credit £ secondary market liquidity

In this quarter's liquidity survey, opinion among sterling credit investors appears to be divided over how well banks are providing liquidity. According to one respondent: "Liquidity is still poor. The Street appears to be slightly short credit and this is despite a pick-up in issuance. This reflects the strong demand in the sterling market, which implies that liquidity is unlikely to improve any time soon."

And yet another respondent says: "Liquidity is reasonably good at the moment. People have learnt the lesson from last year that if there is no liquidity every one gets hurt. Banks are making much more effort than six months ago in a difficult environment."

However both statements can be justified. Liquidity has improved substantially since the market practically froze this time last year, when Paul Mingay, Morley Fund Management's head of credit, felt compelled to write a letter to the investment banks criticising their reluctance to provide liquidity. Nevertheless the market is still far from liquid. And investors are worried liquidity will disappear once again if volatility returns or new issue levels fall – new issues give investors an incentive to shuffle their portfolios and sell older bonds into the market.

As one investor says: "Given the strong investor demand for credit, banks have been able to provide better liquidity. When the market turns, it will be interesting to see who will step up to the plate."

There are however some signs of improvement. One survey participant received a call this month from a consultant asking what a bank should provide in order to become a market maker in sterling corporate bonds (answer: commitment to pricing). The bank is likely to be ABN Amro, which has been hiring in trading and debt capital markets people to cover the sterling market.

Further encouragement, at least in the short term, is that spreads on bonds in the sterling market are now so tight that the market is beginning to see investors looking to sell. The key cause of illiquidity in the bond market is not that banks are not prepared to throw their balance sheets at providing it but that investors are all trading in the same direction.

Less encouraging is the fact that the bookrunner league table for sterling corporate bonds over the past three months shows that a number of banks are bringing bonds to market while scoring poorly in providing liquidity. ■

1. Which bank provides the best secondary market liquidity for *deals that it has brought to market*?*

	Total	Number of Firsts	Seconds	Thirds	Fourths	Fifths
1 UBS	**70**	9	3	3	2	0
2 Royal Bank of Scotland	**53**	4	2	6	3	1
3 Morgan Stanley	**49**	1	6	5	2	1
4 Barclays Capital	**48**	3	5	1	3	4
5 HSBC	**24**	2	1	1	2	3
6 Royal Bank of Canada	**21**	0	3	2	1	1
7 Citigroup	**10**	0	0	1	2	3
8 JPMorgan	**9**	1	0	0	2	0
9 Goldman Sachs	**7**	0	0	1	2	0
10 Credit Suisse First Boston	**3**	0	0	0	0	3

2. Which bank provides the best secondary market liquidity for *all bonds*?*

	Total	Number of Firsts	Seconds	Thirds	Fourths	Fifths
1 UBS	**66**	7	4	3	3	0
2 Morgan Stanley	**65**	7	5	2	1	2
3 Barclays Capital	**44**	3	2	5	3	0
4 Royal Bank of Scotland	**40**	0	3	5	6	1
5 HSBC	**22**	2	1	1	0	5
6 JPMorgan	**20**	0	1	2	3	4
7 Credit Suisse First Boston	**13**	0	1	1	2	2
8 Royal Bank of Canada	**9**	0	1	0	1	3
9 Citigroup	**8**	0	1	1	0	1
10 Goldman Sachs	**7**	0	1	0	1	1

*** for double-A to triple-B sterling corporate bonds**

Bookrunner league table*, ytd 2003

	Survey position†	Amount (£bn)	Number
1 Barclays Capital	4	3.5	29
2 Royal Bank of Scotland	2	3.0	29
3 Citigroup	7	1.6	15
4 HSBC	5	1.1	13
5 Deutsche Bank	11=	0.9	8
6 JPMorgan	8	0.8	8
7 Morgan Stanley	3	0.6	5
8 Goldman Sachs	9	0.6	5
9 UBS	1	0.6	4
10 BNP Paribas	11=	0.4	5

Bookrunner league table*, last 3 months

	Survey position†	Amount (£bn)	Number
1 Royal Bank of Scotland	2	1.6	12
2 Barclays Capital	4	1.3	7
3 Citigroup	7	1.0	9
4 HSBC	5	0.4	4
5 Goldman Sachs	9	0.4	3
6 Deutsche Bank	11=	0.4	2
7 JPMorgan	8	0.2	2
8 Merrill Lynch	13=	0.2	2
9 Lehman Brothers	15=	0.2	1
10 Société Générale	13=	0.2	1

* for double-A to triple-B sterling corporate bonds (excluding banks – public deals only)

† relates to Question 1 — ***Source: Dealogic Bondware***

Methodology

The 22 largest institutional investors in sterling corporate bonds are each allowed one vote – 20 firms participated this month. Firms were asked to designate the one person most qualified to respond – usually the head of sterling fixed-income trading. Voting was conducted via a secure website and respondents were asked to nominate their top five banks for each of the two questions. The results were aggregated – with five points awarded for a first place and one for a fifth place vote.

To keep the survey simple, only two questions are used:

1. With regard to *deals that it has brought to market*, which bank provides the best secondary market liquidity for sterling corporate credits rated in the double-A to triple-B range?

2. With regard to *all bonds*, which bank provides the best secondary market liquidity for sterling corporate credits rated in the double-A to triple-B range?

The aim of the survey is to provide issuers with an idea of which banks are most willing to support deals in the secondary market – and, by implication, which are not. ■