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Peru's Land-Reform Bondholders' Plight

Report Categories:

Trade Policy Monitoring

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Report Highlights:

Peru on January 18, 2014, passed Supreme Decree 017-2014-EF. The decree details procedures as to how Peru will compensate land-reform bondholders. The land-reform bonds were originally issued in the 1970s as compensation for land seized for redistribution among Peru's poor by then leftist dictator General Juan Velasco. Prior to the Constitutional Court's decision, which effectively allows the government to pay a fraction of the amount owed – by some estimates as little as \$400 million – government and private estimates had valued the bonds at between \$1 billion to \$8 billion. FAS Lima foresees the government of President Ollanta Humala favoring the least onerous compensation method; most likely a combination of new government-issued bonds and government-owned agricultural land. Reportedly bondholders are considering suing Peru in foreign or international courts.

General Information:

Peru on January 18, 2014, passed Supreme Decree 017-2014-EF. The decree details procedures as to how Peru will compensate land-reform bondholders. The decree brings the Government of Peru into compliance with the Constitutional Court's ruling of July 16, 2013 (reaffirming the earlier 2001 sentence), whereby the government is legally required to honor its bond debt. The land-reform bonds were originally issued in the 1970s as compensation for land seized for redistribution among Peru's poor by then leftist dictator General Juan Velasco. Subsequent presidents have strongly resisted honoring the bond debt.

Bondholders are given five years to submit their cash out requests. Upon the application's receipt, the Ministry of Finance will verify the veracity of the land-reform bond claim. Bondholders become eligible for payment only after the ministry's confirmation of the bond's authenticity (which can take upwards of two years). Once eligibility is established, the government can take an additional eight years to pay the bondholder. Prior to the Constitutional Court's decision, which allows the government to pay a fraction of the amount owed – by some estimates as little as \$400 million – government and private estimates had valued the bonds at between \$1 billion to \$8 billion.

The decree adopts the valuation method, one of the three methods recommended by the Constitutional Court. Detrimental to bondholders' interests is that the method selected allows the government to fix the bonds' cash out payments to the dollar's exchange rate prevailing on the bonds' date of issue (by when the local currency had been devalued) instead of utilizing the expropriation date as the baseline year. The U.S. Treasury bond interest rate, currently one of the lowest rates in world, will be used to calculate the bonds' accrued interest value.

Eligible bondholders are required to select a payment method; which include cash payments, new government-issued bonds, and government-owned land and or tax credits. FAS Lima foresees the government of President Ollanta Humala favoring the least onerous compensation method; most likely a combination of new bonds and government-owned agricultural land. Incidentally compensation in the form of government-owned land will facilitate the Humala government's policy of bringing idle lands suitable for agriculture into production.

Article 19 of the Decree details the priority whereby bond holders will be paid:

1. Original bondholders, 65 years old or older, or their heirs.
2. Original bondholders, younger than 65 years old, or their heirs.
3. Non original bondholders 65 years old or older.
4. Non original bondholders younger than 65 years old.
5. Institutions that are original bondholders.
6. Institutions that are not original bondholders, but have received the bonds as payment for legitimate debts.
7. Institutions that are not original bondholders and that acquired the bonds for speculative purposes.

Bondholders are considering suing Peru in foreign or international courts. Connecticut-based hedge

fund Gramercy, possessing approximately 15 percent of these bonds is one of the largest bondholders.
See also **GAIN Peru (Internal) Land Reform Debt 7/22/2013**.