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BNP Paribas fine may have a silver lining for credit investors

The French bank should weather the near-\$9bn fine for breaching US sanctions with proscribed states – and may even be compelled to issue attractively-priced debt in response, says Filippo Alloatti, Senior Credit Analyst

Striking the balance: BNP Paribas will suffer under the record \$8.9bn fine dealt by US authorities for concealing \$30bn of transactions with clients in Sudan, Iran and Cuba. It amounts to a 90bps hit on the bank's balance sheet, taking its fully loaded, or Basel III ready, capital ratio at the end of Q1 to 9.7%. Factoring in Reuters' analyst estimates of €1.45bn in net income for Q2, the fine could subtract a further 20 bps in the absence of further action by management, such as asset sales.

Recovery move: Because French banks take pride in capital ratios of 10% or more, this may compel BNP Paribas to issue additional tier one (AT1) debt with the aim of restoring its common equity tier one (CET1). This would present a good entry point: empowered by strong earnings, and incentivised by its aim to replenish capital and be upgraded from ratings agencies negative-watch lists, BNP Paribas can offer an attractive yield. The fine may also prevent a dividend for shareholders, which would further appeal for credit investors.

Wiggle room: The ban on USD clearing that has also been imposed on the bank is harsher than expected. But it becomes effective in January 2015 – and affects limited activities such as oil and gas financing in Paris, Geneva and Singapore – allowing time to appoint another bank to act on its behalf in order for clients to gain access to USD financing. The bank was not forced to sell its US subsidiary, BancWest, which would have been deleterious to its wholesale business.

Looking ahead: The fine almost doubles the combined settlements that the Office of Foreign Assets Control, one of the US authorities imposing the penalty, has previously reached with banks. BNP Paribas' solid balance sheet and strong earnings, however, should enable it to bear the initial impact and any weakness in its USD clearing unit next year. Its penchant for an impressive capital ratio will also probably spur the issuance of new, attractive AT1 paper.

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