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Hedge funds give Greek bonds wide berth

By Sam Jones and Caroline Binham in London

For the hedge funds circling Greece, one thing seems clear – for now, the law is not on their side.

In recent weeks lawyers and traders at top hedge fund firms have pored over the country's laws and constitution – even looking at possible routes of appeal to the European Court of Human Rights – in search of ways in which they might lever greater concessions in the fraught negotiations through which the Greek government hopes to restructure its debts.

But there are few, if any, methods for challenging the government to pay larger sums than are currently being offered. The problem: nine-tenths of Greece's bonds are under the sole jurisdiction of Greek, and not international, laws.

It is a conclusion reflected in the conspicuous absence of one big group of hedge fund managers from the talks to date – the distressed debt specialists, more unkindly known as vulture funds, that might ordinarily have piled into Greece's highly discounted bonds, which trade for a fraction of their par value.

US hedge fund firms such as Elliott Associates and Gramercy, with histories of taking on governments through long and protracted legal battles to extract value, have largely passed Greek bonds over.

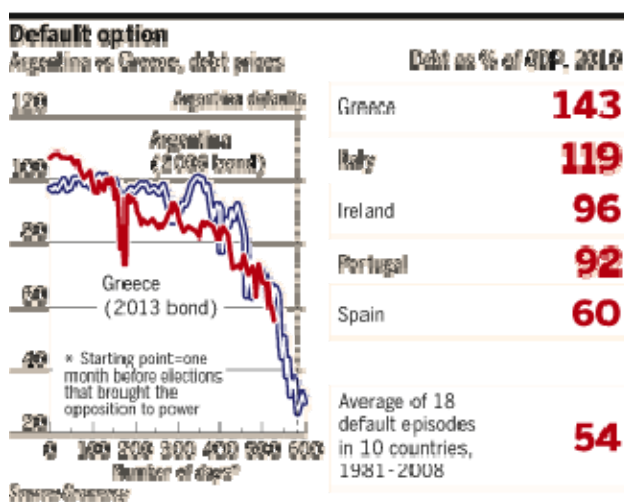
Other debt trading hedge funds, such as Och-Ziff and York Capital, have even been forced to issue terse press releases denying their involvement.

As Rob Rauch, head of research for Gramercy, a \$2.7bn Connecticut-based fund manager that led the pack of creditors negotiating Argentina's debt restructuring in 2007, points out, investors that have bought so far have mostly been "long and wrong".

"The terms of the Greek law debt [debt issued under Greek law] can be changed by government fiat – there is no recourse for holders of that debt," says Mr Rauch.

Whitney Debevoise, partner at the US law firm Arnold & Porter and a former executive director of the World Bank, says: “The most likely outcome [of a legal challenge] is that you are faced with a long road and a lot of transaction costs just to get a restructuring of the instrument you already hold.”

Just two hedge funds have been actively involved in the current PSI discussions between creditors and the Greek government – Marathon and Greylock Capital – and both are pushing for a “voluntary” agreement rather than seeking legal action. Other hedge funds have taken positions based on tactical, short-term trades, with little interest in negotiations.



Ways in which more active hedge funds have challenged sovereign creditors in the past, such as suing governments in the US, are unlikely to be viable in the Greek case. While some Argentinian bonds had clauses which submitted to the jurisdiction of the New York courts, Greek law bonds do not.

“In the US, for a Greek law bond, there’s almost zero chance of any type of action that could turn up any Greek assets,” says Mr Debevoise.

“Lots of people talk about it, but they don’t really consider what assets we are talking about. It’s a lot of brave talk. If the National Greek Bank had deposits [in the US] they would be protected.”

The potential for legal challenges therefore hinges on whether the Greek government passes legislation retrospectively to introduce so-called “collective action clauses” into its debt, under which recalcitrant bond holders could be forced to accept restructurings by a majority vote.

Creditors could first seek to challenge such Greek CAC legislation locally on the grounds that it was unconstitutional, but the process would be lengthy, costly, and likely unsuccessful, lawyers warn. Challenges in US or UK courts about the recognition of such law would also be tricky, since a claimant would have to argue that the Greek government’s actions amounted to confiscation and had failed the “Wednesbury” test of unreasonableness in public bodies.

A final option – to mount a challenge under protocol one of the European Convention on Human Rights, which protects against depriving property without due process and compensation – would, meanwhile, take “years”, according to a partner at one magic circle law firm in London who said it was “in the realm of fantasy football”.

Only one factor gives hedge funds some succour that a legal challenge could succeed – or at least have grounds to be taken seriously as a threat: the position of the European Central Bank.

The ECB and other European central banks’ insistence on their exemption from any voluntary restructuring on their €50bn of Greek bond holdings could yet leave Greece open to attack – if not only on legal grounds, then for the risk of setting a dangerous precedent to spook bond holders in the eurozone’s other troubled economies.

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