

Subject: Re: Banco Espirito continued.....

From: Nav Gupta <[REDACTED]>

Date: Tue, 01 Jul 2014 10:39:04 -0400

To: [REDACTED]

Cc: Paul Morris <[REDACTED]> ,

Vinit Sahni <[REDACTED]> ,

Tazia Smith <[REDACTED]>

Classification: Confidential

Banco Espirito has 3 issues

1. it is in trouble with regulators after it funded its cash position by issuing bills and bonds to retail and institutional clients who has entrusted funds to the bank on a discretionary basis. market participants worry about the firms ability to raise capital.
2. it has a large exposure (3 to 5bn) with Angola
3. management is in flux after CEO stepped down

There is a lot of bad news priced into all levels of the capital structure of these bonds

Espirito will likely issue more equity and AT1 debt. as a result it is likely the senior unsecured and LT2 debt will be shielded from loss-absorption

Both the LT2 issue the BESPL 7.125 23 and the Senior unsecured BESPL 4.75 18 have been hit hard. they have richened already from the lows of the day (The 23's are around 95 mid (8.6%) although hit an intra-day low in the high 80's earlier today) they still look a decent buy to scale into and are 230bp higher

yield than a week ago. The 4.75s 18 yield around 4.4% which is 160bp higher compared to a week ago

From: Tazia Smith/db/-
dbcom@DBAMERICAS

To: [REDACTED], Vinit Sathe/db/-
dbcom@DBAMERICAS,

Cc: Nav Gupta/db/dbcom@DBEMEA, Paul
Morris

Date: 01/07/2014
15:25

Subject: Banco Espirito continued.....
[C]

Classification: Confidential

Rich -

Vinit highlights the BESP 7.125 2023s LT2 (ISIN PTBEQJOM0012). This is subordinated Banco Espirito credit. Trading ~94.125x95.375 or 8.4% (bloomberg). DB trader is wide on these given volatility - his indicative market is 93.5x95.5, so we'd clearly work a level if interested.

Vinit - care to opine further?

Thanks,
Tazia

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(Embedded image moved to file: pic12335.gif)

From: Tazia Smith/db/-
dbcom

To:
,

Cc: Paul Morris, Nav Gupta/db/-

dbcom@DBEMEA

Date: 07/01/2014 09:49
AM

Subject: Fw: DB Early Morning Reid 7/1/14 + some Banco Espirito (BES
PL) trading color [C]

Classification: Confidential

Hey Rich -

Just an FYI , pls see color on BES PL as an FYI (have seen some HF interest
in
the name) also some follow through in incremental demand for euro Banca
MOnTe
Dei Paschi (BMPS IM).

Let me know if you want more flow color or if peripheral banks are not of
interest.

Thx,
Tazia

----- Forwarded by Tazia Smith/db/dbcom on 07/01/2014 09:45 AM -----

From: Tazia Smith/db/-
dbcom

To:

Cc: Joseph Cothron/db/dbcom@DBAMERICAS, Vahe Stepanian/db/-
dbcom@DBAmericas, Jay
Lipman/db/dbcom@DBAMERICAS, Ariane Dwyer/db/dbcom@DBAMERICAS,
Melissa
Mittelman/db/dbcom@DBAMERICAS,
[REDACTED]

EFTA01469247

Date: 07/01/2014 08:22
AM

Subject: DB Early Morning Reid 7/1/14 + some Banco Espirito (BES PL)
trading color [C]

Classification: Confidential

Good Morning -

Please see Jim Reid's 1H/2Q/Month-end summary below citing multi-century low sovereign yields, concerns vs. elation over persistent asset price performance, and a highlight of the underperformance of European financials - Portugal's Banco Espirito Santo (BES PL) tumbled 17% yesterday. See today's inter-day bounce in chart below (be aware that naked short selling was temporarily banned today). On that note, DB's BES PL trader points out that the name was crowded to start the year (long onlies as well as US HFs), and now sees selling pressure from pan-european continent long-only sellers.

Note

the bounce (but also increased supply) post the company's 1.04bn euro capital raise on 5/22 (rights of, struck at 0.65). Recall Portugal's Espirito Santo Financial Group (ESFG) owns 27.4% (Reuters) of Banco Espirito post raise. Please call the desk to discuss further.

Please see the Early Morning Reid below/attached.

Speak with you soon,
Tazia

[attachment "EMR 7.1.14.pdf" deleted by Tazia Smith/db/dbcom]

Banco Espirito (BES PL) Interday Trading 7/1/14
(Embedded image moved to file: pic32338.gif)

Banco Espirito (BES PL) 1-Year Price History
(Embedded image moved to file: pic29126.gif)

Deutsche Bank - Fixed Income
Research

Early Morning Reid - Macro
Strategy
01 July 2014 (6 pages/ 178
kb)

Download the complete
report:
[http://pull.db-gmresearch.com/p/17805-C28E/90612075/-
DB_EMR_2014-07-01_0900b8c
088724b5b.pdf](http://pull.db-gmresearch.com/p/17805-C28E/90612075/-DB_EMR_2014-07-01_0900b8c088724b5b.pdf)

Key Market
Data
(Index @ Close //
Change)
(ITX Crossover @ 242 //
+3)
(ITX Europe 125 @ 62 //
+1)
(CDX 125 @ 59 //
+1)
(CDX HY - pts @ 108.66 //
-0.154)
(S&P 500 @ 1960 //
-0.04%)
(Brent Oil^ @ 112.55 //
-0.66%)
(Gold^ @ 1327 //
+0.83%)
(10 yr Treasury^ @ 2.52 // -1
bp)
^ - Change from previous day's 5:30 GMT to 05:30
GMT

Macro Strategy (J. Reid, N. Burns, A. Ip)

I'll be honest and say that yesterday's EMR was a bit of a daze. I had a belated party for my 40th on Saturday and spent virtually the entire Friday night awake with my builders trying to put a house back together that has been owned by the builders for 8 months. I had 15 people there until 4am Friday night with 3 of them working non-stop until the first guests arrived at 230pm. Never have I been so stressed and tired. So all day Sunday and Monday morning were a bit of a daze. Sadly I'm now back living with builders again as they finish things off after the party. It was blissful for the few hours we were apart. At least we've moved out of the kitchen where we were living and sleeping for nearly 5 months before last week. Hopefully by the time the second half of the year ends I'll never have to see a builder again.

Anyway, the second half has now begun for markets and in our H1/Q2/June performance review today we show that most assets have had a positive year so far. So much so that if the year eventually goes to penalties it will end up being a very poor second half showing in line with many of England's in recent years!! We briefly review the numbers at the end but all the data and charts are in the pdf of this document. Its pretty rare to have almost all main global assets in positive territory this far into a year. Central bank liquidity continues to drive markets in our opinion which has helped this

synchronised uplift in valuations. However we can't help sensing that there's less joy over these returns than might be expected. Investors are worried about valuations in numerous assets and worried that the Fed might become more hawkish soon. There's little chance of the ECB following suit anytime soon though and European Government bonds have had a very good 2014 so far.

Over the last month we've again highlighted how many European Government bond markets have hit multi-century, all time yield lows. Well yesterday it was the turn of the Dutch 10 year yield to go through it's all time low again. The Dutch series is where we have our longest history of any government bond market with data going back to 1517 spanning almost half a millennia. The graph is in the pdf today and further shows just how unique the current situation is. The level of uncertainty about how this all ends must by definition be very high given this.

So as we start H2, Asian markets are trading with a stronger tone this morning helped by a solid start to the global manufacturing PMIs. The official Chinese manufacturing PMI printed at 51.0, in line with consensus and at a six month high. The final HSBC Chinese manufacturing PMI came in at 50.7, slightly below the flash reading of 50.8, but this is also the highest print of the year. The PMIs for other Asian bellwethers including Indonesia and Taiwan were also up on a month-to-month basis. The Nikkei (+1.2%) is the clear outperformer today, on decent volumes and despite a drop in the Japanese Q2 tankan manufacturing index to 12 from 17 previously and

15

expected. The capex component of the Tankan survey was above expectations however (+7.4% vs 6.0%) expected, which is strongest rate of growth since 2007. This has helped USDJPY (+0.1%) today. Outside of Japan, activity has been subdued with Hong Kong markets shut for July 1st holidays. The Indonesian rupiah is poised to record its strongest three-day rally in about fourth months – spurred by comments last week from the Bank of Indonesia that the country's trade balance returned to surplus in May. The AUDUSD is also poised for a solid gain (+0.25%) after the RBA maintained its neutral tone in today's policy meeting.

The last trading day of 1H14 failed to bring with it any volatility associated with month-end and half-end portfolio rebalancing. Indeed, yesterday's S&P 500 volumes were about half that compared to the last trading day of 1H13. Adding to that, the S&P 500 closed virtually unchanged at -0.04%, and for the record the last time we saw a gain or loss of more than 1% in the index was April 16th. One theme to note though was the continued underperformance of European banks across the equity and credit spectrum. Yesterday's underperformance was sparked by a 17% fall in the stock of Banco Espirito Santo which is Portugal's largest bank. The price action was dictated by reports that regulators were concerned over corporate governance between the bank and other related companies and there were also reports that Luxembourg justice authorities had launched an investigation into one of the bank's holding companies (Reuters). Portuguese securities regulator banned naked short selling on the bank's stock for one day. The news weighed on

Portuguese bond yields which added 8bp, and also on European banking stocks in general (-0.75% vs Stoxx 600 -0.09%). Peripheral bank credit traded about 3-5bp wider yesterday - and the European senior financials index (+2bp) underperformed Main (+1.375bp). The two credit indices were trading flat to each other in the middle of June but the recent underperformance of banks has pushed the basis back to nearly 6bp. We still think its likely that Fin Senior will trade through Main in H2 though.

Across the Atlantic, there was focus on the Chicago PMI and home sales data, following which treasury yields spiked up briefly before retracing the move to be largely unchanged on the day. The US Chicago PMI was slightly below expectations 62.6 (vs 63.0 expected) and also below last month's 65.5. Still, our economists note that the PMI was consistent with a large snapback in growth in Q2, and they noted the three-month to June average was 63.7 which is the highest since the three months to April 2011. The other regional activity indicator, the Dallas Fed manufacturing outlook rose to 11.4 (vs 8.5 expected and 8.0 prior). Pending home sales rose 6.1% MoM (1.5% expected) which benefited US homebuilders on the equity side (+1.5% yesterday). In terms of Fed speak, the SF Fed's Williams commented that a first rate hike in 2H15 will be appropriate, but he also reiterated that it may be optimal for the Fed to let inflation run above target in order to balance the Fed's dual mandate.

Perhaps one of the key themes of 1H14 was the surging M&A activity globally.

With 1H14 books closed, the final M&A tally was \$2.2trillion according to

Bloomberg which is a YoY increase of 77%. By region, leading the way was the

resurgence of corporate activity in Europe (+109% YoY), though this was

coming off a low base, followed closely by North America (+79%). In terms of

industry the biggest pickup in activity came in pharma (+677%) and healthcare

(+140%). One reason for the surge in M&A has been the accommodative capital

markets. We saw an example of that yesterday with a jumbo bond deal from

Oracle who priced \$10bn in bonds (the second largest USD offering in the

year-to-date according to Bloomberg) to fund the purchase of Micros Systems.

The deal was sufficiently large to drag other TMT bonds several basis points

wider on the day.

Looking at some of the geopolitical headlines, Ukrainian President Poroshenko

said late on Tuesday that we would end the cease-fire with pro-Russian rebels

and vowed to intensify military operations in the country's east. However the

president also made some concessions including guaranteeing Russian-language

rights and more regional autonomy. Russia also offered some concessions

yesterday including allowing Ukrainian and international observers in its own

border posts along the border with Ukraine. In Iraq, semi-autonomous Kurds

plan a referendum for independence according to a regional government

spokesperson (Reuters). The Kurds plan to keep control of the Kirkuk oil

fields.

There are some mixed headlines elsewhere in China. Firstly China's banking regulator announced a small change in the way that Loan-to-deposit ratios are calculated which our banking analysts think will reduce the system regulatory LDR ratio by 410bp based on end 2013 data. Our analysts think that this will pave the way for more relaxation of Chinese bank liquidity requirements. Secondly, the latest Macau gaming numbers were reported which showed June casino revenues fell 3.7% YoY in June. This is the first drop since 2009, but some are attributing this to the effects of the World Cup.

Turning to the day ahead, the rest of the global manufacturing PMIs/ISMs will be released starting with the final PMIs for Europe. The US manufacturing ISM is expected to show a small bump up to 55.9 (vs 55.4 in May) which would mark a six month high. DB is expecting a print of 55.0. Other highlights on the US data docket are May construction spending and the IBD/TIPP economic optimism index.

YTD performance
review

In YTD terms, of the main indices we track the FTSE-MIB (+14.5%) and the IBEX (+12.8%) have been the star performers. Spanish, Portuguese and Italian bonds have not been far behind. Interestingly commodities make up quite a few of

the other top ten places (with the CRB index, Gold, Silver and Oil returning between 7-11%), but also 2 of the worst 3 with Wheat and Copper both down more than 6%. Also negative was Chinese equities (-1.5%) after disappointing growth in H1 which may explain some part of the weakness for certain commodities. The Nikkei (-6.1%) was the only other asset lower YTD in our sample. Apart from these four all the other assets saw a positive 2014 total return. Credit has put in a good performance in 2014 so far with most major indices returning between 4-7% which is impressive in the low yield, low spread environment.

For the full numbers for the year, Q2 and June see the charts and tables in today's pdf. We also show the YTD numbers all converted to dollars.

Happy
H2!

Other Market
Data
(ITX Sen Fin @ 68 //
+2)
(ITX Sub Fin @ 103 //
+3)
(CDX EM @ 237 //
+4)
(ITX Japan @ 68 //
-1)
(ITX Australia @ 85 //
+2)
(ITX Asia XJ @ 105 //
unch)
(Euro NonSov @ 69.15 //

unch)
(Euro Corp @ 103 //
unch)
(Euro BBB @ 133.94 //
+1)
(Sterling NonGilt @ 115 //
unch)
(Sterling Corp @ 139 //
unch)
(Sterling BBB @ 176 //
unch)
(WTI Oil^ @ 105.65 //
-0.09%)
(Dollar Index^ @ 79.82 //
-0.27%)
(EUR/USD^ @ 1.369 //
+0.31%)
(DJ Stoxx 600 @ 342 //
-0.03%)
(NIKKEI @ 15332 //
+1.12%)
(Hang Seng @ 23191 //
0%)
(VIX @ 11.57 //
+0.31)

Key Economic Data

(Release // DB // Prev //
Con)
(ISM manufacturing (June) // 55.0 // 55.4 //
55.8)
(Construction spending (May) // +0.5% // +0.2% //
+0.5%)
(Unit motor vehicle sales (June) // 16.4M // 16.7M //
16.3M)

Topical Deutsche Bank Publications

* World Outlook - The calm before the storm, 25 June
2014,

http://pull.db-gmresearch.com/cgi-bin/pull/DocPull/1372-1896/72708206/-DB_Worl

d0outlook_2014-06-25_0900b8c0886ac28f.pdf

* FX Daily - The single most important question for policymakers, 24 June

2014,

<http://pull.db-gmresearch.com/cgi-bin/pull/DocPull/1361-CA65/71273754/0900b8c>

088677283.pdf

* European Staffing - Later than it seems, 25 June 2014,

http://pull.db-gmresearch.com/cgi-bin/pull/DocPull/2172-585C/72258420/-DB_FXDa

ily_2014-06-24_0900b8c0886c5a64.pdf

* European Equity Strategy - The return of the stock alpha, 20 Jun 2014,

<http://pull.db-gmresearch.com/cgi-bin/pull/DocPull/6-AB67/74847497/0900b8c088>

6acc70.pdf

* Focus Europe - Down but not out , 20 Jun 2014,

http://pull.db-gmresearch.com/cgi-bin/pull/DocPull/3055-5155/62173638/-DB_Focu

sEurope_2014-06-20_0900b8c0886840eb.pdf

Jim Reid [REDACTED] -

Nick Burns ([REDACTED]) -

Anthony Ip ([REDACTED]) -

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Tazia
Smith
Director | Key Client Partners -
US

DB Securities
Inc
Deutsche Asset & Wealth
Management
345 Park Avenue, 10154-0004 New York, NY,
USA
Tel. [REDACTED]
Fax [REDACTED]
Mobile +1 [REDACTED]
Email [REDACTED]

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