Pricing of Contingent Convertible Bonds
M.J.M. Derksen

Abstract

Contingent Convertible bonds (CoCos) are bonds designed to convert to equity when a bank is close to becoming insolvent. This conversion is typically triggered by an accounting ratio falling below some threshold. However, in the existing literature on the pricing of CoCos no difference is made between accounting values and market values. In this thesis a model is proposed which attempts to fill this gap. In the proposed model, debt is valued under the assumption that the only information available is noisy accounting information, which is only received at discrete moments in time. In this way, it is possible to distinguish between market values and book values in the valuation of CoCos. Another important contribution of the model is the inclusion of the MDA regulations concerning the payment of coupons.