Morgan Stanley

MORGAN STANLEY RESEARCH

Morgan Stanley & Co.
International plc+

Financials Research

Jackie Ineke
Jackie.ineke@morganstanley.com
+41 (44) 220 9246

Lee Street
Lee.Street@morganstanley.com
+44 (20) 7677 0406

Credit Strategy

Andrew Sheets
Andrew.Sheets@morganstanley.com
+44 20 7677 2905

Serena Tang
Serena.Tang@morganstanley.com
+44 20 7677 1149

June 14, 2012

Europe

Investment Grade Credit

European Banks

Closing Out Our Tier 1 Underweight

Standing ahead of the 'Response' phase of our strategists' 'CRIC' (Crisis, Response, Improvement, Complacency) analysis, we close out the Underweight we've had on Tier 1 since February. In a sector whose limited liquidity has been further impacted over the last few months due to LME, we believe that we do not have the luxury of waiting for implementation of the expected final, credible recap of the Spanish banking sector before adding, and so we move Equal-weight.

Adding carefully in high-step Tier 1s: Although the average drop in prices in Tier 1s since February is around 10 points, this masks huge variation. We add Tier 1s which: i) have high coupons and high steps, as we are still very concerned about non-calls; ii) exhibit good relative value versus other Tier 1s; and/or iii) have underperformed. We cannot be choosy about singling out only IG bonds, as there are few left.

Buyers here are hedge funds and private individuals: We believe that both investor bases are looking for further falls in Tier 1 prices to step in and buy, which makes us think we simply won't see that move.

Liquidity is a double-edged sword, but with a more constructive short-term view, just a few buyers here should have a disproportionate impact on pricing. Remember that although dealer inventories are at their lows, if anything they'll likely have even less appetite for risk, as Moody's downgrades hit them in the coming days.

Remember swap gains? SocGen helpfully reminded us of the power of realising swap gains on bonds via tenders, with its recent LME on LT2. We include a table of Tier 1s with large swap gains, for example Abbey's $8.963% with 69 points of swap gains, due to the 2030 call. Due to the Santander ownership, we're hoping that very nervous short-term trading provides opportunities to buy.

Uncertainty remains over the nature and timing of the 'Response' phase – therefore a risk of additional near-term weakness, hence this move only from U/W to E/W. Significant additional weakness could open the way to move O/W at some point over the next few weeks.

Top Picks in Tier 1

Security	Offer	YTC (%)	YTP (%)	1yr high	1yr low
BPCEGP $ 12.5 19	97.0	13.1	14.3	120.0	92.0
BBVASM £ 9.1 14	71.0	27.3	12.3	101.0	68.0
SANTAN £ 11.3 14	87.5	19.0	12.2	108.5	85.0
ISPIM € 8.375 19	76.5	13.6	11.8	103	57.5
BBVASM € 8.5 14	79.0	20.6	10.6	104.0	78.5
ISPIM € 8.047 18	75.0	14.6	9.9	101.0	54.5
BPCEGP € 9 15	83.0	17.2	10.8	104.0	66.0
BNP $ 7.195 37	84.0	8.8	8.0	98.5	69.0
BPCEGP €9.25 15	82.0	17.8	11.3	103.8	65.5

Source: Bloomberg; Morgan Stanley Research; Indicative offer levels on June 14, 2012

European Banks

Closing Out Our Tier 1 Underweight

Over the last three months, Tier 1 has been an illiquid, poorly performing sector plagued by uncertainty over banking regulation and sovereign risk. All are reasons we are now moving the sector from Underweight to Equal-weight. Poor performance, after all, means higher risk premiums. Poor liquidity, in turn, means that we cannot be *too* choosy in timing the market.

This leaves political and regulatory uncertainty. Long-term issues remain, of course, but in the near term we see improvement. Moody's downgrades of the European banking sector are now well advanced and have been somewhat less severe than our (bearish) assumptions. What has been reported of Spain's bank aid package points to a sufficient size to be credible, and sufficient leniency to be workable. While we don't pretend to know the results of this weekend's voting in Greece, there are a number of plausible results that could assuage the worst of market fears, at least temporarily.

At both the sector and strategy level, we'd stress that our more positive view doesn't apply universally: Tier 1's weakness has been uneven, leaving some bonds with highly attractive yield-to-worst, and others sitting uncomfortably at the top of their 52-week range. In this note, we look at the level of repricing in more detail, discuss why poor liquidity means we don't want to be too choosy in flattening our view, and finish with a discussion of the division of bonds in the sector between those we like, and those we don't.

What Does History Say about 'When' to Buy Tier 1?

Before we delve into the specifics of the financial Tier 1 sector, we first need to establish that perfect timing should not, and cannot, be our goal. Volatility in the sector has kept bid/offer wide and dealer inventory low, while low dealer inventory has made prices liable to 'gap' (boosting volatility). This vicious cycle suggests that the price histories we see in the sector are more theoretical then practical. Even if you are wise enough (or lucky enough) to time the bottom of Tier 1 prices perfectly, you cannot expect to actually pick up much paper there.

This problem becomes more acute in the context of our strategists' 'CRIC' framework, where the current 'Crisis' stage is set to invite 'Response' (see *Cross-Asset Strategy: Negative Reinforcement*, June 1, 2012) It is difficult enough adding Tier 1 at quoted levels when dealer inventories are low and bid/offer is wide. In our view, it's likely to be near impossible following a policy response strong enough to drive broad-based buying.

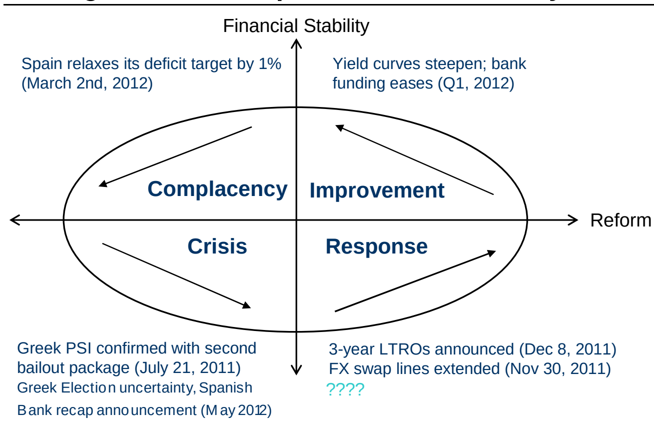
Exhibit 1

Liquidity Challenged: EUR Tier 1 Bid/Offer, in Points

Source: Markit iBoxx, Morgan Stanley Research

Exhibit 2

Moving Towards 'Response' in the 'CRIC' Cycle



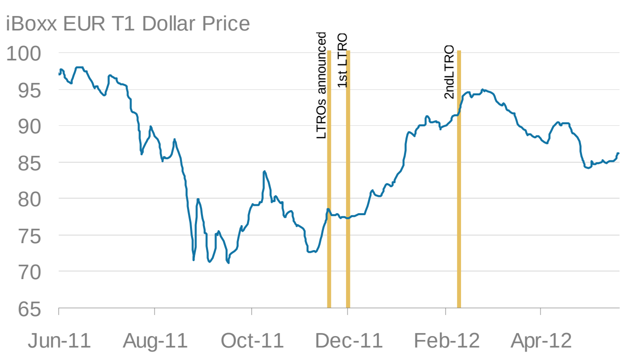
Source: Morgan Stanley Research

Over the past couple of months, even in a risk-off market, Tier 1 bonds normally trade in €1-2 million sizes, with those where you can build up a €20 million position (over at least a week) few and far between. This illiquidity has been compounded by the spate of liability-management exercises (LMEs) which have taken any tradeable bonds out of the market. To this point, **since November 2011, 101 Tier 1 issues have been subject to LMEs, with €47.5 billion tendered for, and €23.0 billion actually tendered.** With the average premium in Tier

1 LME 9.6 points, it's unsurprising that any investor with an ability to trade has been tempted to sell/exchange – leaving the stickier holders with the rump issues.

All this suggests that we'll need to close our Tier 1 Underweight well before policy certainty. Can this work? We find some encouragement in the price action of the sector surrounding the recent LTROs. In Exhibit 3, we plot the average price of the EUR Tier 1 index, noting key dates in the announcement and implication of the ECB's operations.

Exhibit 3
EUR Tier 1 Prices Around the LTROs



Source: Markit iBoxx, Morgan Stanley Research

Tier 1s rallied hard when the LTRO was announced (from 73 to 77). Thereafter, the sector moved sideways for a month before the next 15 points of price appreciation. To be fair, the chart suggests that buying almost any time between September and November was the right call, but buying in late December wasn't too bad either, in the grand scheme of things. Here's where we get down to practicalities though. To have bought in late December, and buying in any size – in almost any class of credit – would have been somewhat challenging, to say the least. For Tier 1s, this was not only nearing the financial year-end, but was in the midst of the first onslaught of LMEs which, as we noted above, averaged a 9.5 point premium. We're left wondering exactly how much liquidity was really at hand in that period.

Again, we'd love to hang back and move up to Equal-weight on this sector right at the point 'Response' is finally unleashed on the market – but we simply don't believe that the offer would be where it was on the screen five minutes prior to that 'Response', and certainly in any decent size. This goes far more for Tier 1 than any other class of bank bonds – hence our move today. Such liquidity problems also dictated why we went Underweight Tier 1s in February, in what seemed to be the midst of a continuing rally – because we need a real rally to ensure that there are plenty of bids.

An Uneven Sell-Off

Another factor complicating the question of adding back Tier 1 risk is the highly uneven nature of the sell-off. Average prices have fallen ~10pts, but this hides a wide degree of variation within the weakness. Taking a closer look at the (dwindling) universe of € Tier 1 bonds that make up this index, we plot the 52-week price history and where they current sit on this range. Bonds, quite literally, are all over the place.

Exhibit 4
Performance Has Varied Greatly Across the Index

Ticker	Cpn	Call	Price History	0% 50% 100%
ACAFP	8.200	Mar-18		
ACAFP	7.875	Oct-19		
BACR	4.875	Dec-14		
BACR	4.750	Mar-20		
BNP	8.667	Sep-13		
BNP	4.730	Apr-16		
BNP	5.019	Apr-17		
BNP	7.781	Jul-18		
BPCEGP	9.000	Mar-15		
BPCEGP	9.250	Apr-15		
BPCEGP	6.117	Oct-17		
DANBNK	4.878	May-17		
DB	5.330	Sep-13		
DB	9.500	Mar-15		
DB	8.000	May-18		
FBAVP	4.625	Oct-14		
MTFG	4.850	Jul-16		
MTFG	5.271	Jan-17		
NYKRE	4.901	Sep-14		
NYKRE	9.000	Apr-15		
SEB	9.250	Mar-15		
SEB	7.092	Dec-17		
SHBASS	4.194	Dec-15		
UBS	4.280	Apr-15		
UBS	7.152	Dec-17		

Source: Markit iBoxx, Morgan Stanley Research

Adding Selectively in Tier 1

As shown in Exhibit 4, many parts of the Tier 1 sector have hardly sold off. The world is a riskier place since our sector downgrade in February (see *Tier 1s: Moving Underweight*, February 8, 2012), with peripheral spreads higher, and Morgan Stanley growth forecasts lower. Ratings downgrade risk continues to hover over the sector. All this suggests that our buying should be selective. We have three goals:

- **Focus on high-step Tier 1s:** We are still very cautious on calls, with our view being that non-called low-step Tier 1s represent cheap perpetual Tier 2 under CRD4. Further, with the draft Crisis Management Directive (CMD) calling for a certain level of 'bail-inable' debt for all banks, again, non-called low-step Tier 1s can fulfill this role – potentially making it cheaper for banks to issue senior (as the buffer below senior is not diminished). Our preference for high coupons extends to retail Tier 1s, where they are expensive to leave outstanding.

- **Select underperformers with relative value:** Exhibit 5 shows some of the worst performers over the last three months, and indicates that the Spanish, Italian and French names are as much as 9.5-31.25 points off their recent three-month highs. While this is not sufficient for us to choose a certain bond, we'd rather be adding those trading marginally off their lows than close to their highs (Exhibit 6 shows one-year extremes). In terms of relative value, we believe that many LT2s still offer better risk/reward versus Tier 1s – particularly when looking at low-to-medium steps on a YTP basis.
- **Keep an eye on swap gains:** SocGen's recent and unexpected (coming so soon after the CMD called for more bail-in debt, not less) tender for LT2 bonds in order to capture swap gains reminds us that these are important, and often a key driver of LME.

Exhibit 5

Tier 1 Performance

Security	Offer*	Abs. change	% change	3m high
$				
BBVASM $5.919 17	60.0	22.00	26.8%	82.0
ACAFP $6.637 17	68.5	15.00	18.0%	83.5
SOCGEN $5.922 17	69.5	14.00	16.8%	83.5
LLOYDS $5.92 15	59.0	10.00	14.5%	69.0
LLOYDS $6.267 16	59.5	10.00	14.4%	69.5
LLOYDS $6.657 37	62.5	10.00	13.8%	72.5
ACAFP $8.375 19	82.0	13.00	13.7%	95.0
HBOS $6.071 14	64.0	9.50	12.9%	73.5
KNFP $10 18	81.0	12.00	12.9%	93.0
BNP $5.186 15	80.0	10.50	11.6%	90.5
£				
BBVASM £9.1 14	71.0	23.50	24.9%	94.5
ABBEY £5.827 16	63.0	16.00	20.3%	79.0
ACAFP £8.125 19	67.0	17.00	20.2%	84.0
ACAFP £5.136 16	59.0	13.50	18.6%	72.5
BNP £5.945 16	60.5	12.00	16.6%	72.5
ACAFP £7.589 20	64.0	12.50	16.3%	76.5
ABBEY £6.222 19	60.0	11.00	15.5%	71.0
SANTAN £11.3 14	87.5	15.50	15.0%	103.0
SOCGEN £8.875 18	71.0	12.50	15.0%	83.5
BACR £6 17	60.5	10.00	14.2%	70.5
€				
SNSSNS €6.258 17	40.5	24.00	37.2%	64.5
PMIIM €9 18	51.0	29.50	36.6%	80.5
PMIIM €5.483 12	51.0	28.00	35.4%	79.0
SNSSNS €11.25 19	59.0	31.25	34.6%	90.3
MONTE €6.997 12	56.0	21.00	27.3%	77.0
ACAFP €7.875 19	72.0	22.50	23.8%	94.5
BPCEGP €4.75 16	51.5	15.50	23.1%	67.0
CRLOG €2.021 12	50.0	15.00	23.1%	65.0
BPCEGP €5.25 14	64.0	17.50	21.5%	81.5
BPCEGP €6.117 17	62.0	16.50	21.0%	78.5

Source: Bloomberg, Morgan Stanley Research; *Indicative offer level as on June 14, 2012

As our Appendix shows, we really cannot hope to focus only on investment grade Tier 1s here. Even though a number should remain IG after Moody's reviews are over, most remain finely balanced on the cusp of HY. With sovereign and CMD-related downgrades to potentially follow, we have little confidence in expecting more than a handful to remain IG before the year is out.

Before moving to our preferred bonds, we would note that one of the drivers of our February move Underweight was a diminishing buyer base for this asset class. This concern remains, and while we cannot sweep forced sales over time due to HY status under the carpet, we would note anecdotally that many of the hedge funds we've visited over the past two months **all have 'buy lists' for Tier 1s,** if they take a lurch down. Further, recent presentations to Swiss-based advisers/private banks have unearthed many sophisticated private individuals simply waiting to pick up particular Tier 1s they like, in a worsening environment. This makes us believe we'll not actually reach the lows we saw in previous periphery crises. Neither of these buyer bases care about ratings, and while the former is clearly not a long-term holder, the latter is.

On the poor liquidity in the market, this can work both ways: When we're bearish, of course it's bad – and this is why we always knowingly jump the gun on any Tier 1 recommendation changes in particular. In this case, with a more constructive view, we believe that in time there will be very few offers on Tier 1 at all. Further, with very poor liquidity, any buying should have an amplified effect on pricing. Let's not forget that it's very unlikely any broker will be 'loading up' on Tier 1s at this point, even if they share our view, as most trading desks are naturally standing ahead of (possibly severe) Moody's downgrades.

Our focus: high steps/swap gains/CRD4 losers: Exhibit 6 highlights a number of bonds we'd look at to get us back up to Equal-weight Tier 1s (we appreciate the irony of this, with so many dropping to high yield, but at least our direction is clear).

The bolded bonds are our picks. The first section includes those with very high steps, where we have a good degree of confidence that they will be called. These are not cheap perpetual Tier 2 if left outstanding under CRD4 and they would not be cheap 'bail in' either, with newly issued Tier 2, or senior, doing the same job at a cheaper price. Here, we left out certain high-step bonds including $ KNFP, € Santan 10.5, £ NWIDE 7.589 (no liquidity at all), € SNS as it's a credit we have concerns about, € SocGen due to lack of value (YTC is just 11.8%) and ACAFP across the board due to a lack of relative value versus the Italians – and ahead of the Greek election.

Exhibit 6

Tier 1s – Top Picks in Bold and Select Other Tier 1s

Ccy	Ticker	Cpn	Next call	Amt o/s	Step	Offer	YTC (%)	YTP (%)	1yr high	1yr low	Reg par call	Swap gain
High steps: Call likely												
$	**BPCEGP**	**12.5**	**30-Sep-19**	**444**	**L+1,298**	**97.0**	**13.1**	**14.3**	**120.0**	**92.0**	**Par**	**17.6**
£	**BBVASM**	**9.1**	**21-Oct-14**	**251**	**L+ 570**	**71.0**	**27.3**	**12.3**	**101.0**	**68.0**	**Make whole**	**5.1**
£	**SANTAN**	**11.3**	**27-Jul-14**	**679**	**L+766**	**87.5**	**19.0**	**12.2**	**108.5**	**85.0**	**N/A**	**5.3**
€	**ISPIM**	**8.375**	**14-Oct-19**	**1,006**	**L+687**	**76.5**	**13.6**	**11.8**	**103.0**	**57.5**	**Make whole**	**12.3**
€	UCGIM	8.125	10-Dec-19	585	L+665	77.0	13.1	11.4	101.0	47.0	Make whole	12.1
€	**BBVASM**	**8.5**	**21-Oct-14**	**645**	**L+574**	**79.0**	**20.6**	**10.6**	**104.0**	**78.5**	**Make whole**	**4.3**
€	**ISPIM**	**8.047**	**20-Jun-18**	**796**	**L+410**	**75.0**	**14.6**	**9.9**	**101.0**	**54.5**	**Make whole**	**19.9**
€	**BPCEGP**	**9**	**17-Mar-15**	**818**	**L+653.3**	**83.0**	**17.2**	**10.8**	**104.0**	**66.0**	**Par**	**4.0**
High steps: Issued to comply with CRD4												
€	ISPIM*	9.5	1-Jun-16	722	MS+757	81.5	16.2	12.1	103.5	56.5	Reg 102 call	3.7
€	UCGIM	9.375	21-Jul-20	339	L+749	79.5	13.7	12.3	102.5	47.0	Par	8.6
Long call Tier 1s with large swap gains												
$	ABBEY	8.963	30-Jun-30	798	L+282.5	96.0	9.4	8.6	111.5	90.0	Make whole	69.3
$	BACR	6.86	15-Jun-32	681	L+173	88.5	8.0	7.0	95.5	64.0	Make whole	40.6
$	**BNP**	**7.195**	**25-Jun-37**	**1,100**	**L+129**	**84.0**	**8.8**	**8.0**	**98.5**	**69.0**	**Par**	**58.8**
£	LLOYDS	7.881	9-Dec-31	245	UKT+440	74.0	11.2	10.4	88.0	59.0	Make whole	40.8
£	LLOYDS	7.754	31-May-21	150	UKT+420	75.0	12.5	10.4	87.0	64.0	Make whole	31.5
£	LLOYDS	7.281	31-May-26	150	UKT+409.5	71.0	11.5	10.4	84.0	56.0	Make whole	34.5
Retail Tier 1s												
$	LLOYDS	7.875	29-Nov-13	424	-	73.5	32.2	10.8	86.0	57.5	N/A	
€	LLOYDS	7.875	29-Nov-13	173	-	74.0	33.0	10.7	86.0	57.5	N/A	
€	**BPCEGP**	**9.25**	**22-Apr-15**	**750**	**-**	**82.0**	**17.8**	**11.3**	**103.8**	**65.5**	**Par**	

Source: Morgan Stanley Research; Note: *ISPIM 9.5%, YT102 call: 15.0%; indicative offer levels as on June 14, 2012

The second section shows those Tier 1s with high steps which were issued to comply with CRD4, but at the time, the final rules for new Tier 1 were not known. ISPIM's €9.5% has a par claim in liquidation, has a pusher (albeit with regulatory override) and it's unclear if the trigger language would comply with CRD4. With a high coupon, we believe there's a strong chance it will try and get rid of it – LME (a second time) – or call it at 102 in 2020, when it should have lost more than 75% of its Tier 1 value under the grandfathering rules (in line with the bond documentation). UCGIM's €9.375% very clearly does not comply with CRD4 as it has a step-up. Again, with such a high coupon, the bank could choose to trigger the regulatory par call when CRD4 comes in (next year), or, at this cash price, try another LME. Once again, in either case, the floating back ends are high so a non-call and inaction on any further LME or regulatory par/102 calls is compensated for, in our view. However, considering the generally harsher language in these bonds, we would rather buy other high-step UCGIM or ISPIMs, at even higher YTC.

The long call section highlights the swap gains for these types of bonds. These generally have lower yields than the YTCs on the high steps, but have a greater likelihood of LME, in our view, as the bank would profit from the swap gain. The recent SocGen LT2 tender highlights that banks are still looking at such trades. We'd also note here that the Abbey $8.963% has must-pay coupons as well, and considering the expected more difficult periphery environment linked to Spain in the short term, this could well cheapen up in the near future due to the ties with Santander, its parent. We believe that Abbey is ring-fenced from Santander, and any widening here would be a buying opportunity. Many investors have asked for such a 'high swap gain' list, so we've included bonds here for information. We excluded long-call RBS as it cannot do LME until next year, we'd note that Barclays, while having 40 points of swap gains, has better yields on LT2, with a similar situation for Lloyds (or at least, YTMs on LT2 not too far from the YTCs here).

Finally, we list a number of retail Tier 1s with fixed, high coupons and no floating-rate back ends. These are simply expensive for the banks to leave outstanding, particularly for Lloyds, which must pay coupons out of post-tax earnings, as these are preference shares. Even without LME, these are at least interesting YTPs. Note, we do not include Deutsche €9.5% here due to lack of value, considering where it's trading, and a regulatory par call, which puts the investor at risk as this bond is currently trading above par.

All our suggestions above deliberately have high coupons, clearly with an eye on the bid from private individuals.

So Why Not Overweight?

We will remain opportunistic in Tier 1 and, as stated above, there are a number of specific negative factors that will not improve for this sector, ratings being the key one. We also have not changed our views on calls, so choosing only the high-coupon Tier 1s limits us at best to an E/W anyway. Further, we see better risk/reward here in LT2s than the Tier 1 sector as a whole.

Risk Factors

- The periphery situation worsens in Spain and no credible response happens in the coming months.
- There is a negative outcome in the Greek elections which causes bank debt at large to sell off, and stay at low levels for months.
- A response to Spain's banking problems comes and indeed, a more broader package is announced which cuts off wider periphery risks, leading to a very strong rally in Tier 1, which outperforms LT2 and senior (where we are both Equal-weight).

Appendix: Ratings Impacts on Tier 1s

Moody's Impact on Tier 1 Bonds

Ticker	Ccy	Cpn in %	Moody's	Fitch	S&P
Bonds which have dropped out of the iBoxx Tier 1 index since May 2012					
BBVASM	€	8.5	Ba1	BB-	BB+
ISPIM	€	9.5	Ba1	BB+	BB+
ISPIM	€	8.375	Ba1	BB+	BB+
ISPIM	€	8.047	Ba1	BB+	BB+
BBVASM	£	9.1	Ba1	BB-	BB+
SANTAN	£	11.3	Ba1	BB-	BBB-
BBVASM	$	5.919	Ba1	BB-	BB+
SANTAN	$	2	Ba1	BB-	BBB-
Bonds gone sub-IG since the May rebalancing, will drop out at the next rebalancing					
DANBNK	€	4.878	Ba2	BBB-	BB+
NYKRE	€	4.901	Ba2		BBB
NYKRE	€	9	Ba2		BBB
DANBNK	£	5.563	Ba2	BBB-	BB+
DANBNK	£	5.6838	Ba2	BBB-	BB+
DANBNK	$	5.914	Ba2	BBB-	BB+
Bonds expected to go sub-IG post review, will drop out of the index subsequently					
UBS	€	4.28	Baa3	BB+	BBB-
UBS	€	7.152	Baa3	BB+	BBB-
BPCEGP	€	6.117	Baa3	BB+	BBB-
BPCEGP	€	9.25	Baa3	BB+	BBB-
BPCEGP	€	9	Baa3	BB+	BBB-
BACR	€	4.875	Baa3	BB+	BBB
BACR	€	4.75	Baa3	BB+	BBB
ACAFP	€	7.875	Baa3	BBB-	BBB-
ACAFP	€	8.2	Baa3	BBB-	BBB-
BACR	£	6	Baa3	BB+	BBB
ACAFP	£	5.136	Baa3	BBB-	BBB-
ACAFP	£	8.125	Baa3	BBB-	BBB-
ACAFP	£	7.589	Baa3	BBB-	BBB-
UBS	$	6.243	Baa3	BB+	BBB-
BACR	$	6.278	Baa3	BB+	BBB
ACAFP	$	8.375	Baa3	BBB-	BBB-
ACAFP	$	9.75	Baa3	BBB-	BBB-
ACAFP	$	6.637	Baa3	BBB-	BBB-

Source: S&P, Moody's, Fitch, Morgan Stanley Research; does not take into account any expected S&P and Fitch actions.

Tier 1s Expected to Remain in the Indices

Ticker	Ccy	Cpn in %	Moody's	Fitch	S&P
€					
BNP	€	4.73	Baa3	BBB	BBB+
BNP	€	5.019	Baa3	BBB	BBB+
BNP	€	7.781	Baa3	BBB	BBB+
BNP	€	8.667	Baa3	BBB	BBB+
DB	€	5.33	Baa2	BBB-	BBB
DB	€	9.5	Baa2	BBB-	BBB
DB	€	8		BBB-	BBB
FBAVP	€	4.625	Baa1	BBB	A-
HSBC	€	5.3687	A3	A-	BBB+
HSBC	€	5.13	A3	A-	BBB+
SEB	€	9.25	Ba1	BBB	BBB-
SEB	€	7.0922	Ba1	BBB	BBB-
SHBASS	€	4.194	Baa3	BBB+	BBB+
£					
ABBEY	£	6.222		BB+	BBB-
ABBEY	£	5.827	Baa2	BBB-	BBB-
ABBEY	£	7.037	Baa2	BBB-	BBB-
BACR	£	14	Baa2	BBB-	BBB
BNP	£	5.945	Baa3	BBB	BBB+
BNP	£	5.954	Baa3	BBB	BBB+
BNP	£	7.436	Baa3	BBB	BBB+
COVBS	£	6.092	Baa3	BBB-	
DNBNO	£	6.0116	Ba1		BBB
HSBC	£	5.844	Baa1	A-	A-
HSBC	£	5.862	Baa1	A-	A-
HSBC	£	8.208	A3	A-	BBB+
NWIDE	£	7.971	Baa3	BBB	BBB
NWIDE	£	7.859	Baa3	BBB	BBB
NWIDE	£	6.25	Baa3	BBB	BBB
NWIDE	£	5.769	Baa3	BBB	BBB
NWIDE	£	6	Baa3	BBB	BBB
RABOBK	£	5.556	A2		A
SHBASS	£	6.4611	Baa3	BBB+	BBB+
STANLN	£	8.103	A3	BBB+	A-
$					
ABBEY	$	8.963	Baa3	BBB-	BBB-
BACR	$	6.86	Baa2	BBB-	BBB
BACR	$	5.926	Baa2	BBB-	BBB
BNP	$	5.186	Baa3	BBB	BBB+
BNP	$	7.195	Baa3	BBB	BBB+
CS	$	7.875		BB+	BBB
CS	$	8.25	A3	BB+	BBB
HSBC	$	5.911	Baa1	BBB+	BBB+
HSBC	$	10.176	A3	A-	BBB+
HSBC	$	4.61	A3	A-	BBB+
HSBC	$	6.8	A1	AA-	A-
NBHSS	$	8.375	Baa3	BBB+	BBB+
NDASS	$	5.424	Baa3	BBB+	BBB+
RABOBK	$	5.26	A2	A-	A
RABOBK	$	11	A2	A-	A
RABOBK	$	5.254	A2	A+	A
STANLN	$	6.409	Baa2	BBB	BBB+
STANLN	$	7.014	Baa2	BBB	BBB+
STANLN	$	8.125	Baa2	BBB	BBB+
STANLN	$	9.5	A3	BBB+	A-

Source: S&P, Moody's, Fitch, Morgan Stanley Research

Disclosure Section

Morgan Stanley & Co. International plc, authorized and regulated by Financial Services Authority, disseminates in the UK research that it has prepared, and approves solely for the purposes of section 21 of the Financial Services and Markets Act 2000, research which has been prepared by any of its affiliates. As used in this disclosure section, Morgan Stanley includes RMB Morgan Stanley (Proprietary) Limited, Morgan Stanley & Co International plc and its affiliates.
For important disclosures, stock price charts and equity rating histories regarding companies that are the subject of this report, please see the Morgan Stanley Research Disclosure Website at www.morganstanley.com/researchdisclosures, or contact your investment representative or Morgan Stanley Research at 1585 Broadway, (Attention: Research Management), New York, NY, 10036 USA.
For valuation methodology and risks associated with any price targets referenced in this research report, please email morganstanley.research@morganstanley.com with a request for valuation methodology and risks on a particular stock or contact your investment representative or Morgan Stanley Research at 1585 Broadway, (Attention: Research Management), New York, NY 10036 USA.

Analyst Certification

The following analysts hereby certify that their views about the companies and their securities discussed in this report are accurately expressed and that they have not received and will not receive direct or indirect compensation in exchange for expressing specific recommendations or views in this report: Jackie Ineke, Lee Street, Andrew Sheets.
Unless otherwise stated, the individuals listed on the cover page of this report are research analysts.

Global Research Conflict Management Policy

Morgan Stanley Research has been published in accordance with our conflict management policy, which is available at www.morganstanley.com/institutional/research/conflictpolicies.

Important US Regulatory Disclosures on Subject Companies

The following analyst or strategist (or a household member) owns securities (or related derivatives) in a company that he or she covers or recommends in Morgan Stanley Research: Lee Street - Barclays Bank(common or preferred stock). Morgan Stanley policy prohibits research analysts, strategists and research associates from investing in securities in their sub industry as defined by the Global Industry Classification Standard ("GICS," which was developed by and is the exclusive property of MSCI and S&P). Analysts may nevertheless own such securities to the extent acquired under a prior policy or in a merger, fund distribution or other involuntary acquisition.

As of May 31, 2012, Morgan Stanley beneficially owned 1% or more of a class of common equity securities of the following companies covered in Morgan Stanley Research: BBVA, BNP Paribas, Santander, Societe Generale, UniCredit S.p.A..

Within the last 12 months, Morgan Stanley managed or co-managed a public offering (or 144A offering) of securities of BNP Paribas, Lloyds Banking Group, Santander.

Within the last 12 months, Morgan Stanley has received compensation for investment banking services from Barclays Bank, BBVA, BNP Paribas, Credit Agricole S.A., Intesa SanPaolo S.p.A., Lloyds Banking Group, Natixis, Santander, Societe Generale, UniCredit S.p.A., BPCE, Nationwide Building Society.

In the next 3 months, Morgan Stanley expects to receive or intends to seek compensation for investment banking services from Barclays Bank, BBVA, BNP Paribas, Credit Agricole S.A., Intesa SanPaolo S.p.A., Lloyds Banking Group, Natixis, Santander, SNS Reaal Bank N.V., Societe Generale, UniCredit S.p.A., BPCE, Nationwide Building Society.

Within the last 12 months, Morgan Stanley has received compensation for products and services other than investment banking services from Barclays Bank, BBVA, BNP Paribas, Credit Agricole S.A., Intesa SanPaolo S.p.A., Lloyds Banking Group, Natixis, Santander, SNS Reaal Bank N.V., Societe Generale, UniCredit S.p.A., BPCE, Nationwide Building Society.

Within the last 12 months, Morgan Stanley has provided or is providing investment banking services to, or has an investment banking client relationship with, the following company: Barclays Bank, BBVA, BNP Paribas, Credit Agricole S.A., Intesa SanPaolo S.p.A., Lloyds Banking Group, Natixis, Santander, SNS Reaal Bank N.V., Societe Generale, UniCredit S.p.A., BPCE, Nationwide Building Society.

Within the last 12 months, Morgan Stanley has either provided or is providing non-investment banking, securities-related services to and/or in the past has entered into an agreement to provide services or has a client relationship with the following company: Barclays Bank, BBVA, BNP Paribas, Credit Agricole S.A., Intesa SanPaolo S.p.A., Lloyds Banking Group, Natixis, Santander, SNS Reaal Bank N.V., Societe Generale, UniCredit S.p.A., BPCE, Nationwide Building Society.

Morgan Stanley & Co. LLC makes a market in the securities of Barclays Bank, BBVA, Lloyds Banking Group, Santander.

The equity research analysts or strategists principally responsible for the preparation of Morgan Stanley Research have received compensation based upon various factors, including quality of research, investor client feedback, stock picking, competitive factors, firm revenues and overall investment banking revenues.

Morgan Stanley and its affiliates do business that relates to companies/instruments covered in Morgan Stanley Research, including market making, providing liquidity and specialized trading, risk arbitrage and other proprietary trading, fund management, commercial banking, extension of credit, investment services and investment banking. Morgan Stanley sells to and buys from customers the securities/instruments of companies covered in Morgan Stanley Research on a principal basis. Morgan Stanley may have a position in the debt of the Company or instruments discussed in this report.

Certain disclosures listed above are also for compliance with applicable regulations in non-US jurisdictions.

STOCK RATINGS

Morgan Stanley uses a relative rating system using terms such as Overweight, Equal-weight, Not-Rated or Underweight (see definitions below). Morgan Stanley does not assign ratings of Buy, Hold or Sell to the stocks we cover. Overweight, Equal-weight, Not-Rated and Underweight are not the equivalent of buy, hold and sell. Investors should carefully read the definitions of all ratings used in Morgan Stanley Research. In addition, since Morgan Stanley Research contains more complete information concerning the analyst's views, investors should carefully read Morgan Stanley Research, in its entirety, and not infer the contents from the rating alone. In any case, ratings (or research) should not be used or relied upon as investment advice. An investor's decision to buy or sell a stock should depend on individual circumstances (such as the investor's existing holdings) and other considerations.

Global Stock Ratings Distribution

(as of May 31, 2012)

For disclosure purposes only (in accordance with NASD and NYSE requirements), we include the category headings of Buy, Hold, and Sell alongside our ratings of Overweight, Equal-weight, Not-Rated and Underweight. Morgan Stanley does not assign ratings of Buy, Hold or Sell to the stocks we cover. Overweight, Equal-weight, Not-Rated and Underweight are not the equivalent of buy, hold, and sell but represent recommended relative weightings (see definitions below). To satisfy regulatory requirements, we correspond Overweight, our most positive stock rating, with a buy recommendation; we correspond Equal-weight and Not-Rated to hold and Underweight to sell recommendations, respectively.

	Coverage Universe		Investment Banking Clients (IBC)		
Stock Rating Category	Count	% of Total	Count	% of Total IBC	% of Rating Category
Overweight/Buy	**1133**	**38%**	**471**	**43%**	**42%**
Equal-weight/Hold	**1250**	**42%**	**472**	**43%**	**38%**
Not-Rated/Hold	**99**	**3%**	**27**	**2%**	**27%**
Underweight/Sell	**461**	**16%**	**121**	**11%**	**26%**
Total	**2,943**		**1091**		

Data include common stock and ADRs currently assigned ratings. An investor's decision to buy or sell a stock should depend on individual circumstances (such as the investor's existing holdings) and other considerations. Investment Banking Clients are companies from whom Morgan Stanley received investment banking compensation in the last 12 months.

Analyst Stock Ratings

Overweight (O). The stock's total return is expected to exceed the average total return of the analyst's industry (or industry team's) coverage universe, on a risk-adjusted basis, over the next 12-18 months.
Equal-weight (E). The stock's total return is expected to be in line with the average total return of the analyst's industry (or industry team's) coverage universe, on a risk-adjusted basis, over the next 12-18 months.
Not-Rated (NR). Currently the analyst does not have adequate conviction about the stock's total return relative to the average total return of the analyst's industry (or industry team's) coverage universe, on a risk-adjusted basis, over the next 12-18 months.
Underweight (U). The stock's total return is expected to be below the average total return of the analyst's industry (or industry team's) coverage universe, on a risk-adjusted basis, over the next 12-18 months.
Unless otherwise specified, the time frame for price targets included in Morgan Stanley Research is 12 to 18 months.

Analyst Industry Views

Attractive (A): The analyst expects the performance of his or her industry coverage universe over the next 12-18 months to be attractive vs. the relevant broad market benchmark, as indicated below.
In-Line (I): The analyst expects the performance of his or her industry coverage universe over the next 12-18 months to be in line with the relevant broad market benchmark, as indicated below.
Cautious (C): The analyst views the performance of his or her industry coverage universe over the next 12-18 months with caution vs. the relevant broad market benchmark, as indicated below.
Benchmarks for each region are as follows: North America - S&P 500; Latin America - relevant MSCI country index or MSCI Latin America Index; Europe - MSCI Europe; Japan - TOPIX; Asia - relevant MSCI country index.

Important Disclosures for Morgan Stanley Smith Barney LLC Customers

Citi Investment Research & Analysis (CIRA) research reports may be available about the companies or topics that are the subject of Morgan Stanley Research. Ask your Financial Advisor or use Research Center to view any available CIRA research reports in addition to Morgan Stanley research reports.

Important disclosures regarding the relationship between the companies that are the subject of Morgan Stanley Research and Morgan Stanley Smith Barney LLC, Morgan Stanley and Citigroup Global Markets Inc. or any of their affiliates, are available on the Morgan Stanley Smith Barney disclosure website at www.morganstanleysmithbarney.com/researchdisclosures.

For Morgan Stanley and Citigroup Global Markets, Inc. specific disclosures, you may refer to www.morganstanley.com/researchdisclosures and https://www.citigroupgeo.com/geopublic/Disclosures/index_a.html.

Each Morgan Stanley Equity Research report is reviewed and approved on behalf of Morgan Stanley Smith Barney LLC. This review and approval is conducted by the same person who reviews the Equity Research report on behalf of Morgan Stanley. This could create a conflict of interest.

Other Important Disclosures

Morgan Stanley & Co. International PLC and its affiliates have a significant financial interest in the debt securities of Barclays Bank, BBVA, BNP Paribas, Credit Agricole S.A., Intesa SanPaolo S.p.A., Lloyds Banking Group, Natixis, Santander, Societe Generale, UniCredit S.p.A., BPCE, Nationwide Building Society.

Morgan Stanley is not acting as a municipal advisor and the opinions or views contained herein are not intended to be, and do not constitute, advice within the meaning of Section 975 of the Dodd-Frank Wall Street Reform and Consumer Protection Act.

Morgan Stanley produces an equity research product called a "Tactical Idea." Views contained in a "Tactical Idea" on a particular stock may be contrary to the recommendations or views expressed in research on the same stock. This may be the result of differing time horizons, methodologies, market events, or other factors. For all research available on a particular stock, please contact your sales representative or go to Client Link at www.morganstanley.com.

Morgan Stanley Research does not provide individually tailored investment advice. Morgan Stanley Research has been prepared without regard to the circumstances and objectives of those who receive it. Morgan Stanley recommends that investors independently evaluate particular investments and strategies, and encourages investors to seek the advice of a financial adviser. The appropriateness of an investment or strategy will depend on an investor's circumstances and objectives. The securities, instruments, or strategies discussed in Morgan Stanley Research may not be suitable for all investors, and certain investors may not be eligible to purchase or participate in some or all of them. Morgan Stanley Research is not an offer to buy or sell any security/instrument or to participate in any trading strategy. The value of and income from your investments may vary because of changes in interest rates, foreign exchange rates, default rates, prepayment rates, securities/instruments prices, market indexes, operational or financial conditions of companies or other factors. There may be time limitations on the exercise of options or other rights in securities/instruments transactions. Past performance is not necessarily a guide to future performance. Estimates of future performance are based on assumptions that may not be realized. If provided, and unless otherwise stated, the closing price on the cover page is that of the primary exchange for the subject company's securities/instruments.

The fixed income research analysts, strategists or economists principally responsible for the preparation of Morgan Stanley Research have received compensation based upon various factors, including quality, accuracy and value of research, firm profitability or revenues (which include fixed income trading and capital markets profitability or revenues), client feedback and competitive factors. Fixed Income Research analysts', strategists' or economists' compensation is not linked to investment banking or capital markets transactions performed by Morgan Stanley or the profitability or revenues of particular trading desks.

Morgan Stanley Research is not an offer to buy or sell or the solicitation of an offer to buy or sell any security/instrument or to participate in any particular trading strategy. The "Important US Regulatory Disclosures on Subject Companies" section in Morgan Stanley Research lists all companies mentioned where Morgan Stanley owns 1% or more of a class of common equity securities of the companies. For all other companies mentioned in Morgan Stanley Research, Morgan Stanley may have an investment of less than 1% in securities/instruments or derivatives of securities/instruments of companies and may trade them in ways different from those discussed in Morgan Stanley Research. Employees of Morgan Stanley not involved in the preparation of Morgan Stanley Research may have investments in securities/instruments or derivatives of securities/instruments of companies mentioned and may trade them in ways different from those discussed in Morgan Stanley Research. Derivatives may be issued by Morgan Stanley or associated persons.

With the exception of information regarding Morgan Stanley, Morgan Stanley Research is based on public information. Morgan Stanley makes every effort to use reliable, comprehensive information, but we make no representation that it is accurate or complete. We have no obligation to tell you when opinions or information in Morgan Stanley Research change apart from when we intend to discontinue equity research coverage of a subject company. Facts and views presented in Morgan Stanley Research have not been reviewed by, and may not reflect information known to, professionals in other Morgan Stanley business areas, including investment banking personnel.

Morgan Stanley Research personnel may participate in company events such as site visits and are generally prohibited from accepting payment by the company of associated expenses unless pre-approved by authorized members of Research management.

Morgan Stanley may make investment decisions or take proprietary positions that are inconsistent with the recommendations or views in this report.

To our readers in Taiwan: Information on securities/instruments that trade in Taiwan is distributed by Morgan Stanley Taiwan Limited ("MSTL"). Such information is for your reference only. Information on any securities/instruments issued by a company owned by the government of or incorporated in the PRC and listed in on the Stock Exchange of Hong Kong ("SEHK"), namely the H-shares, including the component company stocks of the Stock Exchange of Hong Kong ("SEHK")'s Hang Seng China Enterprise Index is distributed only to Taiwan Securities Investment Trust Enterprises ("SITE"). The reader should independently evaluate the investment risks and is solely responsible for their investment decisions. Morgan Stanley Research may not be distributed to the public media or quoted or used by the public media without the express written consent of Morgan Stanley. To our readers in Hong Kong: Information is distributed in Hong Kong by and on behalf of, and is attributable to, Morgan Stanley Asia Limited as part of its regulated activities in Hong Kong. If you have any queries concerning Morgan Stanley Research, please contact our Hong Kong sales representatives. Information on securities/instruments that do not trade in Taiwan is for informational purposes only and is not to be construed as a recommendation or a solicitation to trade in such securities/instruments. MSTL may not execute transactions for clients in these securities/instruments.

Morgan Stanley is not incorporated under PRC law and the research in relation to this report is conducted outside the PRC. Morgan Stanley Research does not constitute an offer to sell or the solicitation of an offer to buy any securities in the PRC. PRC investors shall have the relevant qualifications to invest in such securities and shall be responsible for obtaining all relevant approvals, licenses, verifications and/or registrations from the relevant governmental authorities themselves.

Morgan Stanley Research is disseminated in Brazil by Morgan Stanley C.T.V.M. S.A.; in Japan by Morgan Stanley MUFG Securities Co., Ltd. and, for Commodities related research reports only, Morgan Stanley Capital Group Japan Co., Ltd; in Hong Kong by Morgan Stanley Asia Limited (which accepts responsibility for its contents); in Singapore by Morgan Stanley Asia (Singapore) Pte. (Registration number 199206298Z) and/or Morgan Stanley Asia (Singapore) Securities Pte Ltd (Registration number 200008434H), regulated by the Monetary Authority of Singapore (which accepts legal responsibility for its contents and should be contacted with respect to any matters arising from, or in connection with, Morgan Stanley Research); in Australia to "wholesale clients" within the meaning of the Australian Corporations Act by Morgan Stanley Australia Limited A.B.N. 67 003 734 576, holder of Australian financial services license No. 233742, which accepts responsibility for its contents; in Australia to "wholesale clients" and "retail clients" within the meaning of the Australian Corporations Act by Morgan Stanley Smith Barney Australia Pty Ltd (A.B.N. 19 009 145 555, holder of Australian financial services license No. 240813, which accepts responsibility for its contents; in Korea by Morgan Stanley & Co International plc, Seoul Branch; in India by Morgan Stanley India Company Private Limited; in Canada by Morgan Stanley Canada Limited, which has approved of and takes responsibility for its contents in Canada; in Germany by Morgan Stanley Bank AG, Frankfurt am Main and Morgan Stanley Private Wealth Management Limited, Niederlassung Deutschland, regulated by Bundesanstalt fuer Finanzdienstleistungsaufsicht (BaFin); in Spain by Morgan Stanley, S.V., S.A., a Morgan Stanley group company, which is supervised by the Spanish Securities Markets Commission (CNMV) and states that Morgan Stanley Research has been written and distributed in accordance with the rules of conduct applicable to financial research as established under Spanish regulations; in the US by Morgan Stanley & Co. LLC, which accepts responsibility for its contents. Morgan Stanley & Co. International plc, authorized and regulated by the Financial Services Authority, disseminates in the UK research that it has prepared, and approves solely for the purposes of section 21 of the Financial Services and Markets Act 2000, research which has been prepared by any of its affiliates. Morgan Stanley Private Wealth Management Limited, authorized and regulated by the Financial Services Authority, also disseminates Morgan Stanley Research in the UK. Private UK investors should obtain the advice of their Morgan Stanley & Co. International plc or Morgan Stanley Private Wealth Management representative about the investments concerned. RMB Morgan Stanley (Proprietary) Limited is a member of the JSE Limited and regulated by the Financial Services Board in South Africa. RMB Morgan Stanley (Proprietary) Limited is a joint venture owned equally by Morgan Stanley International Holdings Inc. and RMB Investment Advisory (Proprietary) Limited, which is wholly owned by FirstRand Limited.

The information in Morgan Stanley Research is being communicated by Morgan Stanley & Co. International plc (DIFC Branch), regulated by the Dubai Financial Services Authority (the DFSA), and is directed at Professional Clients only, as defined by the DFSA. The financial products or financial services to which this research relates will only be made available to a customer who we are satisfied meets the regulatory criteria to be a Professional Client.

The information in Morgan Stanley Research is being communicated by Morgan Stanley & Co. International plc (QFC Branch), regulated by the Qatar Financial Centre Regulatory Authority (the QFCRA), and is directed at business customers and market counterparties only and is not intended for Retail Customers as defined by the QFCRA.

As required by the Capital Markets Board of Turkey, investment information, comments and recommendations stated here, are not within the scope of investment advisory activity. Investment advisory service is provided in accordance with a contract of engagement on investment advisory concluded between brokerage houses, portfolio management companies, non-deposit banks and clients. Comments and recommendations stated here rely on the individual opinions of the ones providing these comments and recommendations. These opinions may not fit to your financial status, risk and return preferences. For this reason, to make an investment decision by relying solely to this information stated here may not bring about outcomes that fit your expectations.

The trademarks and service marks contained in Morgan Stanley Research are the property of their respective owners. Third-party data providers make no warranties or representations relating to the accuracy, completeness, or timeliness of the data they provide and shall not have liability for any damages relating to such data. The Global Industry Classification Standard (GICS) was developed by and is the exclusive property of MSCI and S&P. Morgan Stanley bases projections, opinions, forecasts and trading strategies regarding the MSCI Country Index Series solely on public information. MSCI has not reviewed, approved or endorsed these projections, opinions, forecasts and trading strategies. Morgan Stanley has no influence on or control over MSCI's index compilation decisions. Morgan Stanley Research or portions of it may not be reprinted, sold or redistributed without the written consent of Morgan Stanley. Morgan Stanley research is disseminated and available primarily electronically, and, in some cases, in printed form. Additional information on recommended securities/instruments is available on request.

Morgan Stanley Research, or any portion thereof may not be reprinted, sold or redistributed without the written consent of Morgan Stanley.

Morgan Stanley Research is disseminated and available primarily electronically, and, in some cases, in printed form.

Additional information on recommended securities/instruments is available on request.

Cc1406

Morgan Stanley

The Americas
1585 Broadway
New York, NY 10036-8293
United States
Tel: +1 (1)212 761 4000

Europe
20 Bank Street, Canary Wharf
London E14 4AD
United Kingdom
Tel: +44 (0) 20 7 425 8000

Japan
4-20-3 Ebisu, Shibuya-ku
Tokyo 150-6008
Japan
Tel: +81 (0)3 5424 5000

Asia/Pacific
1 Austin Road West
Kowloon
Hong Kong
Tel: +852 2848 5200