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International Capital Markets

The World Bank's $200m "go-it-alone" Eurobond

The World Bank last week offered, via *Shearson Lehman Brothers Intl* as sole lead manager and underwriter, a $200m Eurobond whose implications promise to reverberate around the capital markets for months to come.
While 1985 has been a wild year in Eurobonds, this technique could prove one of the most significant developments of the last 12 months, Eurobond analysts say.

It's the first dollar issue of its type, in publicly listed form, to do without a conventional syndication group. And it is perhaps the natural development of a trend by the big, well-capitalised Eurobond houses to absorb bonds in a small, tightly-controlled underwriting group. This has already reached the stage where Morgan Stanley Intl's Peter Ogden calls many $100m Eurobonds virtual "block trades" on the primary side nowadays.

Shearsons acknowledges that the 15-year **World Bank** Euro is radical in many respects but insists that, on current market trends, such techniques could be here to stay.

The **World Bank** itself has turned upside down traditional underwriter relationships, including such major institutions as Deutsche Bank, in giving the mandate to *Shearsons*. It's a brave move by IBRD Treasurer Eugene Rotberg, and many an issuer before has found that taking on the Eurobond market's heavyweight houses has had long-running repercussions. Remember the EIB's Andre George?
While Eurobond houses questioned by IFR conceded that there's a definite trend towards smaller, but more powerful management groupings for issues, many questioned whether the time for a sole-syndicated deal was ripe.

And it is a serious sole syndication operation. While officially, a selling group is in place, IFR understands that this is largely cosmetic, and perhaps only one or two selling group members are actually involved.
The World Banks were being sold direct to clients in a way that, in one stroke, solves a basic problem of the Eurobond distribution mechanism — the frequency with which issues, mispriced or not, are dumped in the grey market, invariably forcing the lead manager to support the issue.

Cutting the co-managing group removes the stage at which dumping mostly occurs. *Shearsons* has virtual abolute control over the issue, both as to the number of bonds in circulation and as to the price stability.
Early talk that the bond broking community, led by houses like *Guy Butler*, could be frozen out of Eurobond distribution is premature. *Butlers*, a day or two after the **World Bank** launch, was quoting two-way screen prices as bonds recirculated back into markets.
Brokers are restricted to dealing with professional Eurobond houses, although there's always been the suspicion that one broker in fact deals directly with end-clients. One banker mused, however, "Does this raise the spectre that large institutional clients could become active in the grey market through the brokers, once they had received the bonds, and wanted to reoffer them?"

Meantime, a growth of the **World Bank** technique would no doubt consolidate the power of the big guns of the Eurobond underwriters, because of the capital commitment required and the ultimate impossibility of, cost-effectively, hedging such an issue.
Shearsons itself has a capital of $2.1bn, second only to *Merrill Lynch* among the Wall Street investment banks.

The main criticism of the issuing technique was that it could create a position of illiquidity in the bonds, with one banker noting: "I know at least five institutional accounts which turned the issue down because they fear that they could be locked into Shearsons as the only effective market-maker."
For this deal — and Shearsons concedes that only top quality issuers can at this stage employ the technique — those fears look unfounded. Between 8—12 market-makers are reportedly trading the issue, including Merrill Lynch, Bankers Trust, Kidder Peabody, Paine Webber, BankAmerica and Chase Manhattan.

By last Friday, all the $200m issue had been turned over once, and more turnover was being generated as accounts, taking advantage of profits from the New York rally, reoffered bonds back to the market. That resulted in a fairly broad trading base in the bonds.
Finally, the financial engineering behind the Euro, and the allied zero in New York, gets the World Bank ultimately 30-year fixed-rate dollars more or less flat on US Treasuries. Perhaps that the bottom line of this deal — if you can think up a clever, cost-effective idea for an issuer, it strengthens your hand in getting sole lead-managing and underwriting status.
As competitive pressures force down swap fees to perhaps only a meagre couple of basis points, this technique may be the answer to that perennial problem of making money from the Eurobond business.

• In a sharp contrast to the New York euphoria and, at a lesser extent, the euro-optimism in the straight euro-dollar sector, the dullness of the ECU and euro-French franc markets is striking. The sharp increase in Italian short-term rates forced Banque de France to quickly raise euro-FF short-term rates in order to stabilise the franc. In its wake, the Belgian franc came under attack and the **Kingdom's** short-term rate had also to be increased, a move which. of course, negatively affected the country's capital market. Finally, sterling started to suffer from falling OPEC prices.
As a result, not only ECU rates are shifting upward but also the faith in the EEC currency is shaken. Investors as well as borrowers are not currently attracted by ECU offerings. In a similar way, the euro-French franc bond market has lost further ground. A sharp increase in euro-FF short-term rates and the prospect of a devaluation of the French currency against the DM, has deterred foreign investors from buying new euro-FF issues. Credit National new offering felt it last week. **ifr**

Average Market Yields

10 year Maturity

Issue	Semi-Annual Yield	Change on week
US$ Gov't	9.20	−40bp
US$ Euro	9.81	−27
Can$ Gov't	9.91	−26
DM Gov't	6.48	−12
Yen Gov't	6.29	−21
UK Gov't	10.91	11
Swiss Franc Gov't	4.46	−7

Source: Salomon Bros Bond Research