, FIGs issued EUR8.9bn in bonds, +128% above last year's figure. This was the highest July volume registered since 2021, as markets rebounded from the June slump. Moreover, European financial institutions are entering 2H24 from a position of relative strength, with mostly better than expected 2Q24 earnings. The higher-for-longer rates environment has ensured that bank profits remained at elevated levels compared with recent averages, while asset quality indicators and loan demand were stable. Reduced cost of risk assumptions imply a lower perceived risk environment for FIGs over the near term, rounding out a mostly positive backdrop. In conjunction, these factors should act moderately supportive for near-term ESG issuance activity. Most financial institutions have tentatively signalled that they expect a stable or moderately improved operating environment going forward. Paired with rate cuts that are likely to materialise over the coming months and quarters, this should spur further demand for ESG bonds.

Largest deal of 2Q24 also a debut transaction

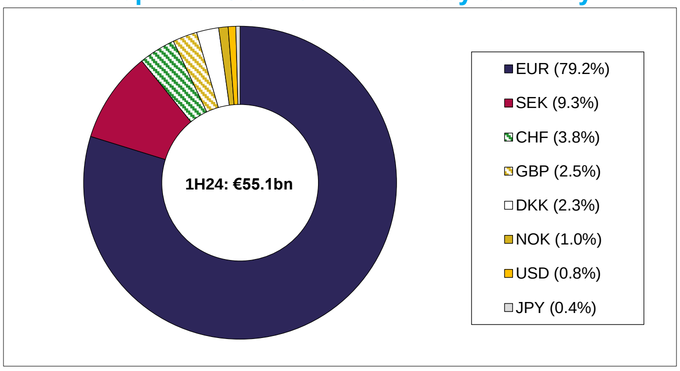
The largest FIG trades of the quarter were placed by UK and Italian institutions. In May, **Lloyds Banking Group** launched its inaugural green bond, following an update to its sustainable bond framework one month prior. The Sr. HoldCo transaction was sized at EUR1bn and carried a maturity of 8NC7. Lloyds' status as national champion and the novelty factor helped drive strong demand, enabling book orders to reach more than 5x deal size. This helped to tighten the spread by 32bps to MS+118bps, leaving just 5bps new issue premium on the table. **Intesa San Paolo** issued its first unsecured euro trade of the year in early April, which came as a dual-tranche offering. The senior preferred bonds were placed into a relatively benign funding window, with the longer-dated 6.5-year leg carrying the green label. It was sized at EUR1bn and generated book orders of 2.5x deal size. This helped the final spread narrow considerably to MS+107bps (-38bps from IPT), thus pricing with only a modest premium of ~3bps. It was Intesa's only green bond so far this year, alongside the Daiwa-led green EuroYen transaction from March. Intesa placed JPY37.1bn across three senior preferred tranches, its largest EuroYen transaction to date.

Number of FIG transactions per tenor bucket



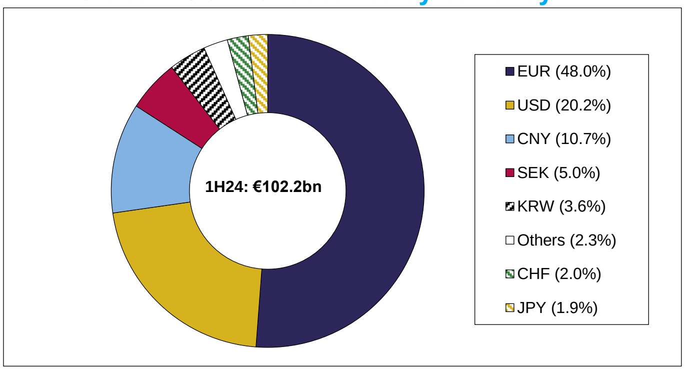
Source: Bloomberg; Daiwa Capital Markets Europe.

1H24 European ESG FIG issuance by currency



Source: Bloomberg; Daiwa Capital Markets Europe

1H24 Global ESG FIG issuance by currency



Source: Bloomberg; Daiwa Capital Markets Europe

Key ESG Transactions 2Q24

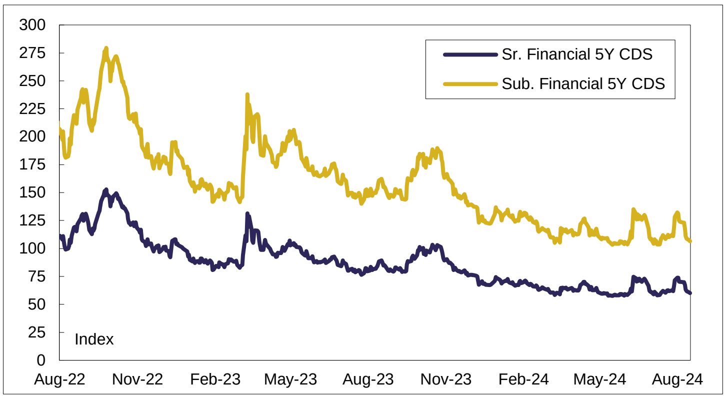
Bank	Rank	Amount	Maturity	IPT (bps)	Final Spread (bps)	Book Orders
SSA						
Italy	Sr. Unsecured (Green)	EUR9bn	13Y	BTPS + 11	BTPS + 9	>EUR84bn
KfW	Sr. Unsecured (Green)	EUR4bn	8Y	MS + 8	MS + 6	>EUR24.5bn
IDA	Sr. Unsecured (SDB)	USD4bn	5Y	SOFR MS + 39	SOFR MS + 37	>USD9bn
IBRD	Sr. Unsecured (SDB)	USD3bn	2Y	SOFR MS + 19	SOFR MS + 17	>USD7.3bn
IBRD	Sr. Unsecured (SDB)	USD3bn	7Y	SOFR MS + 49	SOFR MS + 48	>EUR5.4bn
BNG Bank	Sr. Unsecured (Social)	EUR1.75bn	5Y	MS + 15	SOFR MS + 13	>EUR2.9bn
BNG Bank	Sr. Unsecured (Sustainability)	EUR1bn	7Y	MS + 20	MS + 18	>EUR1.3bn
IBRD	Sr. Unsecured (SDB)	USD1.5bn	4Y	SOFR MS + 30	SOFR MS + 30	>USD2.1bn
CEB	Sr. Unsecured (Social)	EUR1.25bn	7Y	MS + 15	MS + 13	>EUR3.3bn
CADES	Sr. Unsecured (Social)	USD4bn	5Y	SOFR MS + 4	SOFR MS + 40	>USD17bn
AIIB	Sr. Unsecured (SDB)	EUR1bn	7Y	MS + 21	MS + 17	>EUR5.6bn
NRW Bank	Sr. Unsecured (Green)	EUR1bn	7Y	MS + 14	MS + 12	>EUR3.2bn
NWB Bank	Sr. Unsecured (Water)	EUR1bn	7Y	MS + 22	MS + 18	>EUR4bn
UNEDIC	Sr. Unsecured (Social)	EUR1bn	10Y	FRTR + 10	FRTR + 7	>EUR12.7bn
Kommuninvest	Sr. Unsecured (Green)	EUR1bn	3Y	MS + 3	MS + 0	>EUR2.6bn
IDA	Sr. Unsecured (SDB)	GBP800m	5Y	SONIA MS + 30	SONIA MS + 21	>GBP900m
CEB	Sr. Unsecured (Social)	USD1bn	3Y	SOFR MS + 26	SOFR MS + 24	>USD5.3bn
Region Wallone	Sr. Unsecured (Social)	EUR750m	30Y	BGB + 37	BGB + 34	>EUR3.8bn
FIG (Senior)						
Lloyds Bank	Sr. HoldCo	EUR1bn	8NC7	MS + 150	MS +118	>EUR4.6bn
Intesa	SP (Green)	EUR1bn	6.5Y	MS + 145	MS + 107	>EUR2.5bn
Vonovia	Sr. Unsecured (Social)	EUR850m	10Y	MS + 210	MS + 170	>EUR4bn
Belfius Bank	SP (Green)	EUR750m	6Y	MS + 110	MS + 82	>EUR1.25bn
BFCM	SP (Green)	EUR750m	7Y	MS + 110	MS + 75	>EUR2.5bn
BPER Banca	SP (Green)	EUR500m	7NC6	MS + 155	MS + 125	>EUR2bn
Aareal Bank	SNP (Green)	EUR500m	2Y	MS + 280	MS + 255	>EUR1.7bn
Permanent TSB	Sr. Holdco (Green)	EUR500m	6.25NC5.25	MS + 195	MS + 160	>EUR2bn
Sparebank 1 Oesl.	SP (Green)	EU500m	5Y	MS + 95/100	MS + 75	>EUR850m
BayernLB	SNP (Green)	EUR500m	7Y	MS + 130/135	MS + 105	>EUR1.45bn
Swedbank	SP (Green)	EU500m	6Y	MS + 90/95	MS + 65	>EUR1.15bn
Banca Pop di Sondr.	SP (Green)	EUR500m	6NC5	MS + 165	MS + 130	>EUR1.65bn
FIG (Subordinated)						
Nordea	Tier 2 (Green)	EUR750m	11NC6	MS + 170	MS + 150	>EUR2.7bn

Source: BondRadar, Bloomberg; SDB=Sustainable Development Bond; CAB = Climate Awareness Bond; Daiwa Capital Markets Europe

Secondary markets in 2Q24

A series of market shocks over the past couple of months saw CDS prices increase sharply. Prices responded to the announcement of a snap French election, and more recently the broad-based stock market sell-off amid the unwinding of the yen carry trade. In conjunction these events pushed average CDS price up to levels last seen in January. Nevertheless, the current 3-month average price of the senior financials CDS index was only 1bp wider than the preceding three months, while the average subordinated index price remained unchanged over the same period. This higher-risk environment at the end of the quarter resulted in issuers putting trades on hold as spreads widened and funding costs rose. The 3-month difference between the subordinated and senior indices averaged some 50bps, lower than the preceding three-month period (-4bps) and well below the four-year average of 72bps. Solid 2Q24 credit fundamentals and generally stable economic outlooks in most European operating environments ensured that CDS prices returned to recent lows quickly.

iTraxx Financials Index

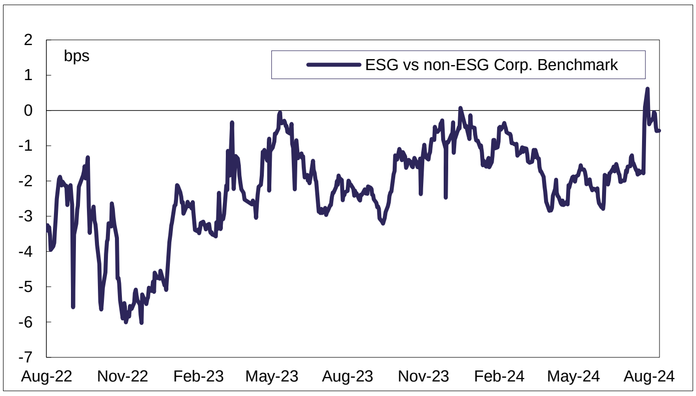


Source: Bloomberg; Data until 20.08.2024; Daiwa Capital Markets Europe

Market volatility erases most of ESG index greenium

The option-adjusted spread (OAS) between the ESG and non-ESG themed indices reflected recent market turmoil, rising quickly above the equilibrium. With market concerns easing, spreads have started to settle below the equilibrium again. This was not captured in the 2Q24 median OAS differential due to its lagged response. During the quarter it was -2bps, slightly wider than the -1bp seen in 1Q24 and 4Q23. However, in early August, the differential briefly moved into positive territory in response to wider market volatility. Arguably, greeniums have steadily been decreasing for some time, and more so during periods of market stress, with some lasting effects. While we expect the differential to widen again, helped by lower funding costs from possible rate cuts, pressure from volatile market moves will remain on eliminating the greenium altogether.

Spreads (OAS) of ESG vs non-ESG benchmarks

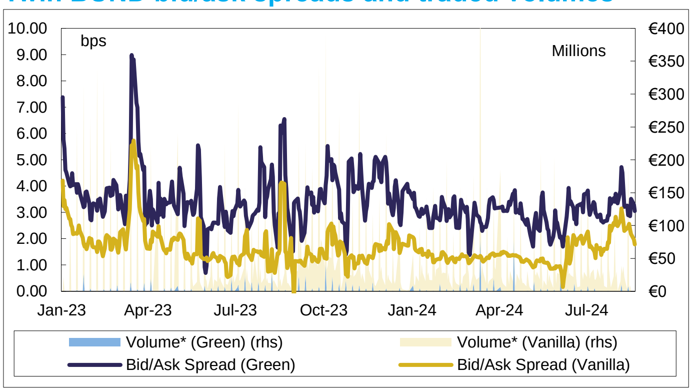


Source: Bloomberg; Barclays MSCI Euro-Corporate ESG Index vs Barclay Pan-European Aggregate Corporate Index; Data until 20.08.2024; Daiwa Capital Markets Europe

Bund greenium approaches series low as trading volumes fall

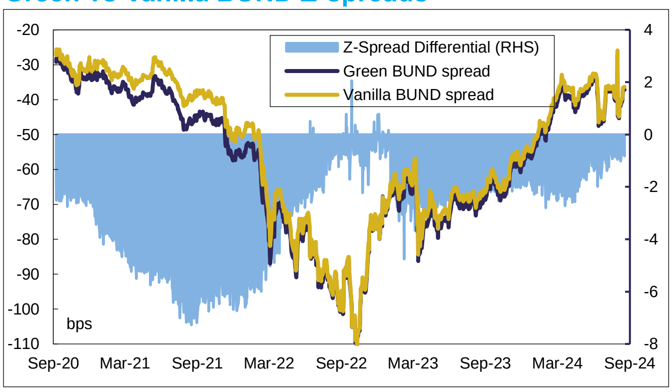
Average greeniums for liquid sovereigns such as German Bunds contracted minimally over the past quarter, with buffers decreasing against the equilibrium. The 2Q24 median spread differential of the German Twin Bunds was -1.5bps compared to -2bp three months earlier. Recent quarterly performance as well as indicative 3Q24 figures are nearing low points observed in 3Q22: -0.8bps and 4Q22: -0.5bps, in line with greenium trajectories seen in primary markets. Bid-ask spreads of the green twin Bund, narrowed against the vanilla bond, as indicative trading volumes have fallen since July (-72% yoy). The 3-day rolling average spread over the past three months was 3bps for the green (previous 3-month reading: 2.9bps) and 1.7bps (1.3bps) for the conventional bond. The average bid-ask spread differential between green and vanilla was 1.3bps over the same observation period, which compares favourably to the series total of 1.7bps.

Twin BUND bid/ask spreads and traded volumes



Source: Bloomberg; until 20.08.2024; Daiwa Capital Markets Europe

Green vs Vanilla BUND Z-spreads



Source: Bloomberg; until 20.08.2024; Germany Aug-2030 Twin; Daiwa Capital Markets Europe

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