

Triple A rated risk-taker opens up shop

A new risk-taker entered the credit derivatives market last week in the form of Primus Financial Products, the first company to obtain a Triple A rating as a prelude to investing by selling credit default swaps. Other investors may copy the approach used by Primus, which would increase the number of outlets that hedgers of risk can use to buy credit default protection and could help smooth credit spread movement.

Primus Financial Products is due to begin trading credit derivatives on May 1 after securing US\$270m of financing last week. It will be the first Triple A rated company to specialise in taking on risk by selling credit default protection swaps on investment-grade entities.

The company expects to sell US\$5bn–\$6bn of notional principal of default swaps within its first year of operation and as much as US\$50bn within five years, which will make it a significant player in the rapidly expanding credit derivatives market.

Primus is run by two highly experienced derivatives professionals. Chief executive *Tom Jasper* is a former global treasurer of Salomon Smith Barney and was co-founder and initial chairman of the International Swaps and Derivatives Association. Chief financial officer *Joe Bauman* is a former head of derivatives sales and structuring at Bank of America, and has also served as ISDA chairman.

The business model for Primus has changed over the last 18 months, as it has sought money in a difficult market for capital-raising. Its initial business model envisaged offering online prices on as many as 1,200 separate credits. Instead, it typically will offer to sell protection on 25 to 50 credits at any give time.

The focus on credit risk that is directly managed by the principals of Primus brought capital from four institutions, with Bermuda reinsurer XL Capital taking the lead investor role. *Michael Esposito*, XL Capital's chairman, has been named chairman of Primus Guaranty, the parent company for the venture.

Calpers, the California state pension fund, is also an investor through Calpers/PCG Corporate Partners, in what is believed to be the first direct investment in a credit derivative trading operation by a pension fund.

Primus Financial's parent company has raised US\$155m of cash equity and has a US\$115m excess loss insurance policy provided by one of its investors, Radian. Aegon USA is the fourth investor. Primus will seek to beat bond fund and CDO performance by selling default swap protection on select credits. It will be able to buy back protection if it thinks a credit looks like going under, but will not routinely buy swaps to manage its performance, according to Jasper.

Charles Truett, formerly senior credit officer for Bank of America, will be chief risk officer of Primus Financial, and will be hiring staff to help monitor risk positions. *Alec Rainsby*, a former managing director at Merrill, will be chief technol-

ogy officer. The company expects to have around 20 staff by the end of the year, according to Bauman.

Gregg Whittaker, former global head of credit derivatives at Chase, who had been involved in the Primus launch plans, dropped out of the project a few months ago.

Primus expects that it will sell protection mainly to dealers at first, though also to credit portfolio managers at major banks. Buyers of protection will be able to trade with Primus online, or by phone.

A number of banks are facing losses on swaps they bought from the now-defunct Enron Credit, so they will be examining the Primus legal structure closely. The addition of a Triple A rated risk-taker to the credit derivatives market is likely to be welcomed by dealers, however. Primus will turn over information about its positions to the rating agencies each week, as part of the arrangement it made to obtain its ratings, which should give extra comfort to dealers buying protection.

The principals at Primus will decide the initial credits on which to sell protection closer to the target launch date of May 1. "The mantra in the first year is diversification and high credit quality," said Jasper.

Jon Macaskill