



# **Contingent Convertibles [CoCos] : A Potent Instrument for Financial Reform (World Scientific-Now Publishers Series in Business)**

*George M von Furstenberg*

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Contingent Convertibles (CoCos) represent debt that is subject to being converted automatically into common equity under pre-specified terms of conversion if the chosen regulatory capital ratio falls to a level triggering conversion. CoCos are that subspecies of contingent capital that references regulatory (Basel III) concepts in its triggers. From 2014, trigger points are set by common equity (Common Equity Tier 1 [CET1]) in percent of risk-weighted assets [RWA] or of more complicated measures of total exposure to a variety of risks, particularly credit risk. This is the first comprehensive book on CoCos, an innovative instrument that has attracted growing attention since it was first issued in 2009.

The book is mostly concerned with going-concern ‘recovery-’ rather than ‘resolution-’ CoCos, because avoiding failure and costly disruption of financial networks without government financing is the first order of business. CoCos hold a high promise of providing fully loss-absorbing equity capital when it is most needed and least available to financial institutions. Yet, having grown out of the 2007–2009 financial crisis, they are still an ‘infant’ reform instrument in many respects. Few of the instrument’s design features (or even the rating, regulatory, and tax treatments) are entirely settled. This book seeks to move the discussion toward, and then past, the main decision points so that CoCos can prove their value for contingency planning and self-insurance all over the world. It is intended to increase the ability of issuers and investors to analyze and understand the different kinds of CoCos.

### **Contents:**

- ***Foundations:***

- Introduction
- Overview of Basel III Implementation Most Relevant for Cocos
- Cocos and the Struggle to Preserve Going-Concern Value
- The Treatment of TBTF Financial Institutions in the Last Crisis
- Strategic Policy Objectives in Privatizing the TBTF Backstop

- ***Why Cocos?:***

- High-Trigger Cocos Compared with Other Bailinable Debt
- Self-Insurance with Cocos Compared to Common Equity
- Automatic Cocos Conversion vs. Voluntary Restructuring
- Reasons for Having Cocos Liabilities on the Balance Sheet

- ***Varieties of Cocos Design and Rationales:***

- Determining Conversion Price and Risk Premium in Cocos
- Write-Down-Only Cocos
- Actual or Prospective Recovery Rates from Converting Cocos

- Government Capital Injections and Bailout Cocos
- Misuses of Cocos in Government-Led Recapitalizations of Banks

- ***Policy Choices and Essentials for Cocos' Success:***

- The Tax Treatment of the Interest Paid on Cocos
- Major Credit Rating Agencies' Approaches to Rating Cocos
- Regulatory Requirements at Cross-Purposes
- Conclusions and Recommendations for Cocos Design and Evaluations

**Readership:** Researchers in Banking, Finance, and Financial Service, Finance Professionals, Law Firms, Accounting, and Financial-Consulting Firms; Portfolio and Wealth Management Specialists; Fixed-Income Investors and Fund Managers; Government Regulators of Financial Services; Libraries and Members of Research and Capital Markets Divisions at National and International Financial Institutions.

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