

Sovereign debt restructuring:

What's wrong and how can it be solved?

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The main problems

Countries that suffer debt crises are not addressing restructuring needs timely

Relief is often insufficient to restore debt sustainability, a pre-condition for effectively pursuing countries' development goals

Holdout bondholders undermine restructuring processes

Evidence I: Insufficient debt relief

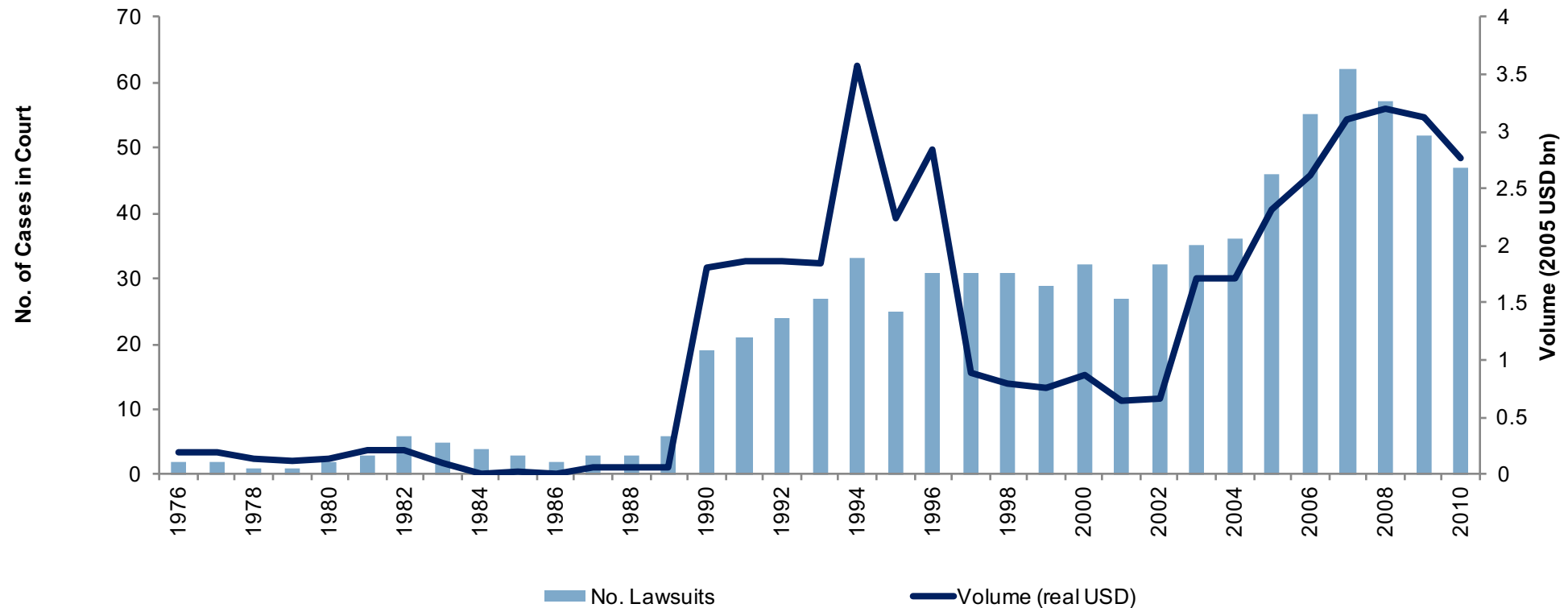
54.4 percent of the 187 restructuring episodes with private creditors since 1970 were followed by another restructuring (also with private creditors) or default within five years

(Source: Guzman, 2016, UNCTAD WP; Guzman-Lombardi 2016; based on Cruces-Trebesch 2014's database)

- This means that countries are not managing to “restore sustainability with high probability” in restructuring processes

Evidence II: Rise in litigation over sovereign debt contracts

(Schumacher-Trebesch-Enderlein 2014)



Evidence III: Vulture funds' victory over Argentina brought exorbitant returns to holdouts

Inter-creditor inequity that will have negative implications for sovereign lending/borrowing markets

- NML Capital's returns over declared purchases of Argentine (most of them defaulted) bonds: approx **1,270 percent**
- Creditors that accepted the country's restructuring proposal got a **discount of 2/3** over their original claims

Evidence on US Justice's approach towards sovereign debt restructuring

August 23, 2013: US Court of Appeals for the Second Circuit affirms Judge Griesa's injunction order blocking Argentina's payment to restructured bondholders, and in its justification defines Argentina as a

“uniquely recalcitrant debtor”

February 19, 2016: Judge Griesa announces that he would drop the injunction if Argentina repealed two domestic laws that impeded paying the holdouts. In his words:

“The injunctions, once appropriate to address the Republic's recalcitrance, can no longer be justified. Significantly changed circumstances have rendered the injunctions inequitable and detrimental to the public interest.”

“President Macri's election changed everything”

Conclusions

Judges from major lending jurisdictions do not understand the complexities and goals of sovereign debt restructuring

- Remedies are doing more harm than good

No matter how much contracts are improved, a system that is not based on sound principles will be fallible

A system for sovereign debt restructuring that works must be principles-based (Guzman-Stiglitz 2016 IPA)

The nine UN Principles for sovereign debt restructuring adopted by Resolution 69/319 are the right basis for creating a system that works