Capital

CBA launches $750m hybrid raising

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CBA will have the ability to raise “more or less” than the expected $750 million in the PERLS VI offering. **Photo: Glenn Hunt**

Jonathan Shapiro

Commonwealth Bank of Australia has ushered in a new generation of Tier 1 bank capital securities as global regulators demand hybrid investors take on more risk to protect banks from failure.

CBA’s $750 million hybrid offer, known as PERLS VI, allows the prudential regulator to invoke a “non-viability term” that converts hybrid investors into shareholders under extreme circumstances to meet new global capital requirements, known as Basel III.

KEY POINTS

- The bank’s hybrid offer is being closely watched by local and overseas banks, says an analyst.
- The offer is the third Tier 1 hybrid by an Australian bank in 15 months.

The bank’s chief financial officer, David Craig, said PERLS VI, which will replace $1.46 billion of maturing PERLS IV securities, demonstrated the group’s “pro-active approach to its ongoing capital management strategy”.

Credit rating agency Standard & Poor’s, which assigned PERLS VI a BBB- rating, four notches below the bank’s senior AA- rating, said Australian bank hybrids were, in effect, “canaries in the coalmine” as new rules were fast-tracked.

“This is the first true perpetual deal and a lot of banks here and around the world are watching this closely,” said Andrew Papageorgiou of boutique funds manager Realm Investment.

“There are several regional banks due to redeem securities either at the end of this year or early next year. In that context, this issue could act as a benchmark of sorts,” Mr Papageorgiou said.

There are also doubts as to whether investors globally are prepared to accept the risks imposed upon them for the cost of capital that banks are willing to provide.

“There is pushback in Europe about what constitutes Tier 1,” said Mr Papageorgiou. “Depending on how successful this transaction is, it gives the banks some impetus to go back to the regulators to work out how they are going to effectively raise capital in this form.”

The PERLS offer is the third Tier I hybrid by a major bank in the past 15 months following $1.33 billion and $1.2 billion raisings from ANZ last year and Westpac in February.

While the ANZ and Westpac hybrids are not fully compliant with the new regulations, the Australian Prudential Regulation Authority has agreed to the instruments and counts them as Tier I capital until their first redemption dates.

The securities, like the PERLS offer, contain “capital conversion triggers” which result in a compulsory conversion of the hybrids into equity should losses erode the bank’ s common equity ratio below 5.125 per cent.

According to brokers, the CBA hybrid will pay a margin of between 380 and 400 basis points over the bank bill rate, which equates to an initial interest rate of 7.43 per cent and 7.63 per cent.

In a highly unusual move, CBA chose not to disclose this margin through documents to the Australian Securities Exchange nor via the toll-free hotline. The exact margin will be set following a bookbuild next week.

The rate disclosed to brokers provides a modest premium over the most recent hybrid offers from ANZ and Westpac which pay 387 and 375 basis points over the bank bill rate.

Institutional hybrid investor Jarod Dawson of PM Capital said that rates on safer, older-generation hybrids issued by Australian banks in overseas markets provided better value.

“We think investors should be focusing their attention offshore when looking for hybrid exposure to Australian major banks,” said Mr Dawson.

“For example, we would prefer CBA’s 3-Year US dollar stock settled hybrid security, which is currently valued at around 450 basis points over the bank bill rate when swapped back to Australian dollars,” he said.

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Jonathan Shapiro followed the Australian corporate bond markets as debt editor at Insto from July 2005. In that time he covered the dramatic events of the global financial crisis and its impact locally. Jonathan also had a year-long stint at the bond syndicate desk at ANZ, providing research and analysis to bankers, traders and senior management. He has studied finance and economics in South Africa and journalism in Sydney.

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