

CDO Newsletter

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THE IMPACT OF THE TRIBUNE COMPANY CREDIT EVENT ON CANADIAN CDO TRANSACTIONS

On December 8, 2008, Tribune Company (Tribune) filed for bankruptcy under Chapter 11 of the *United States Bankruptcy Code*. The filing triggered a credit event under the standardized International Swaps and Derivatives Association, Inc. (ISDA) contracts and documentation, used by market participants when entering into credit default swap (CDS) transactions. Tribune is referenced in 35 of the 77 Canadian CDO transactions monitored by DBRS.¹

Tribune was downgraded to D by DBRS on December 8, 2008. The previous rating of Tribune's senior unsecured MTNs and Debentures was CCC, with a Negative trend. When rating CDO transactions, DBRS typically applies a fixed recovery rate in the range of 33% to 40% to all underlying corporate obligors, depending on the rating of the CDO tranche.² (Note that this is an assumption applied for modeling purposes only.) However, on July 10, 2008, DBRS assigned recovery ratings to the classes of debt issued by Tribune. The senior unsecured notes received a recovery rating of RR6, which corresponds to an anticipated recovery of 0% to 10%. DBRS assigned a recovery rating of RR2 to Tribune's Secured Bank Debt and noted that "while the next three levels of debt may rank differently from a legal perspective in terms of their position in a bankruptcy, DBRS's analysis suggests that even in an optimistic default scenario, all three of the levels would expect to receive negligible repayment, if any." Based on DBRS's analysis, there is a high probability that the Tribune credit event will yield very little recovery value.

To demonstrate the level of ratings stability of the 35 CDO transactions that reference Tribune, DBRS applied two stress scenarios: (1) assume immediate default by Tribune with a 33% recovery and (2) assume immediate default by Tribune with 0% recovery, which is a more realistic scenario based on DBRS analysis. Both stress tests also incorporate all of the credit events that have affected each CDO transaction over the past few months.³

For the scenario assuming 33% recovery for Tribune, the model results indicate that all 35 transactions would be able to withstand this scenario and maintain their current or implied rating (as shown in the table below). Since Tribune was rated CCC in the months leading up to the credit event, DBRS had already incorporated a high probability of default into its modelling for CDO surveillance. As a result, the impact of the default occurring is negligible when a 33% recovery rate is assumed.

Scenario 1: 33% Recovery for Tribune

Required Downgrade from Scenario (Number of Notches)	Number of Transactions
0	35
1	0
2	0

For the scenario assuming zero recovery for Tribune, the model results indicate that 30 of the 35 transactions would be able to withstand this scenario and maintain their current or implied rating (as shown in the table below). With the zero recovery assumption, a larger amount of portfolio loss is realized from the credit event and five transactions would require actual or implied downgrades of one or two notches.

Scenario 2: 0% Recovery for Tribune

Required Downgrade from Scenario (Number of Notches)	Number of Transactions
0	30
1	3
2	2

The required subordination levels have increased for all of the CDO transactions with exposure to Tribune, assuming a recovery of close to zero. Most of the transactions still have sufficient subordination to withstand the stress scenarios applied. However, further ratings migration or losses from future credit events affecting the transactions may result in negative rating actions. For the transactions requiring downgrades under the scenario above, future rating actions will depend on the final recovery of Tribune.

DBRS-rated CDO transactions may be funded by asset-backed commercial paper (ABCP) or other sources. Revisions to the ratings of the transactions may affect the ratings of such ABCP or other notes.

DBRS will continue to monitor the situation and release further information as appropriate on www.dbrs.com.

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1. The 77 Canadian collateralized debt obligation (CDO) transactions mentioned in this newsletter include all public transactions rated by the DBRS Canadian Structured Credit Group that reference corporate obligors, as well as transactions that are not currently rated but are part of a restructuring process under the Montréal Accord. For the purposes of this newsletter, DBRS will use the terminology “implied rating” when referencing the credit strength of transactions covered by the Montréal Accord. Please note that all transactions rated by the DBRS U.S. Structured Credit Group and all private transactions are not included in the transaction total.

2. A small number of the transactions have fixed recovery rates for each of their reference entities (normally between 30% and 40%). In the scenario analysis, DBRS has applied the appropriate fixed recovery rates for these transactions.

3. Credit events that have occurred over the past four months affecting CDOs rated by DBRS include events related to the following entities: Tembec Inc., Fannie Mae, Freddie Mac, Lehman Brothers Holdings Inc., Washington Mutual, Inc., Glitnir Banki hf., Landsbanki Íslands hf, Kaupthing Banki hf. and Controladora Comercial Mexicana S.A.B. de C.V.

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