

## Equity Research

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## Industry Report

## Financials

### Bond Insurers

#### Negative Reaction of Shares in MBI, AGO, AMBC to GDB-Specific Litigation Driven by Media Misread

Shares of bond insurers MBIA (MBI, Buy, \$13 PT), Assured Guaranty (AGO, Buy, \$35 PT) and Ambac Financial Group (AMBC, Neutral) were weaker earlier today, underperformance that may have been a reaction to [a lawsuit filed by a group of hedge funds](#) against Puerto Rico's Government Development Bank (GDB) in the U.S. District Court of Puerto Rico. The litigation was aimed at halting the GDB from making transfer payments to selected creditors to the detriment of the holders of its \$3.75bn in bonds until after the bank's debt has been restructured.

- ▶ While we believe the hedge funds' lawsuit does not represent a negative for the bond insurers, some media sources reported on the lawsuit as if it applied to all of Puerto Rico's debt. "A group of hedge funds sues to keep Puerto Rico from making payments to creditors prior to restructuring its debt," tweeted one reporter.
- ▶ Meanwhile, another media source reported that "a lawsuit has just been filed" to "prevent muni bond holders of Puerto Rican debt from withdrawing their money." The report did not provide specifics about the lawsuit, so we assume they are referring to the one filed by the hedge funds against the GDB. If that was indeed the case, the report blatantly mischaracterized the nature of the legal action and may have raised unwarranted concerns among investors in the bond insurer stocks, in our view.
- ▶ The implication is that the hedge funds are concerned that the GDB is likely to default on its bonds in the near future, and that it has been making "preferential payments and transfers" to "selected government depositors" as they "race for the exits." The hedge funds note that the payments and transfers in question are prohibited by Puerto Rico law and divert cash from bondholders and other depositors.
- ▶ If anything, the hedge funds' lawsuit is a positive for holders of GDB bonds insofar as it represents a step to preserve the cash that would support interest payments or that would ultimately contribute to bondholders' recovery. We have no doubt that Puerto Rico's bondholders and bond insurers will use every legal means at their disposal to protect their interests as the Commonwealth's debt saga plays out, and we think the funds' lawsuit is an early example of many more legal actions to come.

## Appendix: Analyst Certification and Other Important Disclosures

### Analyst Certification

I, Mark Palmer, hereby certify that the views about the companies and securities discussed in this report are accurately expressed and that I have not received and will not receive direct or indirect compensation in exchange for expressing specific recommendations or views in this report.

I, Giuliano Bologna, hereby certify that the views about the companies and securities discussed in this report are accurately expressed and that I have not received and will not receive direct or indirect compensation in exchange for expressing specific recommendations or views in this report.

### Regulatory Disclosures

#### Analyst Stock Ratings Definitions

**BTIG LLC's ("BTIG") ratings, effective May 10, 2010, are defined as follows:**

**BUY** – A stock that is expected at initiation to produce a positive total return of 15% or greater over the 12 months following the initial recommendation. The BUY rating may be maintained following initiation as long as it is deemed appropriate, notwithstanding price fluctuations that would cause the target to fall outside of the 15% return.

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**Distribution of BTIG's Research Recommendations (as of December 31, 2015):**

**BUY: 64.5%; NEUTRAL: 31.7%; SELL: 3.8%**

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**BUY: 89%; NEUTRAL: 5.5%; SELL: 5.5%**

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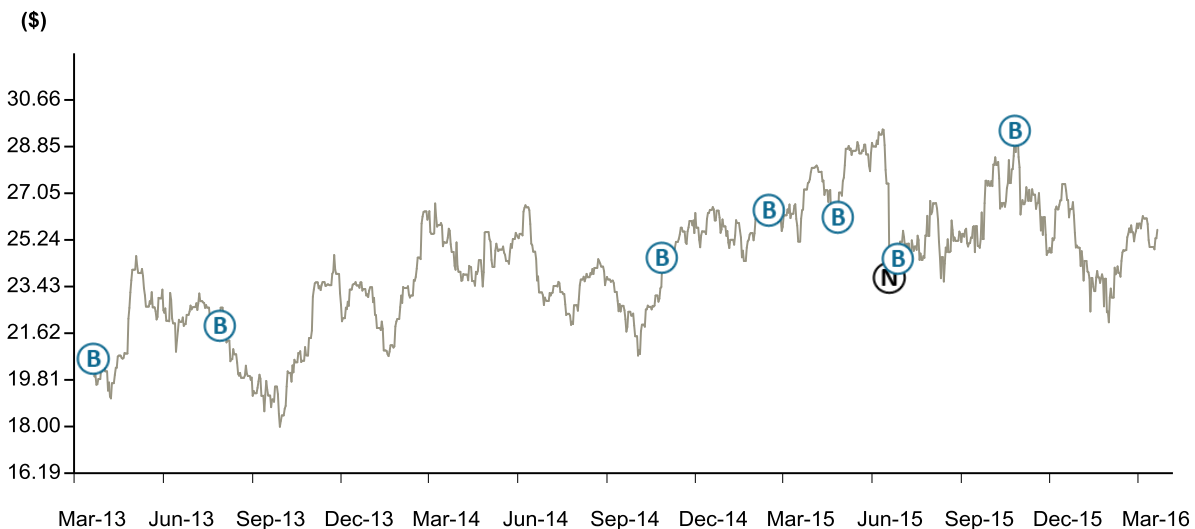
### Company Valuation and Risk Disclosures

#### Assured Guaranty Ltd. (AGO, Buy)

**Valuation:** Our \$35 price target is based on 0.60x our YE16E adjusted book value (ABV) per share of \$63.84, minus \$6.04 per share representing the estimated impact of potential losses related to AGO's insured exposure to Puerto Rico's debt.

**Risks:** The primary risk to achieving our target price include ratings downgrade risks, credit risk related to municipal bond and structured product exposures, and exposures to troubled Puerto Rico credits.

### Assured Guaranty Ltd. (AGO)



*Note: Closing Price and Target Price have been adjusted for corporate actions.*

Date	Closing Price (\$)	Target Price (\$)	Analyst	Rating
05-Dec-11	12.23	35	Mark Palmer	Buy
29-Feb-12	16.80	37	Mark Palmer	Buy
07-Aug-12	11.72	35	Mark Palmer	Buy
08-Aug-13	21.91	37	Mark Palmer	Buy
07-Nov-14	24.53	39	Mark Palmer	Buy
25-Feb-15	26.37	40	Mark Palmer	Buy
07-May-15	26.11	41	Mark Palmer	Buy
29-Jun-15	23.76		Mark Palmer	Neutral
08-Jul-15	24.49	34	Mark Palmer	Buy
05-Nov-15	29.47	35	Mark Palmer	Buy

### MBIA, Inc. (MBI, Buy)

**Valuation:** Our \$13 price target on MBI is based on 50% of our estimate of the company's ABV per share of \$32.24 adjusted for estimated losses of \$5.49 per share related to the company's insured exposure to Puerto Rico's debt.

**Risks:** The primary risks to our valuation include greater than expected losses with respect to insured exposure to Puerto Rico's debt. Increased losses on the broader insured municipal portfolio. The potential negative impact of a credit rating downgrade on ability to write new business.

# **MBIA, Inc. (MBI)**



*Note: Closing Price and Target Price have been adjusted for corporate actions.*

Date	Closing Price (\$)	Target Price (\$)	Analyst	Rating
30-Nov-11	9.70	22.50	Mark Palmer	Buy
30-Jun-14	11.04		Mark Palmer	Neutral
15-Aug-14	10.49	12	Mark Palmer	Buy
12-May-15	9.09	13	Mark Palmer	Buy
29-Jun-15	6.37		Mark Palmer	Neutral
23-Jul-15	6.29	10	Mark Palmer	Buy
05-Nov-15	8.28	11	Mark Palmer	Buy
01-Mar-16	7.93	13	Mark Palmer	Buy

## **Ambac Financial Group, Inc. (AMBC, Neutral)**

**Valuation:** Based on our Adjusted Book Value (ABV) per share multiple valuation for Ambac Financial Group and our recovery analysis, we do not believe that Ambac's valuation is within +/- 15% from current levels over the next 12 months. BTIG does not put price targets on Neutral-rated stocks.

**Risks:** The primary risks to achieving our recommendation include the possibility that reserves against losses associated with RMBS and other insured instruments may prove inadequate, that fiscal stress of state and local governments could translate into increased losses, and that declines in value of investment portfolio could impede Ambac's ability to pay its liabilities.

### Ambac Financial Group, Inc. (AMBC)



*Note: Closing Price and Target Price have been adjusted for corporate actions.*

Date	Closing Price (\$)	Target Price (\$)	Analyst	Rating
16-May-13	23.67	31	Mark Palmer	Buy
04-Mar-14	34.49		Mark Palmer	Neutral

## Company-Specific Regulatory Disclosures

**BTIG LLC expects to receive or intends to seek compensation for investment banking services in the next 3 months from:** Ambac Financial Group, Inc. (AMBC), Assured Guaranty Ltd. (AGO), MBIA, Inc. (MBI)

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**BTIG LLC had an investment banking services client relationship during the past 12 months with:** Ambac Financial Group, Inc. (AMBC), Assured Guaranty Ltd. (AGO), MBIA, Inc. (MBI)

**BTIG LLC managed or co-managed a public offering of securities in the past 12 months for:** MBIA, Inc. (MBI)

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**Additional Information Available Upon Request**

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