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From: Lev Mikheev <lev.mikheev@salutecapital.com>
Sent: 09 March 2010 16:51
To: Lev Mikheev; 'eric.dannheim@moorecap.com'
Cc: Genna Lozovsky; Peter Boone; Tom Hickey
Subject: RE: trade proposal: tier 1's of better european banks

Sorry Eric, an important thing to mention: given the relatively low risk nature of these bonds, and the fact that we are constructing the trade beta neutral vs the PIGS, our allocation framework gives quite a substantial allocation: around $100mm market value.

Please let me know if you would like a call or a meeting to discuss these ideas.

From: Lev Mikheev
Sent: 09 March 2010 15:41
To: 'eric.dannheim@moorecap.com'
Cc: Genna Lozovsky; Lev Mikheev; Peter Boone; Tom Hickey
Subject: trade proposal: tier 1's of better european banks
Importance: High

Eric, while previously we have been focusing on the hybrids of the weak, but systemically important banks, like CMZB, we have recently done some work to incorporate hybrids issued by much stronger European bank names. The names we are looking at the moment are SocGen, BCPE Group and ING.

The idea in the nutshell is to assemble a portfolio of tier 1's of such stronger names, which yield 7-8% to perpetuity, thus better matching the level of yield and the beta of the Greek and Portuguese bonds, but over 10-11% to the call. We think they will be either called or exchanged. These are systemic names, and thus well supported, but they are also under pressure from their regulators to increase core Tier 1. Therefore:

1) They are likely to raise more common equity, thus making hybrids safer.
2) If the current tier 1 rules remain, they will keep issuing and therefore will keep calling on the first call date, to keep the racket going.
3) If the current tier 1 rules change (allegedly part of Basel III), they will call or exchange the current bonds, as they become very expensive capital vs cheap senior debt they can raise.

It is important to understand that these banks monetize large gains when they buy/exchange these bonds back, not just on a difference between the buyback price and par, but also on the swaps where they received fix at issuance, when swap rates were a lot higher. In essence you can think of them having shorted this bonds initially at spreads inside 100 and buying them back now at spreads of 600-1000.

This capital structure management activity slowed down during the annual reporting season that has just ended, and we expect actions leading the whole complex to tighten shortly.