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Ukraine Creditors' Debt Plan Based on Raiding Central Reserve

By The Moscow Times

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LONDON — A debt restructuring plan proposed by Ukraine's biggest bondholders is based on raiding central bank reserves for up to 40 percent of the amortizing debt, but that would be illegal under Ukrainian law, a source with knowledge of the discussions said on Friday.

A creditors' committee, led by Franklin Templeton, has put forward a plan that would save Ukraine $15.8 billion, or more than what it is aiming for, via extending bond maturities by up to 10 years and by cutting coupon payments in initial years, a separate source had said earlier.

But another source familiar with the situation said that the creditors' plan envisaged funding $8 billion — or 40 percent — of the bond amortization's by raiding central bank reserves.

"What will be difficult in this proposal is that 40 percent of the debt is amortized directly by using the reserves of the central bank of Ukraine and that is illegal under Ukrainian law. It demonstrates that nominal haircuts are absolutely inevitable," the source said.

The creditors have said they will not accept a write-down in the bonds' principal while Ukraine says it will not be able to meet the targets set out in an IMF-led rescue package without cutting the bonds' principal. About $23 billion worth of debt is earmarked for restructuring.

Pressure is building on the creditors to take a write-down on the bonds’ principal. Ukraine has passed a law allowing it to impose a moratorium on debt payments. Former U.S. Treasury Secretary Lawrence Summers recently called the bondholders “selfish” and Treasury Secretary Jack Lew has called on them to make “sacrifices.”

The bondholders have responded by citing their efforts to enable Kiev to meet restructuring targets.

“The bondholders are not vulture funds looking for a quick return, they are long-term investors who want a sustainable economy for Ukraine and they believe it’s possible to do this without a haircut,” a source close to the creditors said.

In a statement Friday, Ukraine's Finance Ministry said talks with creditors were gaining momentum and will continue when the side's advisers meet in London next week followed by a teleconference between Kiev and the ad-hoc creditors' committee on June 5.

"The ministry is pleased that engagement between both parties on restructuring Ukraine's sovereign debt is accelerating," the statement said.

The source said that while coupon reductions would save Ukraine $350 million in the initial years, the plan also envisages an annual step-up in coupon interest in later years that would end up adding $1 billion to debt servicing costs over and above what would be acceptable to Ukraine.

"That will end up costing Ukraine much more," the person said.

Ukraine had set itself a deadline of reaching a debt restructuring deal before the International Monetary Fund concludes its review in mid-June.

Ukraine is being advised by Lazard while the creditor committee is represented by Blackstone.