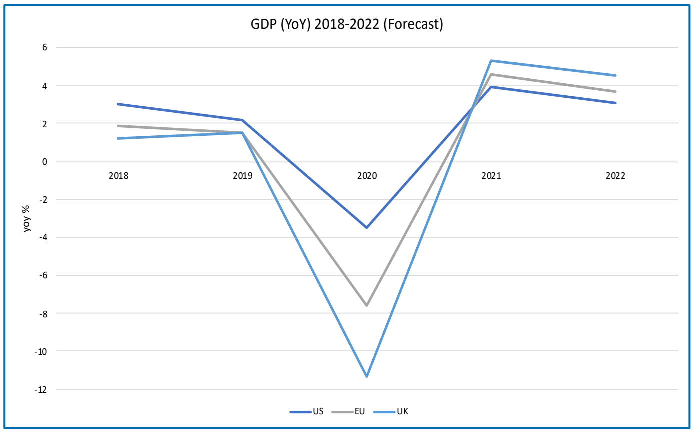
London Bridge Capital

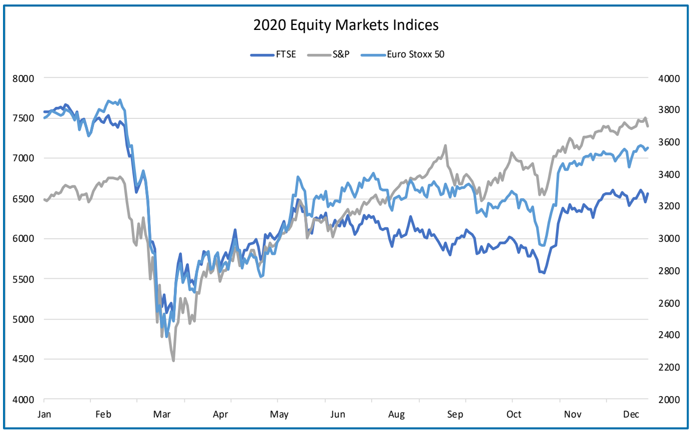
January 2021 Market Update

Executive Summary:

- 2020 was the year we all learned to Zoom, home schooled our kids, and got a dog- at least for the London Bridge Capital team!
- We start 2021 with buoyant markets delivering strong growth, an outcome that looked very unlikely in March last year. The US S&P 500 closed 2020 up 16% over the year. While UK & European stock markets finished below opening levels, momentum as the year closed was positive. The response of equity markets, despite rising COVID-19 infections, reflects the remarkable speed of development of COVID vaccines providing an eventual pathway out of the pandemic.
- However, institutional investors are focused on near term risks in H1-2021. New lockdowns and travel restrictions are impacting businesses and pushing back the point at which Governments can start to withdraw support.
- Utility & infrastructure issuers are always favoured but with continued low interest rates, investors are focused on relative value. As they seek to balance portfolios and generate returns, investors remain hesitant on the value of new deals.
- UK institutional investors have an appetite for targeted transactions, suited to their specific portfolio and see value in bilaterals which can impact their positions.



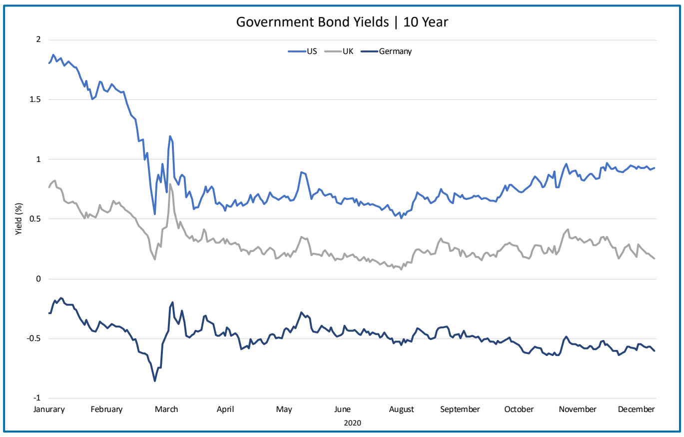
Source: Real GDP, Bloomberg Consensus Forecast data

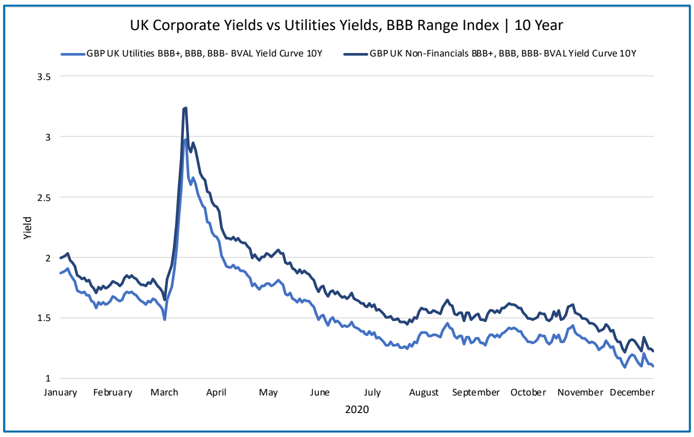


Source: Bloomberg

Credit Markets

- During 2020…
- Rates plunged as markets reacted to the impact of COVID on Europe and the US in March.
- Liquidity was key. Banks and capital markets, backed by Government and Central Bank support, made funds available. Global bond volumes increased 17% (IG) and 22% (NIG) in 2020 (vs 2019).
- While global bond issuance grew in 2020, the Sterling high grade bond market became more domestic. Issuance fell more than 15% mainly due to lower volumes from overseas issuers. UK investors seeking to meet their targets have increased their flexibility including becoming format agnostic, able to buy unlisted private placements, structured transactions, etc.
- Utilities and core infrastructure have remained resilient through the COVID-19 crisis (S&P December report: 75% of EMEA utilities' ratings remain with a stable outlook). However, ratings pressure is tangible. The investment dilemma for issuers, and their shareholders, is how to fund higher capex (in regulated networks and renewables) to meet net-zero carbon ambitions versus lower returns. Will we start to see greater investor differentiation for operational efficiency and sustainability strategies? Quite possibly.
- For investors, how an issuer approaches long term capital structures is important, overlayed with tactical positioning of issuance to meet lower regulatory cost of debt measures.
- We anticipate that global bond market volumes will shrink significantly in 2021 – not only when compared with record issuance in 2020, but also versus recent years.





Source: Bloomberg

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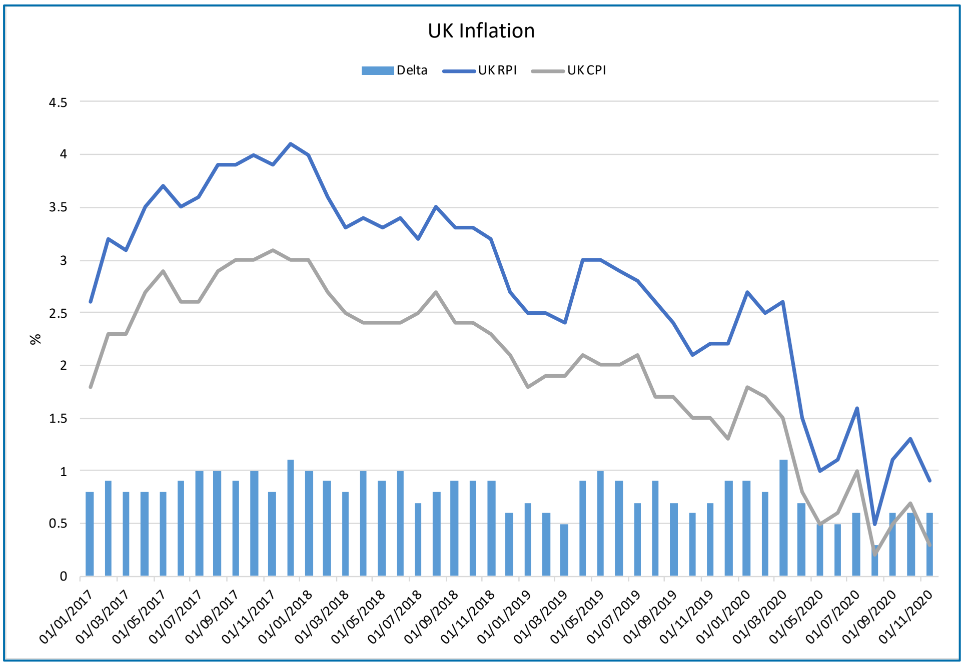
Inflation Issuance

- 2020 finally saw closure of the UK RPI/ CPI debate, with HM Treasury (HMT) no doubt keen to crystalise the expected £100bn saving as COVID costs explode.
- The need to move the UK's prime measure of inflation from RPI to CPI has long been agreed by markets. The challenge is how and when. In March 2020, HMT and the UK Statistics Authority issued a consultation and provided market participants with the opportunity to input their thoughts.
- With the publication of HMT's response in November, we now know that RPI will become CPIH in 2030; that date in the Chancellor's view means the change can progress without compensating bond holders.
- The market will gradually adjust towards a new equilibrium, and now we have clarity, investors are keen to see new issuance given the lack of available deals over the last year.
- Corporate (& Sovereign) new issuance in 2020 was notably low, we have observed investor demand and so expect increased issuance in 2021.



Source: Bloomberg

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