

Hypo Real Estate

More run-off vehicle details - Reiterate Overweight

- We reiterate our Overweight recommendation on HYPORE. We especially favour the DEPPFA LT2 €FRN Dec-2015 at 69. We also note that the Basel III grandfathering amortisation schedule announced over the weekend does not seem to extend beyond incentives to redeem, which reflects positively on low-cash price step-up tier 1's, including the HYPORE €5.864 at 43 (all prices as of 10:45am 13th Sept).
- On the 10th Sept SoFFin confirmed in a public statement that it was increasing HYPORE's total funding guarantees by €40bn in the period towards the end of the year. This will temporarily increase the total funding guarantees available to €142bn, and is intended to overcome any possible liquidity gaps during the transfer of assets to the FMS Wertmanagement run-off vehicle.
- We note that the Handelsblatt reported on the 11th Sept that the bank is currently scheduled to transfer the run-off assets to FMS Wertmanagement on 1st October, and the volume of assets to be transferred has been narrowed down to €180-€185bn, reduced from 'up to €210bn' previously. According to the Handelsblatt, the extra guarantees will be provided in two €20bn tranches: a general guarantee to cover market volatility in the run-up to the transfers, and a technically motivated guaranteed to cover any gaps from temporary mismatches which could arise while transferring assets. The EU is reportedly hoped to provide a temporary approval for the additional guarantee lines by the 22nd September.
- Previously the institution has guided for the asset-transfer to the FMS Wertmanagement run-off vehicle to occur in Q4. If the above schedule can be kept, we note that transferring the assets on the 1st October would effectively give the new clean bank a full final quarter without the transfer-assets. The Handelsblatt article also indicates that the state intends to reprivatise the bank around 2014.
- Separately, we note that Hypo Real Estate Chairwoman Manuela Better reportedly stated on 8th Sept that she was hopeful the institution would return to profit in 2011 (Sueddeutsche Zeitung, 13 Sept). After the transfers to FMS Wertmanagement we believe an earlier return to profitability in 2011 is likely, in part as the costly SoFFin funding guarantees can be removed once the transfer-assets have been jettisoned, although near-term losses may still occur after the transfer in Q4'10 due to provisioning on the remaining CRE assets, or possible one-off charges. The new bank's business plan is based around Pfandbrief covered bonds, which are intended provide duration matched funding.

Banks

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Date	Rating	Instrument
12 Jan 09	Overweight	HYPORE €FRN May 11

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