

Dealing Justly With Debt

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I presume that there are few dissenters from the general proposition that we should try to deal justly with debt. That's the simple, and positive, part. The real issue turns on what that means in practice and how it is to be achieved.

The title of this forum stimulated me to go to the dictionary to see if there was any guidance to be gotten there on how to deal justly with debt. Webster and Oxford define "just" as "reasonable" (a just but not generous decision) and as "in conforming with what is morally upright or good" and "rendering everyone his due". They define "justice" as: "the quality of conforming to law" and "the administration of what is just, especially by the impartial adjustment of conflicting claims".

While the spirit of these words is unassailable, I was disappointed by this search! I don't see that it provides much operational guidance as to what to do about the kind of debt we are presumably here to talk about. If "justice" means conforming to law, that could be taken as an endorsement of the sanctity of contracts and leave little room for seeking anything other than the full repayment of debt—assuming, of course, that the contracts are valid! I'll come back to that in a minute. If "just" refers to "mostly upright", that would seem to open a wide variety of views and approaches, but they would probably lead quickly to conflicting views as to what is morally correct or acceptable.

Notwithstanding the lack of operational guidance here, the reality is that there is a broad acceptance of the proposition that debt can become unpayable and a recognition that certain circumstances may warrant a change in even perfectly legally grounded claims. Bankruptcy legislation, which exists in almost all domestic legal systems, is one such recognition of this reality. Bankruptcy law, and the practices associated with it, help deal with the unpayable debt of corporations and individuals and permit a modification of the original contracts under which creditors have a right to full repayment. These systems by no means work equally well in all countries, but that is being improved. Even in the best of systems, however, difficult judgments are required regarding the capacity of the individual or the corporation to service its debt. Take the airline cases now under negotiation. How much concessions should be gotten from the various unions—and maybe even from the chief executives!—before creditors should agree to a reorganization that involves a write down of their claims?

But even these difficulties pale in comparison to those confronted when the debtor is a sovereign government who borrowed internationally under the law of another country, as has been the case in so many recent financial crises. Here, domestic bankruptcy law does not apply. And there are few rules or guidelines about how to measure capacity to pay or to determine what concessions must be made by the many involved parties.

But what is an unpayable debt in the context of a sovereign government? For any government, its capacity to service its debt is a function of its revenue generating capacity and the decisions made regarding expenditures other than debt service. A government can, in some sense, always tax more or spend less to make resources available to service its debt. But where does one draw the line? Too much taxation can, in the end, be economically inefficient and counterproductive. Reducing expenditures can cut into basic services that many would rank morally preferable or in some way more desirable than debt service.

Here, while I personally have great sympathy and respect for some of those in the NGO community and elsewhere arguing the case for debt relief, I don't find the case they make operationally very helpful. The issue is made even more complicated in the case of poorer countries, where it must be seen in the broader context of the entire package of financial assistance the country may be receiving. Part of the motivation for this assistance is to help the country promote its own development and to help it finance needed social services for its public before it is capable of providing for those needs from its own resources. Debt relief can free up budgetary resources that would otherwise be used to service that debt. It can be a one off, permanent provision of help to the country. Other forms of aid increase the total resources available to the country. These forms of aid tend to flow over time. There are advantages and disadvantages to each of these forms of assistance. But it is also the reality that they are, in part at least, substitutes for each other. More debt relief provided by governments can, and sometimes does, reduce the resources available to support other forms of aid.

Thus, the question of justice should not be seen simply in terms of debt relief. It should be seen, instead, in the context of all the various instruments through which the richer countries of the world deal with the poorer countries. This makes the operational task of helping these countries more complicated than simply calling for greater debt relief. Most people in the official international community see the issue in this broader context. In this view, the aim should be to get the country's debt to a sustainable position and deal with the broader needs of the country through the full array of aid and other mechanisms that are available—and, indeed I would argue, to enlarge and enhance these initiatives!

Let me give you some additional examples of the problems I see with the position on debt taken by some in the NGO community. The Jubilee USA Network says that "... debts whose service causes impoverished people to be denied access to education, health care and clean drinking water" should be declared invalid through an arbitration process.¹ This is emotionally appealing. But is it operational? Consider even the U.S. There are unquestionably impoverished people—and in fact a growing number—in the U.S. who are receiving inadequate schooling with devastating effects on their capacity to reach their potential, and, from that, a loss to the economy. Should the U.S. government cease servicing some of its debt and devote that money to education? Most people, I suspect, would say no, but may argue that, to the extent there is a real issue here, it should be dealt with through increased taxes or lower expenditure elsewhere, actions on which there may be little flexibility in the poorer countries. One could make an additional argument here that may apply to poorer countries as well, that tampering with the debt will reduce access of the government to financial markets and thereby reduce the potential to invest in schools and hospitals, thereby hurting those the debt relief is intended to help.

But, there is a further problem with the idea of "arbitration". The NGOs do not want the IMF setting the financial envelope for debt relief, nor do they accept that it should be left to the debtor

and the creditors, who they fear, I presume, may negotiate a deal hurtful of the poor. Hence, they propose a neutral arbitration, informed by civil society, and instructed to find a "just" haircut to be applied to the creditors. They say this is what occurs under Chapter 9 of the U.S. bankruptcy code and that should be the model. But that is not the case. Under Chapter 9, the court can only approve a plan that has the support of the debtor and at least one class of creditors. Moreover, neither creditors nor the debtor would accept the concept of a third party vetoing a decision on debt restructuring that had been agreed to by the debtor government and its creditors.²

Some approach the issue from a different angle and call for action to void what they call "odious debt". Again, I quote from Jubilee which defines such debt as:

"..... loans to dictators who stole the money; debts corresponding to corrupt and wasteful "development" projects; loans that were made with the purpose of purchasing the tools of repressing democracy; debts contracted in combination with policy conditions which aggravated poverty, reduced living standards, and/or otherwise undermined the debtor country's capacity to achieve independent economic and financial development and thus the ability to repay the loans; and other illegitimate and odious debts."

Personally, I have no illusions about the existence of something like odious debt. But the real issue is how to deal with debt more generally when it becomes unpayable. And this goes beyond any notion of odious debt. The international community has shied away from mechanisms built on concepts such as odious debt and has concentrated on the broader issue. In the case of some governments, I suspect they eschew that kind of an approach for political reasons—governments may not want to recognize or defend some of the things they have done in the past! Others won't accept an approach that requires such Solomonic decisions! There is also a case to be made that dealing with debt in this way could introduce a new source of risk that could seriously affect the workings of the secondary market and, its corollary, the ability of sovereigns to mobilize new money.

Again, I would ask whether the NGO approach is operational. Who decides which debt falls into these categories? What are the values or criteria to be applied? If the odious debt deals were cut between one government and another, who decides—and by what criteria—on the balance to be struck between the wronged citizens of the debtor country and the taxpayers of the creditor country who will absorb the cost of the debt relief. Are the latter not, in some sense, also victims?

But other approaches to providing debt relief have been accepted increasingly over the last decade and I would argue that what really matters for the indebted country is whether those other approaches are delivering real debt relief. There are two aspects to this:

- (1) Have mechanisms been designed that are operationally successful and that don't require judgments such as how "odious" a particular debt may be. And,
- (2) Has relief actually been delivered and, if so, has it been timely and is it in appropriate amounts?

On the first aspect—the mechanisms themselves—this has been an evolutionary process—and, of course, there are legitimate questions about whether the pace at which these mechanisms have been developed and implemented has been appropriate to the problem. Many would say not. Certainly the record of the 1980's is pretty dismal. The rescheduling of official bilateral debt in low income countries through the Paris Club produced little long- term relief and, in fact, led to a snowballing of debt because of the accumulation of interest on rescheduled claims. Absent sufficient growth rates in the affected countries, debt profiles worsened and became increasing unsustainable. Similarly, in the case of commercial bank claims, the delay in accepting the need for a write down of such claims—a delay motivated, in part, by a fear of weakening the balance sheets of already fragile international banks with unknown implications for the international financial system—contributed to the poor performance of many emerging market countries, especially in Latin America, in the decade of the 1980s.

But things changed in the later 1980s. Among other things, the Brady plan recognized the legitimacy of international debt reduction and brought about a real reduction in the debt that some countries owed to commercial banks. The 1990s then saw a sea change in attitudes and approach. On commercial bank debt, London Club operations became more effective and the World Bank's Fifth Dimension provided resources to poorer countries to buy back their commercial debt at very large discounts—effectively eliminating medium- and long-term commercial bank debt for many of these countries.

On bilateral official debt, the Paris Club instituted progressively more generous restructuring terms under initiatives agreed at various G-7 Summits.³ Moreover, during the latter part of the decade a number of industrial countries, including the U.K. and France, began to write off completely all their ODA claims on some of the poorest countries. Finally, under the Heavily Indebted Poor Countries (HIPC) Initiative, the claims of the multilateral financial institutions, including the IMF, were brought into the debt reduction process for the first time, along with another notching up of the relief provided by bilateral official creditors. Was all of this done fast enough? No! And I applaud the NGOs for keeping up the pressure to speed the process.

But there have been positive and significant results.

As of end-March, 2003 debt relief has been committed to 26 poorer countries. Overall HIPC debt relief, together with bilateral debt relief under the traditional mechanisms and additional bilateral debt forgiveness over and beyond the HIPC Initiative, amounts to about two-thirds reduction in the overall stock of debt of these countries. That relief has cut the debt service of these countries relative to government revenue from over 27 percent in 1998 to 15 percent last year and will take it to below 11 percent in 2005. It has also helped these governments increase social expenditures from less than 6 percent of GDP in 1999 to over 9 percent in 2002—an amount four times that spent on debt service.

All of this said, I believe that more needs to be done. But care needs to be taken in the way it is done:

(1) Justice needs to be assured for all parties to the operation, creditors as well as debtors;

(2) Country policy performance should remain a key to these operations; we need to be clear on this: without sensible economic policies, debt relief will do little to help the people we all want to see helped;

(3) Care needs to be taken to balance the mix of debt relief and new aid flows: they each have a role to play; they are not perfect substitutes; and, in some instances, more of one, particularly debt relief, may come at the cost of less of the other, with little if any gain to the country. And,

(4) This should be done in a way that does not unduly inhibit the capacity of markets to provide appropriate financing to these countries in the future. We will not help these countries if relief is provided in a way that calls into question the basic validity of contracts.

But, there is still something missing in all of this. Markets have changed. Countries rely much less on commercial bank credit and much more on securitized debt issued in the international bond markets. It is this latter debt that has been at the heart of the debt problems in many emerging market countries: Ukraine, Pakistan, Russia, Ecuador and, most recently, Argentina and Uruguay. There are cases in which familiar mechanisms, such as debt exchanges, may be sufficient to provide the relief needed by a country. However, there are other cases where these mechanisms are not up to the task.

The international markets lack a reasonably predictable and orderly means to deal with the debt of primarily emerging market countries—a hopefully increasing class of countries—to deal with their debt to private creditors, including debt issued on the bond markets of the world. It is this void that led Anne Krueger, the First Deputy Managing Director of the IMF, to propose the Sovereign Debt Restructuring Mechanism (SDRM) 18 months ago.

The major motivation for the proposed SDRM is to help reduce the unacceptably large costs associated with disorderly defaults by sovereign governments whose debt burden has become unsustainable. We have all watched in some horror the collapse that has taken place in Argentina and the enormous cost paid by so many people in that country—and, yes, also by the creditors of Argentina—from the massive financial and economic dislocation and disruption that has occurred. I do not believe that what has occurred was inevitable.

The dislocation and disorder that occurs in such cases is often the result of a reluctance on the part of the country's authorities, first, to confront the underlying policy problems or, subsequently, to approach the country's creditors for relief when its debt has become unsustainable. In too many cases, the authorities gamble for redemption through ever less credible policy measures rather than face the uncertainty of approaching the country's private sector creditors for the needed relief. Argentina in the summer and fall of 2001 is all too dramatic an example of this phenomenon.

And why the hesitancy to approach creditors? There are, of course, reputational reasons: no government or individual minister wants to admit the reality of the country's debt problem. In some cases, of course, these will be the same people who oversaw the accumulation of that debt! There is also the concern regarding future access to capital markets. But, importantly, it is also the fact that there is simply no mechanism to reasonably assure the country that, upon approaching its creditors, there will be an orderly, predictable, and transparent process to reach a

negotiated settlement with creditors to restructure the country's debt in line with the prospective capacity of the country to service that debt.

This reality inevitably puts the official community and the IMF, in particular, in a difficult position in deciding whether to continue to support the country's policies in the absence of a restructuring of its debt. In the face of unsustainable debt burdens, continued Fund lending would be no panacea. Perhaps it could buy a little time. But increasing the burden of debt that benefits from the Fund's preferred creditor status may only increase the magnitude of the debt adjustment that must eventually be borne by private sector creditors and bilateral official creditors in situations where there is no underlying improvement in the country's capacity to service its debt.

Quite obviously the preferred course of action is to prevent such crises from occurring in the first place and many of the initiatives in the Fund and elsewhere are aimed precisely at that objective. Stronger economic and financial policies have been combined with improving the environment for private sector decision making in ways that should facilitate the assessment and management of risk. This offers the best prospect of allowing countries to reap the potential gains from globalization, while minimizing the likelihood, and potential severity, of crises. Robust assessments of the strength and soundness of banking systems and a country's financial system more generally; encouragement of the adoption of internationally recognized standards and codes and of best practices in numerous areas of economic policy making and institution building; and better surveillance or monitoring of country policies by the authorities themselves, as well as by the IMF, are all part of these efforts.

Unfortunately, despite best efforts, crises will still occur and some of us believe better mechanisms are needed to reduce the costs of these crises. Bankruptcies occur domestically and there is virtually no one who argues against the adoption of legal mechanisms to deal with such events. Am I missing something in thinking that similar capacity is needed for sovereign governments in an increasingly complex international financial system?

So what is needed? In the first instance, a way needs to be found to deal with the well known collective action problem. The existing system fails in this respect, and this market failure provides the rationale for public intervention. Collective action problems complicate the process of reaching agreement on a restructuring. There is a danger that individual creditors will decline to participate in a voluntary restructuring in the hope of recovering payment on the original contractual terms, even though creditors—as a group—would be better served by agreeing to such a restructuring.

The problem of collective action is most acute prior to a default, where individual creditors may have some reasonable hope of continuing to receive payments under the terms of their original contracts. A debtor that had reached agreement with the bulk of its creditors on a restructuring would doubtless hesitate to default on a small amount of the original debt simply to secure unanimity in the restructuring. But if a significant proportion of creditors elect not to participate in a restructuring, each hoping to be part of a small minority, the restructuring will inevitably fail.

Following a default, the options facing creditors—particularly those who have no interest in litigation—are more limited, and so the problems of collective action may be less acute. But they are still present! It is notable that all of the proposals for improving current arrangements for

sovereign debt restructuring have at their heart a recognition of—and measures to address—collective action problems.

But we should not fall into the trap of believing that default is a good solution to collective action difficulties. Of course, there is no doubt that following default, agreement on a restructuring would eventually be reached. But default—and the associated uncertainties regarding creditor—debtor relations—often leads to widespread economic dislocation. Proposals for strengthening arrangements for debt restructuring are intended to increase the likelihood that early agreement—preferably before default occurs—can be reached on a restructuring that can restore viability. Neither debtors nor their creditors should bear unnecessarily large costs in these crisis situations.

Here an aside: If Argentina and its creditors reach a settlement in a reasonable time—after policies become better defined and more acceptable and a genuine dialogue begins, some will declare success. I would say we can already declare that outcome a failure—and a massive failure—because of the loss and suffering that has already occurred, at least arguably as a result of the absence of a robust mechanism to help the authorities and the country's creditors deal with the looming debt problem in a timely—and less disruptive—manner.

Many of us believe that these weaknesses of the current system can be resolved only through a mechanism that has the features of the proposed SDRM. In my own view, while collective action clauses (CACs) and some of the other proposals now also being pursued could help, they can only be complementary to an SDRM, i.e., both are needed.

Under the SDRM that has been proposed by the Fund, there would be five major features:

- (1) the sovereign debtor would, if needed, have protection from disruptive legal action by creditors while negotiations were underway; this could be provided, in appropriate circumstances, through a stay on litigation, preventing creditors from seeking court decisions for repayment while negotiations are under way; the possible automaticity and the triggers for such possible stays has been a widely discussed point in the debate on the SDRM;
- (2) the creditors would have some assurances that the debtor will negotiate in good faith and will pursue policies—most likely to be designed in conjunction with seeking financial support from the IMF, that help protect the value of creditor claims and help limit the dislocation in the economy; the Fund's policy on lending into arrears is key in this regard;
- (3) creditors could agree to give seniority and protection from restructuring to fresh private lending, to facilitate ongoing economic activity through the continued provision of, inter alia, trade credit (something akin to debtor in possession financing);
- (4) a supermajority of creditors could vote to accept new terms under a restructuring agreement; minority creditors would be prevented from blocking such agreements or enforcing the terms of the original debt contracts, i.e., they would be bound by the decision of the majority; ⁴ and,
- (5) a dispute resolution forum would be established to verify claims, assure the integrity of the voting process, and adjudicate disputes that might arise.

In developing the SDRM, we have been guided by a number of principles. In particular,

First, the mechanism should only be used to restructure debt that is judged unsustainable. It should neither increase the likelihood of restructuring nor encourage defaults.

Second, any interference with contractual relations should be limited to those measures that are needed to resolve the most important collective action problems.

Third, the framework should be designed in a manner that promotes greater transparency in the restructuring process, and that encourages early and active creditor participation during the restructuring process. It should not increase the role of the Fund in this regard.

Fourth, the integrity of the decision making process under the mechanism should be safeguarded by an efficient and impartial dispute resolution process.

Fifth and finally, the SDRM should not give rise to an expansion of the Fund's legal powers.

The specific proposal that has been put forward—which is now formulated in rather specific terms in a statement from the Managing Director to the IMFC which was discussed at the meetings of that body in Washington in mid-April—has evolved since Anne Krueger first surfaced this issue. That evolution has been guided by what is, I believe, the most ambitious consultative process ever engaged in by the Fund on an important policy proposal. These modifications include the way in which a stay on litigation may be activated while negotiations are underway with creditors; the way in which members of the Dispute Resolution Forum (DRF) would be selected so as to assure their independence from the Fund; the powers that may be exercised by the DRF and its rule making authority; the role of the Fund in activation of the mechanism; and there are others. These modifications reflect the very helpful discussions that have taken place in a wide diversity of fora with the official sector, bankruptcy practitioners, the international legal community, NGOs, and many others. As always, of course, some have welcomed the modifications made, others would have been happier to stick with certain elements of the original proposal. My own view is that virtually all of the changes have improved the proposal and have helped to secure greater support for the proposal—support which, within the Fund, now includes over seventy percent of the membership.

The debate on SDRM has also contributed in other ways. First and foremost, there is far greater understanding of all these issues, and the related legal and institutional complexities, than existed 18 months ago. Secondly, the discussion has given new impetus to the push in the official community to encourage the use of collective action clauses in sovereign debt issues. That push began with the Rey report of the G-10 in the mid 1990s, but had accomplished very little until new life was breathed into the effort in the context of this discussion. Similarly, there is now widespread agreement—at least in principle—on the desirability of agreeing on a voluntary code of good conduct that would, among other things, foster greater transparency, provide guidance to debtors and creditors regarding procedures for contact and negotiations, and would help provide greater predictability to the restructuring process under any legal framework. I would note in this connection that a Code could be made applicable to a broad set of circumstances, ranging from periods of relative tranquility to periods of acute stress, and could constitute an established set of best practices. In contrast, proposals for strengthening arrangements for debt restructuring have a more limited scope and purpose, i.e., to facilitate the resolution of financial crises.

By its very nature, a voluntary Code, while potentially helpful, could not resolve collective action problems. Moreover, a Code could only be effective to the extent to which it is able to attract broad support among debtors and their creditors. Accordingly, the most promising approach to developing a code that could form the basis of a broad consensus would be for it to be developed jointly by debtors, their creditors, and other interested parties (including the IMF).

In my own view, as I indicated, I believe these initiatives are best seen as complementary to SDRM. They are not sufficiently powerful by themselves to provide what is needed to deal with the more complex and potentially damaging crises that may occur. Nevertheless, a system with reasonably comprehensive and robust CACs and a well defined and widely supported code of conduct will be an improvement on the system that currently exists.

Now let me try to deal with some of the criticisms that have been lodged against the SDRM.

In her summary of a conference on SDRM that took place at the Fund in late January, Ann Pettifor faults the proposal because "... only private creditors would have to reduce their claims."⁶ This is not correct. It is true that the proposal assumes continuance of the preferred creditor status of the IMF and some other multilateral organizations, but bilateral official creditors would be expected to provide relief on their claims on the country. Private creditors absolutely insist on this, and it was always foreseen in the proposal that bilateral official creditors would share the burden.

A second point that Ms. Pettifor and others make is that "... SDRM would not return poor, indebted countries to viability/sustainability." I believe there is some confusion here. The SDRM is not aimed at the poorest countries. It may be relevant to a very few of them that have large amounts of debt outstanding to private creditors (such as Nigeria). But for the low income countries, generally, there is the HIPC initiative. I know some criticize how the HIPC is working, and the amount of relief that is being delivered, but those are separate and distinct issues.

There are also those in the NGO community who fault the proposal for not including a process through which countries can be discharged of their obligation to repay what they call "odious debt". As I indicated earlier, I am not here to say that there is no odious debt in the world! That is not the point. The point is that the SDRM has a quite specific purpose, i.e., to help deal with the problems of market-access countries whose debt has become unsustainable, and to establish a system for more orderly and coordinated negotiation between the country and its creditors for debt relief in such circumstances. As in economics, where there is an axiom that there should be one policy instrument for each economic objective, so here too it is worth keeping in mind the single objective of the SDRM. It is interesting to note that neither private creditors, who presumably would have to give less relief if so called odious debt were set aside, nor the emerging market countries themselves, have voiced support for this proposal to write off odious debt.

Questions and challenges have also been raised about the role of the IMF under the SDRM. There are several dimensions to this. It is proposed that the SDRM be created through an amendment to the Fund's Articles of Agreement, rather than through a new international treaty. The rationale is straightforward. Helping countries manage their debt problems and the economic and certain institutional aspects of their interface with international capital markets falls squarely under the IMF's mandate. SDRM fits within the boundaries of that mandate.

Creating a new international treaty would likely be a much more complicated and uncertain undertaking than amending the Fund's Articles of Agreement. The Articles have been amended before and it is therefore a process familiar to the membership. Moreover, an amendment can take effect when three fifths of the members having eighty five percent of the voting power have accepted the amendment. Upon such acceptance, the amendment becomes binding on all members and, therefore, universally applicable immediately. Amending the IMF's Articles rather than creating a new international treaty would also provide the framework with greater stability. Withdrawing from a free standing treaty may have little cost to the withdrawing country. Withdrawing from the Fund, however, deprives the country of the benefits of membership in the IMF as provided for under the Articles of Agreement.

As proposed, the amendment would create no new legal powers for the Fund itself. Among other things, it would permit majority voting by creditors to bind in minority or dissenting creditors to a debt relief plan the creditors themselves negotiate with the member. And it would establish a Dispute Resolution Forum with powers to assure the integrity of the process and help resolve disputes that may arise; but this forum would be independent of the Fund.

Apparently most controversial in the eyes of some NGOs and other critics of the proposal, is that the Fund would continue to have a role in assessing the sustainability of the country's external position, including its debt. Some see this as putting the Fund in the position of dictating the terms of any settlement between the country and its creditors. Some also see it as incompatible with the role of the Fund as itself a creditor, and indeed a preferred creditor. Let me take these issues separately.

The Fund has traditionally been treated as a preferred creditor by debtor countries and by other creditors, i.e., by the private banks and capital markets and by bilateral official creditors. It is widely accepted that, as the institution providing finance to a country in times of crisis and in times when other sources of credit have often disappeared, it is appropriate for the Fund to have preferred status. The argument is simply that crisis financing would likely not be forthcoming without that protection. This status, of course, means that, in the event debt relief is sought, the other creditors must provide a greater share of the needed relief than would be the case if the IMF too reduced its own claims. It seems odd that this preferred status of the Fund is accepted as appropriate by private and official creditors affected by it in the way I just described, while others, such as NGOs which are not so affected, are opposed.

The other aspect of the Fund's role criticized by some is its role in policy formulation and, thus, judgments regarding debt sustainability. As Ann Pettifor says in her report on the earlier mentioned conference on SDRM, "the Fund would play a preemptive role in shaping the outcome of any debt crisis resolution negotiations. They will do this by setting the country's level of debt sustainability. In addition, the Fund will continue its existing role of determining the debtor's economic policies. The IMF effectively disempowers the debtor, all other creditors and civil society." This supposed role of the Fund would certainly surprise anyone who has negotiated a Fund arrangement with a member country. Those negotiations are inevitably difficult, they involve extensive discussions, lots of give and take, and lots of concessions on all sides before an agreement is finally reached. The Fund does not ride in with the parameters defining sustainability chipped in stone.

Beyond that, there is no single set of macroeconomic policies dictated by a country's particular condition, even in a crisis situation. There are temporal trade-offs—how much adjustment to aim for and how fast—and there are trade-offs in terms of who makes the necessary adjustments and sacrifices.

This then brings in an important related point rightly emphasized by NGOs: the call for civil society to have a role in the discussions leading to a debt relief plan. I agree absolutely that that should be the case. The issue is not whether they should participate—especially in democratic societies—but through what fora and mechanisms that participation should be organized. And this goes to the issue of how policies and debt sustainability are really determined. In this context, the government budget is the key instrument of policy. That is where debt service capacity will in the first instance be determined. And, contrary to the views of some of the NGO community, the country's budget is not dictated by the IMF. In most countries, and increasingly so, it comes out of a parliamentary process that determines the overall framework of the budget, spending priorities, judgments about taxing capacity, and all the other aspects of the final budget presentation. The Fund is part of that process through its discussions with the government. Civil society should certainly be part of that process as well, through representations to the government, participation in parliamentary debate, the giving of testimony, lobbying and through all other means traditional to the specific culture of each country. That is where affective participation is required; that is where transparency is needed; and that is the process through which the tradeoffs that ultimately help determine sustainability will be made.

Let me say a few words on the prospects for the SDRM. Whatever those prospects, I believe the proposals made regarding SDRM have stimulated an extremely important and productive debate that has vastly increased everyone's understanding of these issues. The atmosphere created by the prospect of an SDRM has also, in my view, been the single most important factor in the progress that has been made to formulate and to encourage the use of collective action clauses and, more recently, the impetus given to work on a code of good conduct for those operating in the international capital markets. The past few weeks have seen a number of news articles speculating on the future of the SDRM. Some have hinted, prematurely in my view, at its death. I would not rush to judgment at this time! Bankruptcy legislation took many years to enact in the United States. These are not easy concepts and people need to be persuaded. As I indicated, in the Executive Board of the IMF, over seventy percent of the membership support the SDRM. Even those now opposed support much of the substance of the proposal. I believe more work and more thinking is called for and that is what has been requested by the IMFC.

Finally, back to the issue of Justice.

If the world is going to deal justly with debt, it needs an approach that not only deals with the debt problem after the chaos has occurred as, most dramatically, in the recent case of Argentina, but also can help prevent that chaos and the enormous cost it involves for the citizens of the subject country and for its creditors. I believe the SDRM holds that promise.

¹ Jubilee USA statement on arbitration, April 2, 2003, p.2.

² This could be a possible outcome under their approach since the debtor government might be willing to tighten policies in the near term to accelerate re-access to capital markets.

³ These initiatives (and the debt reduction they allowed) were announced at Houston, Toronto (up to one-third), London (up to 50 percent), Naples (up to 67 percent), Lyon (up to 80 percent), and Cologne (up to 90 percent).

⁴ The statutory basis of the SDRM approach would provide the legal framework under which a debtor and its creditors could act as if common collective action clauses were included in all relevant debt instruments.

⁵ Report of the IMF's conference on the Sovereign Debt Restructuring Mechanism. 22nd January, 2003, IMF Headquarters, Washington, D.C. By Ann Pettifor and Kunibert Raffer, 23rd January, 2003. Jubilee Research at the New Economics Foundation.