

12 August 2024

## ANZ + Suncorp. A small opportunity arises for Suncorp Group Tier 2 investors out of the shadows

**IAM Capital Markets**

*We see potential for these bonds to be bought back/tendered at \$107-\$108 based on historical experience and the senior / subordinated (T2) differential.*

Post ANZ's acquisition of Suncorp Metway, we see a small opportunity arising for Suncorp Group Tier 2 investors to capitalise on higher bond returns. For background, Suncorp Group is the old insurance business that will continue to have Tier 2 (T2) and Additional Tier 1 (AT1) instruments outstanding. The positive catalyst we expect to translate into potentially higher bond returns is that Suncorp Group will materialise post ANZ transaction with too much capital.

What does this mean? Well, with too much capital you can generally do two things:

1. Return to shareholders - through buybacks/special distributions; and/or
2. Return to debtholders - through buybacks/tenders.

Re (2), historically Australian insurers have had to pay up to buyback/tender existing capital instruments. The recent evidence points to QBE paying up to \$2-\$5 above market to buyback its USD capital instruments. If this is the case, then a similar outcome for T2 investors would be viewed positively from a capital upside perspective. Examining the senior / subordinated (T2) differential for Suncorp Group, it appears to be around 100bps. For an instrument with 4.5 years credit spread duration, this would equate to an increase of AUD4.5ppts in price (all else-equal the issuer would have to "pay-up"). However, even if the securities are not called as expected, you still earn a healthy margin of 3m BBSW + 235bps until call date of July 2029 (currently ~6.80%). This suits those investors who think rates may continue to stay higher for longer as well.

Suncorp Group is currently sitting on too much capital at not only a common equity tier 1 (CET1) level but also a total capital (includes CET1, AT1, and T2) level. This means they can effectively do (1) and (2) as above. In the T2 space, the most obvious candidate for a buyback/tender is the Suncorp Float 06/27/2034. Note, there are four T2 notes outstanding that could be bought back/tendered.

Why? Well, three key reasons driving this:

1. This line is AUD600m outstanding and so management would get a better bang for buck from optimising their funding base in this security.

2. This line has the shortest maturity (2034 vs 2035-2038). In essence, the shorter the maturity, the less insurance equity credit is given by the rating agencies, which means the security becomes effectively expensive debt.
3. The capital was used to fund the bank and so would be transferred back to the group post transaction. Would make sense from an administration perspective to then enact this capital optimisation strategy.

ISIN	Name	Ticker	Ask Yield to ...	Bid Yield to M...	Coupon	Next Call D...	Maturity	Amt Issued(ML)	Series	BB R...	Mty Type	Announce Cu...	Ask Px	Source
AU3FN0081386	Suncorp Group Ltd	SUNAU	5.907	5.944	FLOAT	06/27/2029	06/27/2034	600.00	HTN	NR	CALLABLE	09/20/2023 AUD	102.707	BCMP
AU3FN0075644	Suncorp Group Ltd	SUNAU	6.327	6.351	FLOAT	12/01/2028	12/01/2038	250.00	HTN	NR	CALLABLE	02/20/2023 AUD	103.673	BCMP
AU3FN0055802	Suncorp Group Ltd	SUNAU	6.087	6.103	FLOAT	12/01/2025	12/01/2035	250.00		BBB+	CALLABLE	08/21/2020 AUD	101.076	BCMP
AU3FN0067906	Suncorp Group Ltd	SUNAU	6.090	6.107	FLOAT	06/01/2027	06/01/2037	290.00	HTN	BBB+	CALLABLE	03/27/2022 AUD	102.022	BCMP

Source: Suncorp Group Bloomberg

## Capital instruments

	Semi-annual coupon rate/ margin above 90 day BBSW	Optional Call / Exchange Date	Issue Date	GI \$M	Bank \$M	SGL \$M	Regulatory Capital \$M	Accounting Balance <sup>1</sup> \$M
<b>31 December 2023</b>								
SGL Subordinated Debt 2 <sup>2</sup>	225 bps	Dec 2025	Sep 2020	250	—	—	250	249
SGL Subordinated Debt 3 <sup>2</sup>	230 bps	Jun 2027	Apr 2022	290	—	—	290	289
SGL Subordinated Debt 4 <sup>2</sup>	265 bps	Dec 2028	Mar 2023	250	—	—	250	248
SGL Subordinated Debt 5 <sup>2,3</sup>	235 bps	Jun 2029	Sep 2023	—	600	—	600	597
<b>Total subordinated debt</b>				<b>790</b>	<b>600</b>	<b>—</b>	<b>1,390</b>	<b>1,383</b>
SGL Capital Notes 2 (SUNPG) <sup>2</sup>	365 bps	Jun 2024	Nov 2017	165	210	—	375	374
SGL Capital Notes 3 (SUNPH) <sup>2</sup>	300 bps	Jun 2026	Dec 2019	389	—	—	389	386
SGL Capital Notes 4 (SUNPI) <sup>2</sup>	290 bps	Jun 2028	Sep 2021	55	350	—	405	400
<b>Total Additional Tier 1 capital</b>				<b>609</b>	<b>560</b>	<b>—</b>	<b>1,169</b>	<b>1,160</b>
<b>Total</b>				<b>1,399</b>	<b>1,160</b>	<b>—</b>	<b>2,559</b>	<b>2,543</b>

Source: Suncorp Group Investor Presentation

The 29/34 does not qualify for equity credit. Its original maturity was short of the 15yr minimum for equity credit, but as it was raised specifically for the bank, equity credit wasn't a consideration. So as of the bank's sale, it is excess with no equity credit. Thus, it is not only an expensive debt, but given the proceeds of the sale and re-capitalisation, it should be considered excess debt, not just expensive.

## Research Report Disclosure

IAM Capital Markets Limited (AFSL 283119) ('IAM Capital Markets') is a financial service business and provides general financial product advice only. As a result, this document, the Content and the Reports are not intended to provide financial product advice and must not be relied upon or construed as such. IAM Capital Markets does not express any opinion on the future or expected value of any financial product and does not explicitly or implicitly recommend or suggest an investment strategy of any kind. The Content and the Reports provided in this document have been prepared based on available data to which IAM Capital Markets have access. Neither the accuracy of that data nor the research methodology used to produce the Content and Reports can be or is guaranteed or warranted. Some of the research used to create the Content and the Reports is based on past performance. Past performance is not an indicator of future performance. Any forecasts are predictive in character and based on specified assumptions generally available at the time and no reliance should be placed on the accuracy of any forecast information. The actual results may differ substantially from the forecasts and are subject to change without further notice.

The data generated by the research in the Content or the Reports is based on research methodology that has limitations; and some of the information in the Content or the Reports is based on information from third parties. IAM Capital Markets does not guarantee the currency of the Content or the Reports. If you would like to assess the currency, you should compare the Content or the Reports with more recent characteristics and performance of the assets mentioned within it.

You acknowledge that investment can give rise to substantial risk and a product mentioned in the Content or the Reports may not be suitable to you. The Content and Reports have been provided or made available by IAM Capital Markets without taking account of your objectives, financial situation, and needs. IAM Capital Markets strongly recommends that you seek independent accounting, financial, taxation, and legal advice, tailored to your specific objectives, financial situation or needs, prior to making any investment decision. Neither IAM Capital Markets, nor any of its directors, authorised representatives, employees, or agents, makes any representation or warranty as to the reliability, accuracy, or completeness, of the Content and Reports. Nor does IAM Capital Markets accept any liability or responsibility arising in any way (including negligence) for errors in, or omissions from the Content and Reports. IAM Capital Markets, its staff and related parties earn fees and revenue from dealing in the securities as principal or otherwise and may have an interest in any securities mentioned in this document. Any reference to credit ratings of companies, entities or financial products must only be relied upon by a 'wholesale client' as that term is defined in section 761G of the Corporations Act 2001 (Cth). IAM Capital Markets does not provide tax advice and is not a registered tax agent or tax (financial) advisor, nor are any of IAM Capital Markets' staff or authorised representatives. IAM Capital Markets does not make a market in the securities or products that may be referred to in this document.

An investment in notes, corporate bonds, syndicated loans, or any debt instrument should not be compared to a bank deposit. Notes, corporate bonds, syndicated loans, or any debt instrument have a greater risk of loss of some or all an investor's capital when compared to bank deposits. IAM Capital Markets is not licensed to provide foreign exchange hedging or deal in foreign exchange contracts services. IAM Capital Markets may quote to you an estimated yield when you purchase a bond. This yield may be calculated by IAM Capital Markets on either A) a yield to maturity date basis; or B) a yield to early redemption date basis. Some bond issuances include multiple early redemption dates and prices, therefore the realised yield earned by you on the bond may differ from the yield estimated or quoted by IAM Capital Markets at the time of your purchase.

To the extent IAM Capital Markets has utilised research from BondAdvisor, the following Disclaimer applies. BondAdvisor has acted on information provided to it and our research is subject to change based on legal offering documents. This research is for informational purposes only. We note that this security offering is only being made to investors who are not retail clients under the Corporations Act nor located outside Australia. This information discusses general market activity, industry or sector trends, or other broad-based economic, market or political conditions and should not be construed as research or investment advice. The Content of this Report is not intended to provide financial product advice and must not be relied upon as such. The Content and the Reports are not and shall not be construed as financial product advice. The statements and/or recommendations on this web application, the Content and/or the Reports are our opinions only. We do not

express any opinion on the future or expected value of any Security and do not explicitly or implicitly recommend or suggest an investment strategy of any kind. The Content and Reports provided have been prepared based on available data to which we have access. Neither the accuracy of that data nor the methodology used to produce the Report can be guaranteed or warranted. Some of the research used to create the Content is based on past performance. Past performance is not an indicator of future performance. We have taken all reasonable steps to ensure that any opinion or recommendation is based on reasonable grounds. The data generated by the research is based on methodology that has limitations; and some of the information in the Reports is based on information from third parties. We do not guarantee the currency of the Report. If you would like to assess the currency, you should compare the Reports with more recent characteristics and performance of the assets mentioned within it. You acknowledge that investment can give rise to substantial risk and a product mentioned in the Reports may not be suitable to you.

You should obtain independent advice specific to your particular circumstances, make your own enquiries and satisfy yourself before you make any investment decisions or use the Report for any purpose. This Report provides general information only. There has been no regard whatsoever to your own personal or business needs, your individual circumstances, your own financial position or investment objectives in preparing the information. We do not accept responsibility for any loss or damage, however caused (including through negligence), which you may directly or indirectly suffer in connection with your use of this Report, nor do we accept any responsibility for any such loss arising out of your use of, or reliance on, information contained on or accessed through this Report.

© 2024 IAM Group | Income Asset Management Group Limited ABN 42 010 653 862 (ASX: IAM) and wholly owned subsidiaries, IAM Capital Markets Ltd ABN 86 111 273 048 AFSL 283119, IAM Cash Markets Pty Ltd ACN 164 806 357 as corporate authorised representative (no. 001295506) of AFSL 283119, Trustees Australia Limited ABN 63 010 579 058 AFSL 260038 and IAM Funds ABN 54 643 600 088, together the IAM Group.

The information in this document is for general information purposes only and does not purport to contain all matters relevant to any particular or financial instrument. It is not intended to be a recommendation, offer or invitation to purchase, sell or otherwise deal in securities or other investments. Before making any decision in respect to a financial product, you should read the relevant Financial Services Guide and Product Disclosure Statement available from IAM Group <https://www.incomeam.com> and seek independent and specific advice from an appropriately qualified professional. IAM Group shall not be liable for any errors, omissions, defects or misrepresentations in the information or for any loss or damage (whether direct or indirect) suffered by persons who use or rely on the information contained here.