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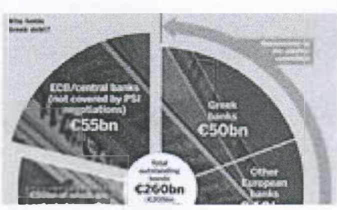
# Greek debt talks open Pandora's box

By Sam Jones in London

Greek negotiators may be about to reach a final agreement with creditors on the country's huge debt burden but, as with the original bonds, any deal may not be worth the paper it is written on.

Fraught discussions on Wednesday – led on the creditor side by veteran technocrats Jean Lemierre, special adviser to the chairman of BNP Paribas, and Charles Dallara, managing director of the Institute for International Finance – have hit on a formula with Greek officials that an untested minority of bondholders could yet reject.

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Several hedge fund managers that hold Greek debt have said they have not been involved in the talks and will not be agreeing with the "private sector involvement" (PSI) deal – which centres on a 50 per cent loss on bondholders' capital and a reduction in the interest they receive.

Alongside them are insurance companies, fund managers and pension funds that also have little incentive in agreeing to the negotiated terms.

The creditor steering committee Mr Lemierre and Mr Dallara head represents bondholdings worth an estimated €155bn of Greece's outstanding €260bn debt. That leaves a further €50bn or so of such uncanvassed private bondholders once European Central Bank and eurozone national central bank holdings are excluded, according to estimates by JPMorgan.

It is these private bondholders that must now be brought on board for a negotiated settlement if the Greek government is to succeed in its goal of a "voluntary" debt swap on its full borrowings and avoid a default.

"The [expected] agreement is a short-term fix. The market will be happy with it for a few days or a week but then we run into the hard stuff," said an executive at one multibillion-dollar hedge fund that owns Greek bonds and has not been party to the negotiations. "The hard part is going to be getting the rest of the bondholders [outside the creditor committee] to agree."

Even members of the committee concede the process is unlikely to succeed in time for the crunch date: a €14.5bn bond repayment falling due on March 20.

"As a firm we are not convinced that any deal today is the last deal," said Robert Rauch, director of research at the $2.7bn hedge fund Gramercy, which led negotiations for bondholders in the restructuring of Argentina's debt in 2007. "This is a multiplayer negotiation and not all the players are even at the table."

Gramercy is one of numerous hedge funds that say they have avoided buying into Greek debt – even though it has been trading at huge discounts in recent months – because they still do not see it as cheap enough.

"The eventual solution for Greece is at least two, three if not four years off and will involve two, maybe several, rounds of haircuts to get to something final," said Mr Rauch.

The biggest hedge fund holders of Greek debt include Marathon Asset Management, Vega Asset Management, Greylock Capital and Saba Capital. Many more have remained outside the official discussions, however. For several, bets on Greek bonds have so far proved to be lossmaking.

The options available to Greece and its advisers, Lazards and Cleary Gottlieb, should full agreement fail are hardly attractive. Foremost among them would be Greek legislation to insert "collective action clauses" into the country's existing debt stock.

Such clauses could be exercised to force a recalcitrant minority of bondholders to agree new terms, but in doing so they could trigger credit default swaps written on Greek debt – a dangerous move that could trip the eurozone into a full-blown banking crisis.

Part of the problem was that many of Greece's unknown creditors were thought to be holding out for exactly such a CDS trigger, one fund manager said.

Insurance companies in particular, bank traders note, were buyers of Greek CDS in an effort to try to hedge their exposures last year and now are likely have little incentive to stomach a painful debt swap.

"There isn't much of a reason for anyone to agree to the terms precisely because of the threat of CAC clauses," said a fund manager who owns Greek debt. "If people think they are going to get forced into a deal anyway, then why agree to the terms before you have to? Especially if by not doing so you can trigger your CDS."

Whatever the outcome of negotiations in the run up to March, there is little doubt among many bond investors about the worth of the PSI process.

As the Emerging Sovereign Group, a $1bn hedge fund owned by US private equity giant Carlyle, told its clients last year, European politicians have opened a "Pandora's box" that now looks likely to lead to a "repricing of sovereign default risk across the euro area".