+--+

Euro Finance Chiefs Race to Avert Default as Greek Bonds Drop
2011-06-14 09:38:11.354 GMT

By James Hertling and Jennifer Ryan

June 14 (Bloomberg) -- European finance chiefs begin the final stage of hammering out a Greek rescue to prevent the euro area's first sovereign default after the country was slapped with the world's lowest credit rating by Standard & Poor's.

Yields on 10-year Greek bonds climbed to 17.12 percent today, a record in the 17-nation euro-area's history, before an emergency session of finance ministers in Brussels. They're seeking to narrow differences on how investors share the cost of easing Europe's biggest debt burden and to wrap up a new financing plan at a leaders' summit on June 23-24, a year after Greece received a first bailout.

"The market is placing much too high a probability on this possibility that Greece will default imminently," Peter Westaway, chief European economist at Nomura International Plc, said today on Bloomberg Television's "First Look." "Policy makers just aren't going to let Greece default. It's completely fanciful to think this is going to happen."

S&P said yesterday the nation is "increasingly likely" to face a debt restructuring, reflecting political pressure on investors not to dump Greek holdings. The cost to insure Greek debt, the most expensive in the world, indicates a chance of about three in four that Greece will default in the next five years. The government today sold 1.6 billion euros ($2.3
billion) of 26-week treasury bills at a yield of 4.96 percent.

"Greece will default; it's a question of when, rather than if," said Vincent Truglia, managing director at New York-based Granite Springs Asset Management LLP and a former head of the sovereign risk unit at Moody's. "It's a basic solvency issue rather than a liquidity issue. Only a debt writedown will do."

S&P's Risks

The S&P cut to CCC from B reflects "our view that there is a significantly higher likelihood of one or more defaults," the rating company said. "Risks for the implementation of Greece's EU/IMF borrowing program are rising, given Greece's increased financing needs and ongoing internal political disagreements surrounding the policy conditions required."

While the European Central Bank has said it could accept a plan in which creditors voluntarily agree to buy Greek bonds to replace maturing debt, the monetary policy makers have warned against a German proposal that maturities on Greek debt be extended for seven years, an outcome that rating companies said would be considered a default.

'Very Determined'

“The very determined attitude of the ECB is what makes the involvement of the private sector so explosive,” Commerzbank AG analyst Lutz Karpowitz said today in a note.

The yield difference, or spread, between 10-year German bunds and Greek securities of a similar maturity widened to a record 1,413 basis points.

No other sovereign nation is graded as low as CCC by S&P, a spokesman said by e-mail. Moody Investors Service cut its rating on Greece to Caa1 on June 1, leaving only Ecuador as a worse sovereign risk. Not all countries’ debts are rated.

“The rating agencies are now playing catch-up with the market,” said Gianluca Salford, a fixed-income strategist at JP Morgan in London. “The market is pricing in a very high probability that there will be a credit event around Greece. The agencies are just catching up to the negativity that’s already priced in by the market, not the other way around.”

S&P also said it has a negative outlook on Greece’s debt.

“Our negative outlook indicates that a downgrade to ‘SD’ could occur if Greece undertakes one or more debt restructurings or maturity extensions on terms that constitute distressed debt exchanges as defined by our criteria,” S&P said. SD is a “selective default.” A restructuring would likely “result in one or more defaults under our criteria,” it said.

Recovery Rating

S&P said that its recovery rating on Greece’s debt is ‘4,’ indicating it estimates bondholders would recover 30 percent to 50 percent of their investment.

A “financing gap has emerged in part because Greece’s access to market financing in 2012 and possibly beyond, as envisaged in the current official EU/IMF program, is unlikely to materialize,” the report said.

Greece’s Finance Ministry said in a statement that S&P’s decision “ignores” the “intense consultations” to resolve the nation’s crisis taking place between officials at the European Commission, ECB and International Monetary Fund.

“The decision by Standard and Poor’s also neglects the determined efforts of the Greek government to avoid at any costs any possible violation of Greece’s contractual obligations, and the strong desire of the Greek people to plan for their future within the euro zone,” the statement said.

For Related News and Information:
Search for central bank stories: NSE MONETARY POLICY <GO> Sovereign credit ratings: CSDR <GO> Credit-default swaps: GCDS <GO>

--With assistance from Linzie Janis, Simon Kennedy, Gabi Thesing, Garth Theunissen, Daniel Tilles and Abigail Moses in London and Maria Petrakis in Athens. Editors: Patrick G. Henry, Jones Hayden

To contact the reporters on this story:
Jennifer Ryan in London at +44-20-7073-3492 or jryan13@bloomberg.net;
James Hertling in Paris at jhertling@bloomberg.net

To contact the editor responsible for this story:
Craig Stirling at +44-20-7673-2841 or cstirling1@bloomberg.net