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Pimco Says Greek Debt Extension May Avoid Triggering CDS (2)
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(Updates with analyst comment in sixth paragraph.)

By Paul Dobson

May 25 (Bloomberg) -- Pacific Investment Management Co.'s head of European credit portfolio management said Greece may manage to extend the maturities of its bonds without causing credit-default swaps to pay out.

"Before you get to a really bad outcome, I think you're going to get some kind of voluntary process in place first and that means it doesn't necessarily trigger CDS, it doesn't necessarily get people into trouble straight away," Luke Spajic said on Bloomberg Television's "The Pulse" today in an interview with Maryam Nemazee. "There will be this kind of soft, coercive suggestion that the debt should be extended."

Greek government bond yields and five-year credit-default swaps surged to records since Luxembourg Prime Minister Jean- Claude Juncker, who also leads the group of euro-area finance ministers, said on May 16 he wouldn't rule out a "reprofiling" of Greek debt. Swaps pay the buyer face value in exchange for the underlying securities or the cash equivalent should a borrower fail to adhere to its debt agreements.

The longer officials are able to draw out the debt crisis, the more time investors have "to immunize against the problems of contagion," said Spajic, who is based in London at Pimco, which runs the world's biggest bond fund. "Policy makers in Europe, the central bank in particular, they're all trying to buy time and ensure that banks in Europe get their capital ratios ready. If this were brought forward to within the next few days, for instance, no one's ready for that kind of event."

Bond Yields

Ten-year Greek government bonds were little changed, with the yield at 16.77 percent, as of 11:11 a.m. in London. The yield reached 17.10 percent yesterday.

European Central Bank leaders and European Union policy makers are working to prevent Greece from defaulting on its debt, with ECB Governing Council member Christian Noyer yesterday saying a restructuring would be a "horror story."
European Union President Herman Van Rompuy said at the Organization for Economic Cooperation and Development in Paris on May 24 that there are "clear red lines: avoiding a default and avoiding a credit event."

"Chances of a non-triggering event are increasing," Peter Schaffrik, head of European fixed-income strategy at RBC Capital Markets in London, said in an e-mailed note. "This could lead to some selling pressure on the underlying bond markets," he wrote, though it's likely that "sizes in the CDS market are simply too small to cause a large stir in the underlying sovereigns markets."

Investors also need to be wary of the impact of sovereign nations' credit on corporate bonds, Spajic said.

"You've got to look at the sovereign very carefully, take a credit view rather than a rate view," and then decide which corporate entities are at risk of contamination, he said.

"Banks are obvious, but other corporates are suffering too. You can point to utility companies in the likes of Portugal, you can look at the banks in Greece. The best example is probably the Spanish banking system," he said.

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