This week, mall operator General Growth Partners (GGP) and newsprint maker AbitibiBowater both filed for bankruptcy, after failing to persuade bondholders to restructure voluntarily.

Now lawyers involved in these bankruptcy proceedings tell the Financial Times that the credit default swaps are the problem -- mainly, bondholders who have purchased CDS on this debt have little incentive to negotiate or play ball, since the CDS, if the counterparty honors the agreement, makes them whole.

FT: Some creditors, including Citigroup, which held a small exposure to AbitibiBowater, hedged themselves in the CDS market, meaning their economic interest in the deal was different to lenders who had not bought credit insurance, according to people familiar with the matter. Citigroup declined to comment.

Lawyers say CDS holdings were also a factor in the default and filing for Chapter 11 protection of General Growth Properties this week. Restructuring advisers expect many more such cases involving so-called fallen angels, or firms originally investment grade, since CDS was widely sold on such names.

Now just take a wild guess. What firm is most likely to be on the other end of Citi's CDS purchase? AIG maybe?

If it is AIG, it means our bailout is pushing companies into bankruptcy that might otherwise be able to restructure.

Note that this has been alleged before, though previously with GM's ongoing failure to get its bondholders to exchange debt for equity. Now those involved in actual bankruptcies are citing it as a problem.

See Also:

Mall Owner General Growth Declares Bankruptcy (GGP)
How AIG Is Driving GM Into Bankruptcy (AIG, GM)
AIG Dismisses Talk Over Ed Liddy's Goldman Shares (AIG, GS)
CDS Blamed For Corporate Bankruptcies

CDS=SCAM. Insurance without reserves is was and always will be a ponzi type scam.

I doubt it is AIG - I don't think they wrote single name corporate exposures. this shorting in the CDS market has been going for a while and many companies have been complaining about it - such as the monolines. when they complained, many people said they were just whining and shorting is all American and essential to the market.

Now that it is showing up in another context - and with a possible connection to the clearly evil AIG - suddenly you are concerned about the perils of shorting CDS? sounds a little suspect

It is shame Joe doesn't understand the difference between Ch. 11 reorganization and bankruptcy. Both companies identified in the article filed for Ch. 11, which is a court administered financial reorganization.

with aig having 4 PR firms, which ones do you work for?

do we have enough jails for all these crooks?????? the seller is a crook and the buyer: they all knew this wasnt insurance!!

AIG and Lehman did post collateral under their CDS (I'm not talking about what AIG did after the bailout - which I view as the US govt posting collateral on their behalf). In fact, the Lehman close-out process was relatively smooth in that respect. Dealers pretty much run hedged books (unlike AIG, which took huge, concentrated directional bets).

So, what "reserves" are you guys talking about? Do insurance companies mark their exposures to market and increase reserves accordingly (like CDS counterparties do via collateral posting)? I don't think that's even possible (e.g. do they increase reserves if there's a bad weather report in florida? or if a policyholder goes to the doctor for chest pain?).

The new CDS clearinghouse is good because, among other things, it erases notional amounts from the system and flat out increases margin requirements. But, there were margin requirements all along for most counterparties.

CDS are not inherently evil. Enough of the demonization (save that for rated structures like CDOs and ABS currently being touted by the government as the answer to our prayers with TALF and Legacy Securities PPIP). Was CDS' popularity due in part to helping dealers keep their margins high since you don't need to disclose individual trades like you do in cash bonds? Yes - but that can be fixed. Should people like AIG be subject to position limits? Probably yes. Are there improvements that need to be made to the product? Yes - and with the big bang protocol and the clearhouses, there are great improvements being made. The one serious problem I see (which is the one this article addresses) is how to deal with voting in bankruptcy -- when a voting unsecured creditor can make more with a bankruptcy filing than a restructuring. But, perhaps that should be addressed in the bankruptcy code instead.

Lets play pretend and blindly assume its AIG so we can vent pent up anger at the system.

Hey,

How bout confirming its AIG or not or who it acutally is.

That is newsworthy.

"hedged themselves in the CDS market"

This makes sense. They insured themselves against a loss in their bonds. Consequently, they will be paid something either way, and are simply trying to figure out the best deal. What's the problem? Wouldn't you do that? The other creditors took a risk by not buying CDS insurance. What am I missing?

@Don: whether there is a problem at all first requires you to make the judgment that restructurings outside of bankruptcy are preferable to actual bankruptcies. If you have that belief, then CDS have been problematic because if a lot of your bondholders are hedged via CDS, then they may prefer a bankruptcy filing (and a CDS payout) over a restructuring. So, you end up with more bankruptcy filings because you can't get the votes necessary to avoid it.

A company is complaining that it couldn't negotiate a restructuring outside of bankruptcy because lenders would not "play ball". So, why/how did you get into the
situation that you needed to restructure? And why do you believe that restructuring outside of BK court is better than in court?

This is a shift where investors have more power and companies (with their many lobbyists) are complaining loudly. So be it. I do not see why a BK restructuring is so bad yet a restructuring outside is good. I suppose it is your point of view that matters.

CDS did not cause anything that got the company to a BK/Restructuring point to begin with. Too much borrowing probably did. Other bad decisions etc.

Agreed with Don the Libertarian (10:36am) as well.

ques said: Apr. 17, 11:43 AM
Anyone know who ACTUALLY wrote the CDSs on General Growth Partners?

cp said: Apr. 17, 11:53 AM
Joe-

The headline is misleading. You are making a declarative statement and your post is speculating. Why not add a ?, or ask for info from your vast readership?

Disappointed when I read through this one. I'm trying to sort fact from fiction.

tv is right.

cityhall said: Apr. 17, 12:25 PM
Assuming CDS writers aren't a class of creditor in bankruptcy proceedings, the real creditors have an incentive to vote for plans that screw the CDS counterparties in favor of uninsured debts in other classes. It shouldn't matter if it's chapter 11 or chapter 7, if the holders of insured bonds can vote against their direct interests in one class, they can presumably collect CDS payouts while preserving more of the company's cash to pay out their uninsured claims.

IHOP said: Apr. 17, 1:13 PM
@cityhall - Yeah, it's definitely a possibility.

I don't see why AIG would be a major seller of single name CDS on abitibi or general growth. It doesn't make sense. If anything, they'd be buyers to use as hedges.

IHOP said: Apr. 17, 1:18 PM
I should clarify and say hedge against any (corporate) CDS CDOs they might own.

Disappointed said: Apr. 18, 8:32 AM
Please don't say "AIG Bailout Pushing Others into Bankruptcy" then say in your post "Who's on the other side? AIG maybe?"

If you have no basis on which to accuse AIG, then please stop spreading disinformation, in time where populism is all the rage and people are ready to chop others' heads off at the drop of a hat.

I myself have been absolutely disgusted with AIG's conduct throughout their bailout, and agree with your assessment of them as a "Black Hole," but you at the Business Insider should know above all that you can't make claims without any evidence.

Jose said: Apr. 18, 5:14 PM
Either way, I still don't understand why taxpayers should have to pay off the gambling debts of AIG Financial Pirates