



## Story of the Week

### Codere delays coupon payment again as its PD soars to new heights

Spanish gaming company Codere SA [announced on September 13](#) that it will delay the payment on its USD 300mn of 9.25% bonds by two days to September 17. This is the third such event from the company since June when the company [missed a EUR 30mn payment](#), and the latest missed coupon was one that was actually due on August 15, with a 30-day grace period. Codere also said that it paid a penalty to amend the early-maturity terms of a EUR 99mn loan from private-equity companies Canyon Partners LLC and Blackstone Group LP's GSO Capital Partners that require Codere to repay the facility if it pays the missed coupon. The loan facility was also expanded by an additional EUR 35m.

Figure 1 shows the RMI 1-year probability of default (RMI PD) for Codere, the cost to insure Codere's bonds and price of the company's 8.25% bonds maturing in 2015. Both RMI's PD model and the market estimate of Codere's credit risk suggest heightened likelihood of a default event for the company. In fact, the company's RMI PD has been on a steady, upward course since March 2012. Codere's credit standing moved into junk territory (PD-implied credit rating based on historically observed default rates for credit rating agency ratings) in June 2012, reflecting increased default risk a year before the missed coupon. The International Swaps & Derivatives Association (ISDA) has been asked to rule whether the two-day delayed payment by Codere constitutes a default under credit default swap contracts.

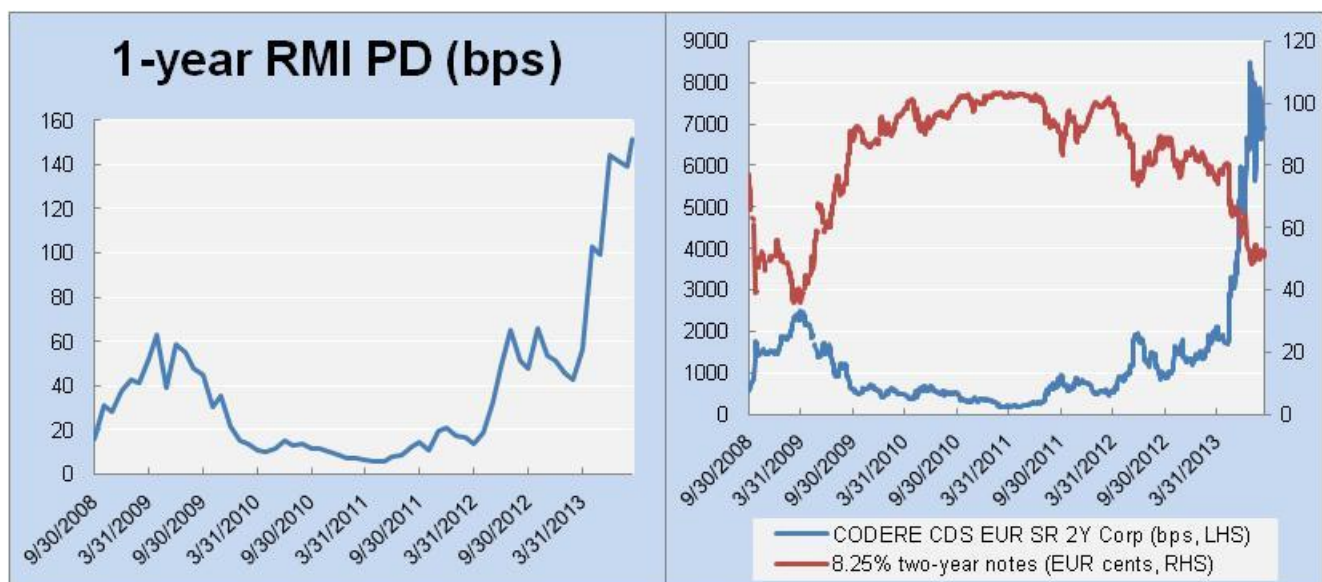


Figure 1. Source: Bloomberg; CMA; RMI

According to [Bloomberg](#), Codere's bonds have the highest yields among western European entities that have not restructured or filed for bankruptcy and credit default swap contracts on the company's debt are the second-most expensive in the world after US-based and privately held Energy Future Holdings Corp.

Based on the most recent calibration of the RMI PD model, Codere's default risk is most sensitive to its distance to default (DTD), or volatility-adjusted leverage, which takes into account a firm's liabilities, market capitalization and market volatility. Figure 2 shows the deteriorating trend of Codere's DTD over recent years, and Figure 3 illustrates the reasons for this decline. It is easily observable that Codere has displayed mounting gross debt burden, tumbling market value and increased market volatility – all of which negatively influence DTD. In general, lower DTD leads to higher RMI PDs.

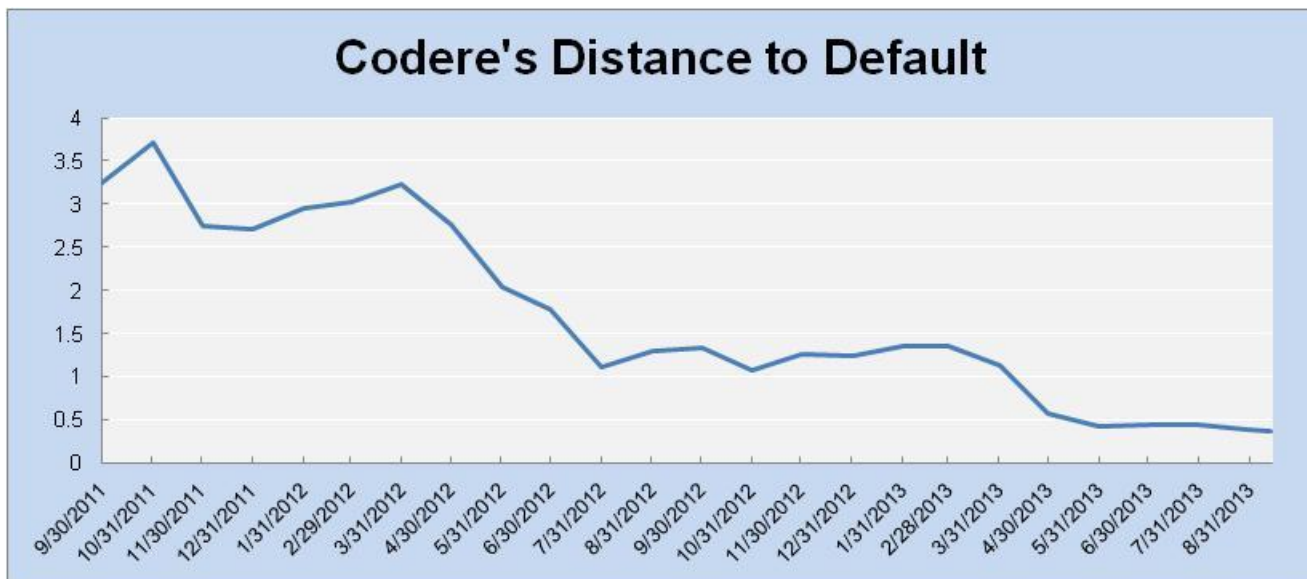


Figure 2: Codere's DTD has fallen almost 90% from where it was two years ago. *Source: RMI*  
 Note: DTD measures the distance of a firm's implied asset value from its default point, in terms of standard deviations in the asset value. Lower DTD equals higher likelihood of default.



Figure 3: Codere's total liabilities, market capitalization and stock volatility. *Source: Bloomberg*

Codere's market value has tumbled over 65% this year as the company reported its sixth consecutive quarter of losses for Q2, hit by Argentina's imposition of a smoking ban in October 2012 and new gambling regulations in Mexico; the two Latin American countries were Codere's most important markets by revenue. Moreover, total liabilities of the company have almost tripled since 2005.

Table 1 lists several leverage and liquidity ratios to highlight Codere's elevated leverage and tightening liquidity. The Altman's Z-Score for Codere, which indicates the probability of a company entering bankruptcy within the next two years (a score below 1.8 indicates potential bankruptcy), sank to 1.2 at the end of Q2 from 1.87 two years ago. Moody's downgraded Codere's probability of default rating to Ca and affirmed its long-term rating at Caa3, after the company deferred the June 15 coupon.

FS dated	6/30/2013	12/31/2012	12/31/2011	12/31/2010	12/31/2009	12/31/2008	12/31/2007
Total Debt/Equity (%)	N/A*	1191.57	520.13	638.96	1220.35	1015.69	478.84
Cash Ratio	0.25	0.29	0.4	0.35	0.44	0.38	0.32
Current Ratio	0.65	0.73	0.77	0.68	1.06	0.91	0.93

Table 1: Codere's leverage has increased while its liquidity fell. *Source: Bloomberg*  
 \*Codere's equity was negative (-EUR18.95mn) as of June 30, 2013.

**In the News****S&P cuts Argentina's sovereign rating on rising legal risk**

**Sep 10.** Standard & Poor's downgraded Argentina's long-term sovereign foreign currency credit rating to CCC-plus from B-minus on Tuesday, and said the outlook on the rating remains negative. The credit rating agency cited "increased risks to debt service stemming from a lawsuit over the debt the government of Argentina still maintains in default". The US Second Circuit Court of Appeals on August 23 upheld a lower court's ruling, which ruled that Argentina cannot make payments on its restructured debt while refusing to pay investors of USD 1.33bn in defaulted notes. ([Reuters](#))

**Verizon borrows USD 49bn in bond market record**

**Sep 11.** Verizon completed the largest debt sale on record, issuing a total of USD 49bn of bonds amid strong investor demand. The company offered generous yields on the securities relative to other similarly rated bonds, with the 10-year bond selling at a yield of 5.19%, 57bps higher than its existing debt with the same maturity. The order book reached USD 100bn, almost double the size of orders for Apple's USD 17bn offering in April. The US-based telecommunications company plans to use the proceeds to fund its USD 130bn acquisition of the 45% stake in Verizon Wireless it does not already own. ([Financial Times](#))

**Madrid to help Spain's banks rebuild balance sheets**

**Sept 11.** Spain's largest lenders are set to receive a boost to their balance sheets as the Spanish government looks to allow banks to reclassify deferred tax assets (DTAs) as tax credits by the year's end. The country's banks have been lobbying the government for months on this issue, arguing that other eurozone countries have already made similar changes. DTAs are assets booked on bank losses or provisions that can be used to offset tax bills in profitable times; they currently comprise about EUR 50bn on Spanish banks' balance sheets, or almost 40% of Spanish bank's core tier 1 capital. Although DTAs will not be factored into a bank's capital buffet under Basel III, tax credits will be, as governments must honor them even in bankruptcy cases. ([FT](#))

**China shadow banking returns as growth rebound adds risks**

**Sep 11.** China's broadest measure of new credit roughly doubled in August from the previous month, the first pickup in credit growth after an unprecedented four straight quarters of declines. Aggregate financing was CNY 1.57tn and new CNY loans contributed 45% of it. The latest data on credit growth suggests a resurgence of shadow banking that poses risks in the financial sector and that special attention and alert need to be paid to manage the risk. ([Bloomberg](#))

**Singapore tightens rules on unsecured loans to rein in debt**

**Sep 11.** In a bid to rein in the city-state's rising household debt, the Monetary Authority of Singapore (MAS) has introduced new restrictions to the amount of credit card and other unsecured loans banks can make to individuals. The rules, which are to take effect in stages from December 1, include limiting the total amount of unsecured loans an individual can take to 12 times his or her monthly income. The non-performing loans written off by banks in 2012 have risen 21% to SGD 226mn year-on-year, while the republic's household debt as a percentage of its GDP had climbed to around 75% from 55% in 2010. Nevertheless, Singapore's debt-to-asset ratio remains relatively low as compared to other Asian countries. ([Reuters](#))

**Indonesia lifts interest rate for second time in two weeks**

**Sep 12.** In an attempt to arrest the rupiah's decline, control Indonesia's current account deficit and suppress inflationary expectations, Bank Indonesia (BI) unexpectedly raised its main lending rate for the second time in two weeks. The raising of the BI rate by 25bps to 7.25%, its highest since May 2009, surprised many economists as the cost of borrowing had already climbed 125bps since June. Bank Indonesia also slashed its GDP growth forecast to 5.5% on slowing investment and consumer spending. ([Financial Times](#))

**Colombia's Verizon-like deal signals more to come**

**Sep 13.** Colombia's state-controlled oil producer, Ecopetrol SA, sold USD 2.5bn bonds during the week ending September 15, in its first overseas offering since 2009 and Colombia's largest issuance ever. Ecopetrol's USD 1.3bn 10-year notes, the biggest portion of the sale, was sold at a price that yields 3.05 percentage points above Treasuries, less than the 3.18 percentage point premium for bonds in emerging markets with similar maturity and credit rating. Dollar debt issuance in the Latin America region has totaled USD 3.7bn this month, more than the total amount issued in August, according to Bloomberg data. ([Bloomberg](#))

**China factory output in August grew at fastest pace since March 2012** ([Wall Street Journal](#))

**UK banks face USD 79bn capital boost in future rules** ([Bloomberg](#))

**Slovenia targets grey economy in push to boost public finances** ([WSJ](#))

**Hungary central bank expands lending plan to boost GDP** ([Bloomberg](#))

**Credit Suisse opens European coco path** ([Bloomberg](#))

**Political turmoil lifts Italian yields above Spain's for first time in 18 months** ([Reuters](#))

**Bank of Korea holds rate steady as economy shows resilience** ([Business week](#))

**Vietnam five-year yield rises to March high as loans sap demand** ([Bloomberg](#))

**Moody's alters sovereign rating method to better assess risk** ([Bloomberg](#))

**Household debt in Malaysia has not reached alarming level, says Zeti** ([Bernama](#))

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