

Norway's Only Pure AT1 Fund

Stockholm (HedgeNordic) – About a year ago, Borea Asset Management launched **Borea Obligasjon**, a special fund that solely invests in additional tier-1 (AT1) securities issued by Norwegian savings and commercial banks. “Borea Obligasjon is the only pure AT1 fund in Norway,” portfolio manager Magnus Vie Sundal (*pictured*) tells HedgeNordic. This pure AT1 fund has now joined the Nordic Hedge Index.

AT1 securities are a relatively young asset class born out of the financial crisis of 2008, acting as a critical instrument in regulators’ post-crisis bail-in strategy. The goal of these securities is to improve banks’ ability to mitigate risks and limit the reliance on the public purse during a banking crisis. AT1 notes, which represent hybrid capital absorbing losses when a bank’s regulatory capital ratio falls below a certain trigger level, can absorb losses either by converting into common equity or suffering a principal write-down before taxpayers have to step in.

Borea Obligasjon predominantly invests in NOK-denominated AT1s issued by savings banks and selected commercial banks. “Most of NOK AT1s are issued by larger banks, but we are happy to buy AT1s from smaller banks that are paying a liquidity premium,” says Sundal, one of the portfolio managers in charge of Borea Obligasjon. “In fact, we find that these banks often have higher leverage ratios and are generally well capitalised, although with somewhat lower lending portfolio diversification,” he emphasises. Borea Obligasjon uses leverage and can raise its exposure to up to 150 percent. A portion equal to the borrowed amount is invested in more liquid AT1s. “We also include USD AT1s issued by the large Nordic banks,” adds Sundal.

These deeply subordinated bonds carry higher yields than traditional fixed-income securities, and Borea Obligasjon seeks to offer investors access to the return potential of this young and growing asset class. “We always aim to offer our clients something they cannot get elsewhere,” says Sundal. “We believe this product is a good contribution to our clients’ investment universe.”

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The ratings of AT1 securities are several notches below the issuer’s credit rating because of their subordinated status. The AT1’s ratings, however, may not always fully reflect the underlying strength of the balance sheets supporting them. “The Norwegian savings banks are in an exceptional position compared to many peers: they hold a substantial amount of equity, with many posting leverage ratios above 10 percent,” explains Sundal.

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The team running Borea Obligasjon also “believe the Norwegian welfare state represents the ultimate backstop for Norwegian consumers.” According to Sundal, “this helps ensure debt service ability in the retail market, towards which most savings banks are focused.” Sundal goes on to explain that “the organisational structure gives the incentive to replenish banks with equity long before AT1’s triggers on write-downs are reached,” which “gives us comfort that losses will be kept at a minimum, while still offering a decent return in today’s low-yielding environment.”

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Borea Obligasjon delivered a cumulative return of 9.4 percent since launching in August of last year. In the first seven months of 2020, the fund gained 5.7 percent. "We are very happy with the performance and have seen increasing interest from investors throughout the year," Sundal comments on the fund's inception-to-date journey. Borea Obligasjon now has about NOK 1.6 billion under management, slightly shy the NOK 2.0 billion managed by the asset manager's flagship fixed-income hedge fund, **Borea Høyrente**.

Welcome to the Nordic Hedge Index!