Bond Analysis: Barclays PLC 8.0% Perpetual (2029 Call) (6M 2023)

VMWM Research | October 27, 2023

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- **Bond Recommendation:**

Conservative Risk Appetite: UNDERWEIGHT

Moderate Risk Appetite: OVERWEIGHT

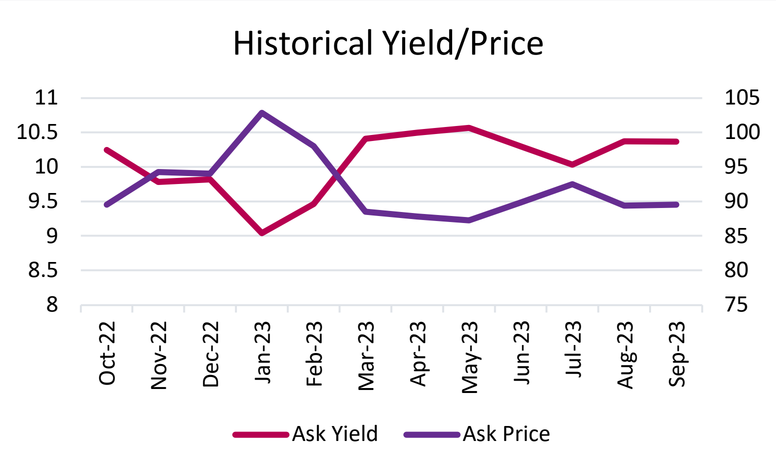
Aggressive Risk Appetite: OVERWEIGHT

ABOUT THE COMPANY

Barclays PLC (BACR) is a British multinational investment bank and financial services company. Its origins can be traced back to 1690 in London. Barclays has a global presence, offering a wide range of services in retail, wholesale, and investment banking, along with wealth management, mortgage lending, and credit cards. It has operations in over 40 countries and holds significant positions in Europe, the US, Africa, and Asia.

The company is listed on the London Stock Exchange and is a constituent of the FTSE 100 Index, indicating that it's one of the largest companies by market capitalization listed on the exchange. It has also had a secondary listing on the New York Stock Exchange. Barclays, like other major banks, is navigating a landscape of increased regulation, the impacts of the COVID-19 pandemic on the financial industry, and the digital transformation of banking services, which includes adapting to new technologies and increasing competition from fintech companies.

Barclay's PLC: Bond Term Summary	
Parent Company	N/A
Issuer	Barclays PLC
Currency	USD
Issued Amount	2,000,000 (M)
Issue Date	08/08/2022
Tenor	Perpetual/Call
Yield to Worst (As of October 26, 2023)	10.911
Coupon	8.0000%
Issuer Credit Rating (S&P)	BBB+
Outlook (S&P)	Stable
Maturity Type	Perpetual/Call Next Call date: 3/15/2029
Maturity	Perpetual/Call
Day Count Basis	30/360
Use of proceeds	General Corporate Purposes; Bail-in; Basel III Additional Tier 1



Recommendation: BACR's diversified global presence ensures resilience in various economic climates. Recent performance reflects 2.4% year-on-year income growth, enhanced cost efficiency (cost-to-income ratio reduced to 60.0%), and a robust capital and liquidity position (CET1 ratio at 13.8%, LCR at 158.0%). Furthermore, upgraded issuer ratings signify financial stability. With an attractive coupon of 8.0% and yield of approximately 10.9% yield to worst (YTW), the BACR 8.0% Perpetual Bonds compare favourably to peers and present a compelling opportunity that aligns with current market conditions.

ECONOMIC OVERVIEW (UNITED KINGDOM)

The United Kingdom (UK) generated the most revenue for BACR in 2022, with the Group earning close to 59.7% of its net revenues from that jurisdiction, according to Bloomberg. On April 21, 2023, S&P Global Ratings (S&P) revised the outlook on its unsolicited 'AA' long-term foreign and local currency ratings on the UK to Stable from Negative. It affirmed the 'AA/A-1+' unsolicited long- and short-term foreign and local currency sovereign ratings. The Stable outlook reflects the UK's stronger recent economic performance and more contained budget deficits over the next two years. S&P now expects only a shallow economic contraction of 0.5% in 2023, while the government's supply-side policy measures and improving relations with the EU should support medium-term growth prospects, despite existing structural constraints. This is balanced against risks stemming from the UK's still-constrained fiscal position, characterized by elevated general government debt amid higher interest rates and possible spending pressures given the upcoming general election (due January 2025 at the latest). Under S&P’s projections, general government debt should modestly decline from 2024 but the primary budgetary position should remain in deficit through 2026.

SIX MONTHS ENDED JUNE 30, 2023 (6M23)

GBP (In Millions)	FY 2020/21	FY 2021/22	6M22 June 30, 2022	6M23 June 30, 2023
Total income	21,940	24,956	13,204	13,522
Total operating expenses	14,659	16,730	9,127	8,062
Net profit	6,205	5,023	2,475	3,111
Return on average tangible shareholders' equity	13.1%	10.4%	10.1%	13.2%
Trailing 12 Months Net interest margin	1.07	1.33	1.13	1.44
Cost-to-income ratio	67.0%	67.0%	69.0%	60.0%
Net Loans	361,451	398,779	398,779	401,405
Total assets	1,384,285	1,513,699	1,589,230	1,549,714
Common equity tier 1 ratio	15.1%	13.9%	13.6%	13.8%
Liquidity coverage ratio	168.0%	165.0	156.0%	158.0%
Net stable funding ratio	N/A	137.0	N/A	139.0%

For the six months ended June 30, 2023, BACR’s Group Total Income grew to GBP 13.5 billion compared to the GBP 13.2 billion recorded in the previous year for the same period. This represents an increase of 2.4% year-on-year (YoY) and was driven primarily by a 16.0% increase in income from Barclays UK, driven by net interest income growth from higher rates, including continued structural hedge income, partially offset by product dynamics in deposits and mortgages. Income from the Consumer, Cards and Payments segment also grew, reflecting higher balances in US cards, growth in client assets and liabilities, and higher rates in Private Bank. This was partially offset by a 10.0% decline in the Corporate and Investment Banking segment, reflecting lower client activity in Global Markets and Investment Banking fees. Income from Barclays International declined by 2.0%.

Group Total Operating Expenses for the period declined to GBP 8.1 billion, down 12.0% YoY from the GBP 9.1 billion recorded in the previous year as some Litigation and conduct charges from the previous year were not repeated. Net Profit grew to GBP 3.1 billion from GBP 2.4 billion in the previous year, representing an increase of 25.0% YoY as overall performance benefited positively from the non-recurrence of the previously mentioned Litigation and conduct charges.

Improvement in Net Profit resulted in a higher Return on average Tangible Shareholders' equity (RoTE) of 13.2% compared to the 10.1% recorded in the previous year. This indicates that the Group was more efficient in generating profits from its tangible equity base in the current year. The Cost-to-income ratio also showed improvement, falling to 60.0% from 69.0%. The cost-to-income ratio is a financial metric used to evaluate the efficiency of a company or organization in managing its operating costs relative to its income or revenue. It is calculated by dividing the total operational costs or expenses by the total income or revenue generated by the Group. This reduction in the cost-to-income ratio is generally viewed as positive because it suggests that the Group has become more efficient in controlling its expenses relative to its revenue, which can contribute to higher profitability.

During the period, BACR sustained strong balance sheet ratios such as a Common Equity Tier 1 (CET1) ratio of 13.8% and a Liquidity Coverage Ratio (LCR) of 158.0%, which remain robustly above Basel III requirements. The CET1 ratio is a critical regulatory capital ratio used to measure a bank's financial strength and capital adequacy. It represents the proportion of a bank's core equity capital (common equity) to its risk-weighted assets. In this case, BACR has a CET1 ratio of 13.8%, which indicates that the bank has a solid capital base compared to its risk-weighted assets. The LCR is another important regulatory ratio for banks. It measures a bank's ability to meet its short-term liquidity needs by holding sufficient high-quality liquid assets. A Liquidity Coverage Ratio of 158.0% means that BACR has more than enough liquid assets to cover its short-term obligations.

The Net stable funding ratio remained robust at 139.0% after becoming a newly implemented measure towards the end of 2022. This ratio is also above the minimum requirements stipulated under the Basel III Framework. The Net Stable Funding Ratio is a financial metric used in banking to assess a bank's long-term liquidity and ability to meet its funding needs over a year. It measures the proportion of stable funding sources (such as long-term deposits and capital) to the amount of stable assets (such as loans and investments) a bank holds. A ratio of 139.0% indicates that the bank has more than enough stable funding to cover its stable assets, which is generally seen as a positive sign. It suggests that the bank is well-prepared to meet its long-term funding needs.

OUTLOOK

Diversified Business Model Supports Adequate Future Performance

BACR's diverse international banking franchise provides resilience in challenging economic conditions. Our assessment recognizes its leading market positions, diversified franchise, and strong track record in strategic execution and stable earnings. The Group follows a two-division model: Barclays UK and Barclays International. This approach, prioritizing the UK and the US, results in a balanced revenue base. As a significant UK incumbent bank, BACR holds substantial market shares, particularly in credit cards. Despite competition and economic volatility, Barclays UK has cautiously grown its loan portfolio and accumulated significant deposits, ensuring a solid income outlook. Barclays International bolsters the bank's stability through diversification. Even in turbulent economic conditions, BACR has shown earnings resilience thanks to its consistent strategy and effective execution. Although it faced notable conduct and litigation charges last year, these were absorbable through earnings, with many legacy legal and regulatory matters resolved. In summary, BACR's diversified international presence, strong market position, and strategic focus position it well to weather economic and financial challenges, ensuring stability and resilience in its operations.

Earnings Expected to Improve Over the Years and Capitalization to Remain Stable Despite Increasing Payments to Shareholders

BACR's earnings outlook for the rest of 2023 is positive. Strong revenues in the first six months are expected to persist throughout the year, driven by rising interest rates that have boosted net interest income. S&P also anticipates a resilient 2023 for BACR's earnings, with a projected Net Interest Margin (NIM) of approximately 1.5% for the full year, up from 1.33% in 2022. Non-interest income is expected to remain stable, contributing to a solid year-on-year earnings improvement. However, provisioning costs and expenses are set to increase over the next two years. Operating expenses are projected to grow in the mid-single digits in 2023, and credit losses are expected to widen in 2023. Despite this, the increase in credit costs is manageable for BACR because the Group maintains a robust capital position, which bolsters its ability to absorb credit losses. A CET1 ratio of 13.8% at the end of June 2023 is comfortably above the minimum regulatory requirement of 11.4% in its main jurisdiction. The slight decrease in the CET1 from the end of 2022 is primarily due to dividends, share buybacks, solid Risk-Weighted Asset (RWA) expansion, and other factors. Nevertheless, the Group continues to generate a strong CET1 capital buffer in the first half of 2023, indicating its ability to operate within its target CET1 range of 13%-14% over the next two years.

Post-Pandemic Asset Quality Should Continue Under the Group's Proactive Risk Management Practices
Barclays faces ongoing challenges due to exposure to volatile markets and riskier lending practices. While the Group maintains firm capital reserves and prudent risk management practices, it grapples with losses in areas like leveraged finance. Mortgage lending is a significant part of its business, and there are concerns about its higher exposure to consumer credit. The Group also engages in derivatives and traded products, which bring market and counterparty risks, interest rate and foreign exchange risks. Managing large employee pension schemes adds another layer of complexity. Notwithstanding, BACR is actively implementing tighter controls to mitigate risks, especially regarding securities over-issuance. However, its outlook remains influenced by the evolving landscape of financial markets and lending practices. S&P underscores that BACR maintains conservative provisioning practices, actively manages its loan book to anticipate stress, and has well-diversified wholesale lending portfolios that support asset quality. These point to efforts to maintain an acceptable level of asset quality.

Funding And Liquidity are Balanced and Stable
BACR benefits from a diverse deposit base, which includes its granular UK retail and corporate franchise. Additionally, the Group has demonstrated its ability to access wholesale funding in various market conditions, strengthening its funding profile. S&P considers BACR's liquidity sufficient, supported by its substantial liquid asset portfolio and robust liquidity metrics. As of March 31, 2023, the bank's liquidity buffer exceeded the minimum regulatory requirement by £122 billion. This buffer primarily comprises 82% cash held at central banks and 18% in government bonds. Barclays' liquidity coverage ratio ranks favourably among European global systemically important banks. Similarly, its net stable funding ratio is positioned towards the upper end of the European peer group, according to S&P.

ISSUER RATINGS ANALYSIS

Standard & Poor's: BBB+/Stable
On May 19, 2023, S&P upgraded BACR's rating to 'BBB+' from 'BBB' while maintaining a Stable outlook. The upgrade reflects BACR's strategic execution of initiatives, international diversification, and cautious balance-sheet management. BACR's strategic and geographical diversification has borne fruit, enabling the Group to generate adequate earnings and maintain excess capital. At the same time, S&P believes BACR's balance sheet is in an adequate position to cushion an uncertain global financial environment. Its liquidity pool is dominated by central bank reserves and had a weighted average surplus of more than £100 billion throughout the first quarter of 2023. Alongside this, BACR's lending book is also in a strong position, with low nonperforming loan balances and close management of idiosyncratic pockets of risk. While overarching complexity and operational risk should continue to weigh on the Group's strengths, S&P has confidence that it can sustain the improved rating upgrade.

Moody's: Baa1/Stable
On March 20, 2023, Moody's upgraded BACR's rating to 'Baa1' from 'Baa2' while maintaining a Stable outlook. Moody's anticipates that the Group's earnings should exhibit increased strength, greater diversification, and enhanced sustainability compared to previous periods. Additionally, it foresees that asset risk should maintain its current stability, and capital and liquidity should remain robust. Nevertheless, Moody's suggests that BACR's profitability is expected to persistently lag behind that of most global peers. This

discrepancy is attributed to the superior scale, and market share these peers enjoy across various capital markets products. Furthermore, Moody's believes that in adverse market conditions or significant isolated charges, BACR's profitability is likely to be more profoundly impacted.

BOND RATINGS ANALYSIS

Standard & Poor's: BB-

In May 2023, as part of the simultaneous upgrade of the Issuer rating, the rating of the 8.0% Perpetual Bond was also raised from 'B+' to 'BB-'. However, it's important to note that the bond rating is lower than the issuer's. This rating discrepancy arises because the 8.0% Perpetual Bonds are categorized as Junior Subordinated debt in the creditor hierarchy. In a company's capital structure, different types of debt securities have varying levels of seniority when it comes to repayment in the event of financial distress or default. Senior debt holders are typically higher in the hierarchy and have a greater claim on the company's assets and cash flows than junior or subordinated debt holders. The 'BB-' rating for the 8.0% Perpetual Bonds indicates they are of lower credit quality than the overall issuer. This lower rating signifies that, in the event of financial difficulties or bankruptcy, holders of the 8.0% Perpetual Bonds may have a lower priority in receiving repayment than holders of higher-ranked debt securities issued by BACR.

COMPARABLES ANALYSIS

When compared to peers of a similar S&P credit rating, the coupon on BACR 8.0% Perps is higher than the peer average of other Perpetual bonds in the space. The BACR 8.0% Perps also have the most attractive yield to worst (YTW) at approximate 10.9%, as calculated by Bloomberg. We assessed the YTW calculated by Bloomberg because it considers the possibility of the bond being called at the earliest callable date. The BACR Perps also have the most distant upcoming call date.

Issuer	Barclays PLC (BACR)	Societe Generale (SOGGEN)	Lloyd's (LLOYDS)
Bond Ratings (S&P)	BB-	BB	BB-
Bond Issue	BACR 8 PERP	SOCGEN 7 ⅞ PERP	LLOYDS 6 ¾ PERP
Indicative Yield to Worst (%)	10.911	9.299	9.995
Coupon Rate (%)	8.000	7.7875	6.750
Amount Outstanding ($)	2,000,000,000	1,750,000,000	500,000,000
Country of Risk	UK	FRANCE	UK
Currency	USD	USD	USD
Maturity type	PERP/CALL	PERP/CALL	PERP/CALL
Next Call Date	3/15/2029	12/18/2023	6/27/2026

Source: Bloomberg (October 26, 2023)

INVESTMENT POSITIVES

1. **Diversified Business Model:** Barclays' diverse international banking franchise provides resilience in challenging economic conditions, with leading market positions and a balanced revenue base between Barclays UK and Barclays International. This diversification can help mitigate risks and stabilize earnings.
2. **Strong Earnings Growth:** For the half-year ending June 30, 2023, Barclays Group experienced a 2.4% year-on-year growth in total income and a 25.0% year-on-year increase in net profit. This suggests positive momentum in earnings performance.
3. **Improved Efficiency:** Barclays showed improved efficiency with a lower cost-to-income ratio, falling from 69.0% to 60.0%. This indicates better cost control and potentially higher profitability.
4. **Robust Capital Position:** Barclays maintains a strong Common Equity Tier 1 (CET1) ratio of 13.8% and a Liquidity Coverage Ratio (LCR) of 158.0%, which are comfortably above regulatory requirements. This indicates a strong capital base and the ability to meet short-term liquidity needs.
5. **Stable Issuer Ratings:** Both Standard & Poor's and Moody's upgraded Barclays' issuer ratings, indicating improved creditworthiness and financial stability.
6. **Attractive Bond Yield:** The BACR 8.0% Perpetual Bonds offer a higher coupon rate than peers with a similar S&P credit rating. Additionally, they have an attractive yield to worst (YTW) at approximately 10.9%, considering the possibility of an early bond call.

INVESTMENT NEGATIVES

1. **Economic Dependence on the UK:** Barclays generated a significant portion (close to 59.7%) of its net revenues from the United Kingdom. This concentration of revenue in a single jurisdiction can expose the bank to risks associated with the UK's economic performance.
2. **Upcoming General Election:** The upcoming general election in the UK (due in January 2025 at the latest) introduces political uncertainty, and there may be potential spending pressures that could affect the bank's profitability.
3. **Asset Quality Challenges:** Barclays faces ongoing challenges related to exposure to volatile markets, riskier lending practices, and concerns about its consumer credit exposure. These challenges can affect the bank's asset quality.
4. **Increasing Expenses:** While Barclays has improved efficiency, it is projected that operating expenses will grow in the mid-single digits in 2023. This could potentially impact profitability.
5. **Potential Market Volatility:** Despite resilience, Barclays' earnings are subject to market volatility, and there are risks associated with market conditions, especially in areas like leveraged finance and derivatives.
6. **Bond Rating Lower Than Issuer:** The bond rating of the 8.0% Perpetual Bonds is lower than the issuer's rating because they are classified as Junior Subordinated debt, implying a lower claim in case of financial distress or default. This lower bond rating suggests higher credit risk for bondholders.

CONCLUSION

BACR's diversified global presence ensures resilience in various economic climates. Recent performance reflects 2.4% year-on-year income growth, enhanced cost efficiency (cost-to-income ratio reduced to 60.0%), and a robust capital and liquidity position (CET1 ratio at 13.8%, LCR at 158.0%). Furthermore, upgraded issuer ratings signify financial stability. With an attractive coupon of 8.0% and yield of approximately 10.9% yield to worst (YTW), the BACR 8.0% Perpetual Bonds compare favourably to peers and present a compelling opportunity that aligns with current market conditions. Therefore, we recommend that investors consider buying BACR 8.0% Perpetual Bonds for their strong appeal as follows:

Conservative Risk Appetite: UNDERWEIGHT (Due to the Perpetual bonds being consider Junior Subordinated Debt)

Moderate Risk Appetite: OVERWEIGHT

Aggressive Risk Appetite: OVERWEIGHT

SOURCES

BACR COMPANY WEBISTE, BACR COMPANY FINANCIALS, BACR SECOND QUARTER MD&A DOCUMENT, REUTERS, FITCH RATINGS, BLOOMBERG, OPPEHNHEIMER & CO., STANDARD & POORS, MOODY'S INVESTOR SERVICES

DEFINITIONS

- **OVERWEIGHT** - Security is deemed to be undervalued and is expected to outperform compared to the average market return and/or return of comparable securities in the same sector or industry.

- **MARKETWEIGHT** – Security is expected to provide similar returns compared to the market in general or at the same pace as comparable companies; neither strongly positive nor negative.

- **UNDERWEIGHT** – Security is deemed to be overvalued and is expected to underperform compared to the average market return and/or return of comparable securities in the same sector or industry.

- **ZEROWEIGHT** – This security is substantially distressed or at risk of a shock which may significantly impair its value.