

Lehman and MF Global boost claims trading in Europe

The Lehman and MF Global insolvencies have given a crucial boost to bankruptcy claims trading in Europe, and will develop into a market similar to the US, although not as big. That is the view of Gamma Finance, a London based advisory boutique that puts buyers and sellers of illiquid assets like bankruptcy claims together.

The biggest publicity boost to the market has been the fact that some types of Lehman claims are now trading above par, due not least to big litigation wins by the administrators of the UK-based arm, LBIE.

These European wins by Tony Lomas' team from PricewaterhouseCoopers have added US\$1 billion to the creditors' pot over the last 12 months. This represents under 2 per cent of the estimated US\$53.8 billion outstanding in LBIE claims, although many of these many never been agreed as valid.

Consider this; since Lehman Brothers collapsed in September 2008 the FTSE 100 has risen by 19.3 per cent, while the secondary market price of unsecured claims against LBIE has risen to 20 per cent above par. No wonder bankruptcy claims are beginning to attract interest from a wider circle of players.

This is a big contrast to market sentiment just after the collapse of Lehman, when claims traded hands at around 20 cents to the dollar and many feared a systemic collapse of the global financial system.

Florian de Sigy, founder and managing partner of Gamma Finance, says:

"The secondary market in insolvency claims is a market which did exist prior to 2008/2009, but has taken new shape given these high profile liquidations".

"Constrained asset owners, many of whom have greatly marked down the value of these holdings, now need to take a renewed look at any claims on their books and examine their options," says de Sigy.

"This becomes especially important given that the pay-out process on many of these liquidations will take several more years."

Basel III and Solvency 2

De Sigy believes Basel III and Solvency 2 will prompt more banks and insurers to sell bankruptcy claims, since these measures raise the cost of holding illiquid assets.

He says: "Given the levels of impaired assets being reported across the banking sector at present and the impact this is having on capital ratios, the benefit to institutions of a speedy resolution is understandable, as well as the potential scale of the market."

"However, given the wide variety of claims against different Lehman Brothers entities and the differing prices attached to these, optimising the exit price from such positions isn't straightforward," he says.

Gamma is based in London and has been registered with the FCA since 2009. It has advised on deals across a whole range of illiquid asset types, totalling around US\$1 billion. Its clients include both buyers and sellers of bankruptcy claims, as well as other illiquid assets. On Lehman in particular, the firm has advised hedge and private equity funds, as well as "private equity-esque institutions."

It is not surprising that some holders of claims don't understand the difference between the London-based LBIE and New York-based LBIH, and how the different insolvency regimes play out.

A lot of people find it surprising that claims can trade above par, says de Sigy.

MF Global and the Special Administration Regime (SAR)

The UK authorities reacted to the Lehman collapse by passing new legislation aimed at improving the way the collapse of big, complex financial institutions are handled, the Special Administration Regime (SAR).

SAR has been used to notable effect in MF Global, says Dan Nolan, who advises on bankruptcy claims for Gamma.

Thanks to SAR, says Nolan, "the MF Global administration has moved on very, very quickly, with certain types of claims now trading at close to par."

Other popular bankruptcy claims in the secondary market include those emerging from the Icelandic banks, says Nolan. This leads him to anticipate that the market in bankruptcy claims will grow to become a permanent feature in Europe, although it won't be as large as in the US.

"Banks have always had distressed claims desks," he says. "And there are always businesses that need to be restructured."

It is important that the SAR system is used to encourage a method for easily trading insolvency claims in Europe.

Returning to the example of LBIE, the administrators at PricewaterhouseCoopers estimate that the wind-down of the European arm will take at least another five to eight years. The value of claims can therefore still fluctuate wildly.

"This market won't exist in its current state forever; assumptions can and have changed as cases are settled and judgements made," says Nolan.

"Finding the right buyers for each type of claim is very important. Equally, because the process against Lehman in the US remains at a very different stage, it is important that asset owners understand what type of claim they actually have."