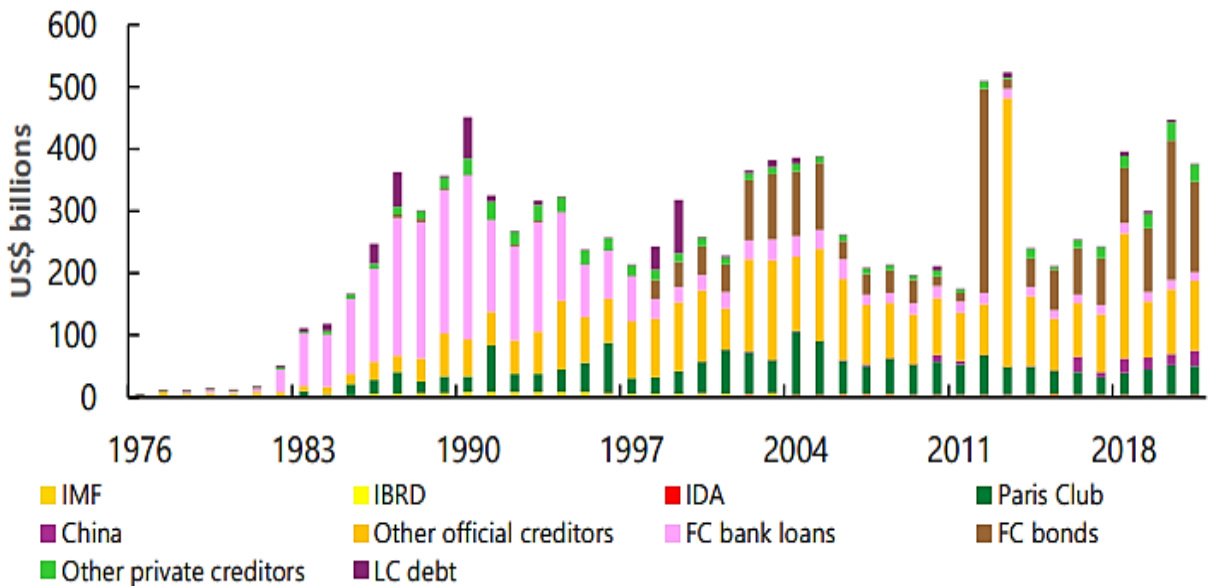


FROM COUNTRY RISK, TO FINANCIAL CRISIS AND DEBT NEGOTIATIONS

CIFE SEMINAR ROMA-BERLIN-NICE 2023
MICHEL-HENRY BOUCHET

1

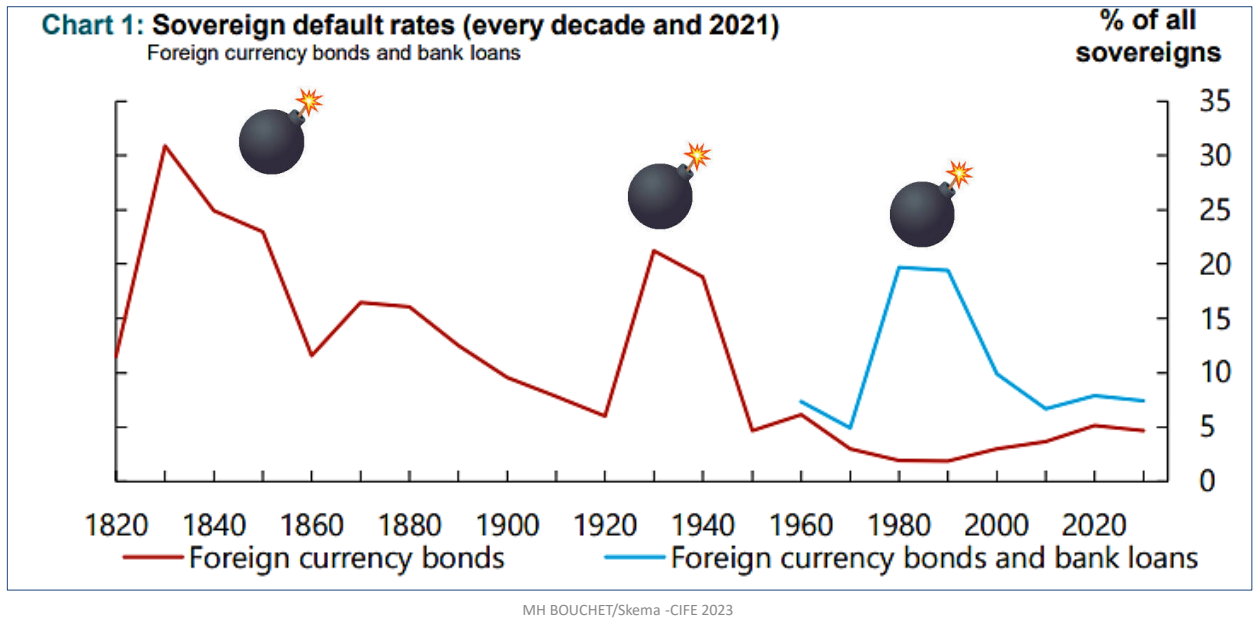
TOTAL SOVEREIGN DEBT IN DEFAULT BY CREDITOR 1976-2021



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SOVEREIGN DEFAULT RATES IN % OF ALL SOVEREIGNS



3

LIQUIDITY AND SOLVENCY THRESHOLDS

Flow variable

- ▶ **Liquidity** = Debt Service ratio < 33% of X
Interest/X ratio < 25%

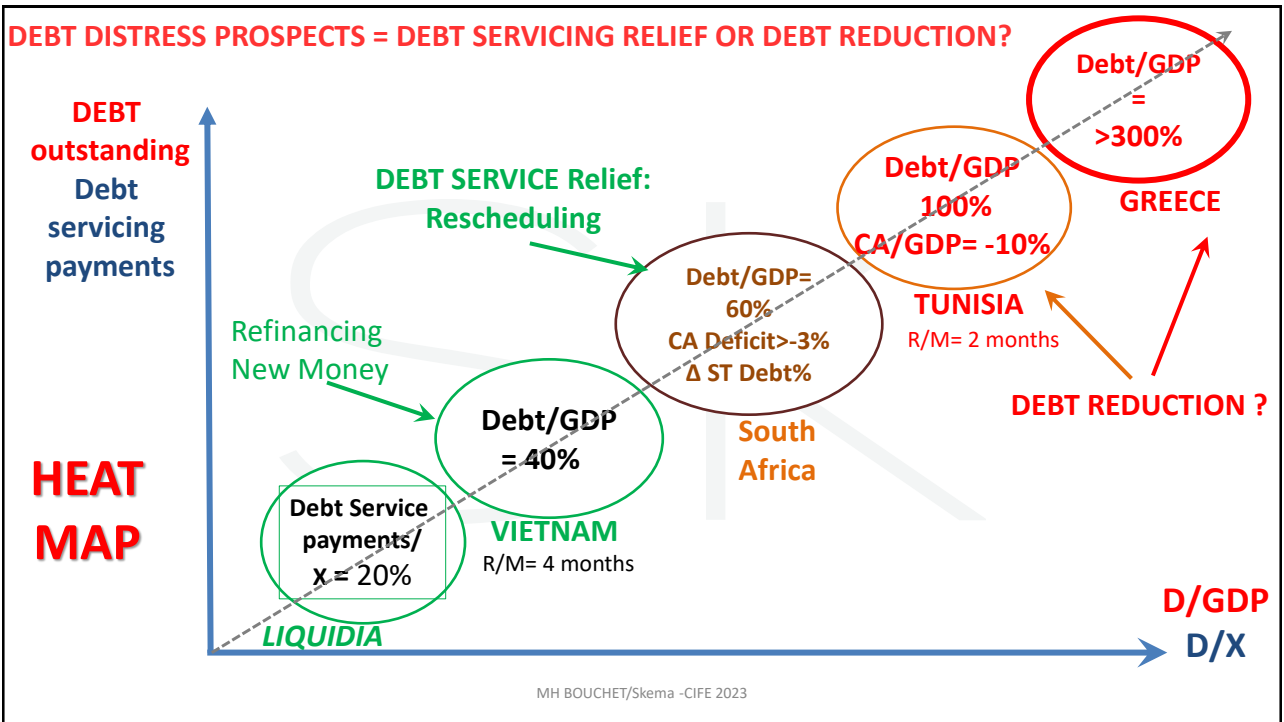
Stock variable

- ▶ **Solvency** = Debt/GDP < 66%*
Debt/Exports < 150%
Reserves/months of Imports > 6 months

* average debt crisis threshold 1970-2010 Reinhart/Rogoff (Maastricht)

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4



5

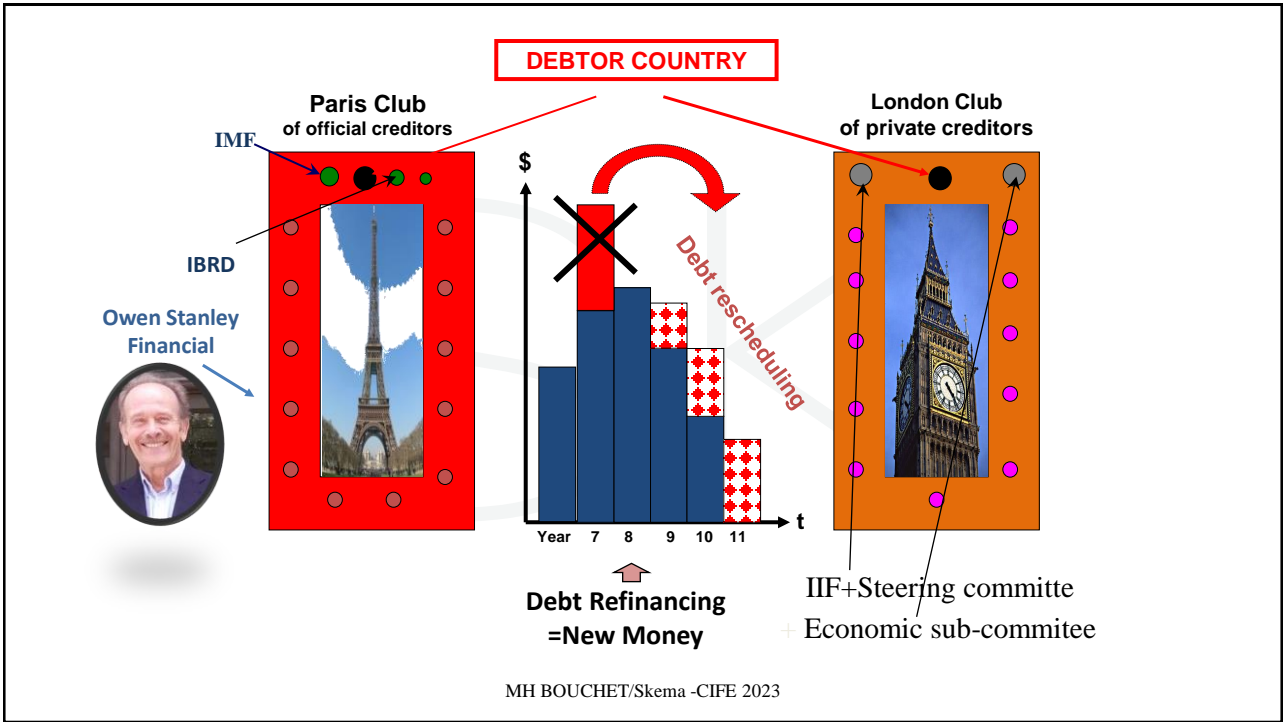
WHO'S WHO?

Five main groups of private and official creditors:

1. The IFIs: IMF and World Bank + RDBs
2. The **Paris Club** of OECD governments
3. Private suppliers: trade debt
4. The **London Club** of international banks
5. Institutional investors (pension and investment funds, hedge funds): Eurobond holders

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THE PARIS CLUB 1956-2023

Total number of agreements		478
Total number of debtor countries		102
Total amount of debt		614 Billion \$
Total number of countries in "Classic Terms"		61
Total number of countries in "Houston Terms"		21
Total number of countries in "Naples Terms"		33
Total number of countries in "Cologne Terms"		37

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TOTAL DEBT OUTSTANDING OF ARGENTINA

Paris Club's claims as of 31 December 2019, excluding late interest (In USD million)

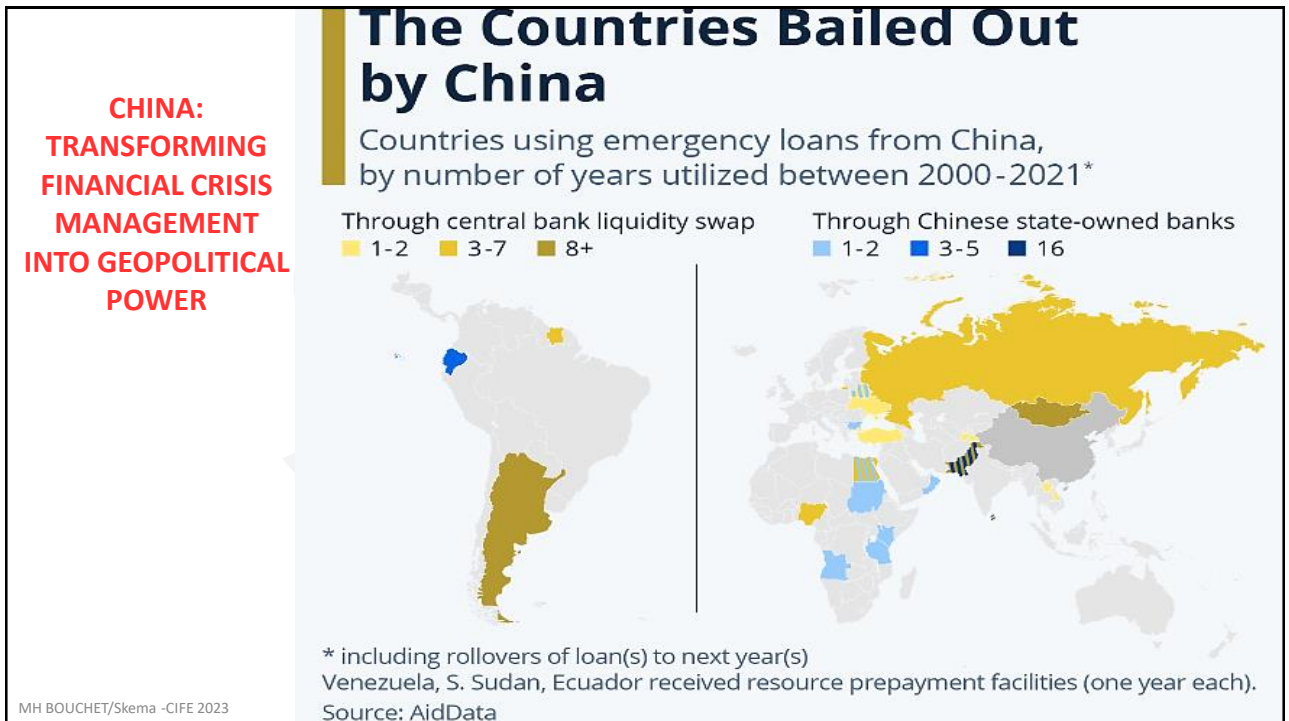
ODA: Official Development Assistance
NODA: Non-Official

DEBTOR COUNTRIES	ODA claims	NODA claims	TOTAL
Afghanistan	24	1 378	1 401
Albania	610	10	620
Algeria	285	1	286
Angola	475	1 187	1 662
Antigua and Barbuda	4	123	127
Argentina	336	1 863	2 198

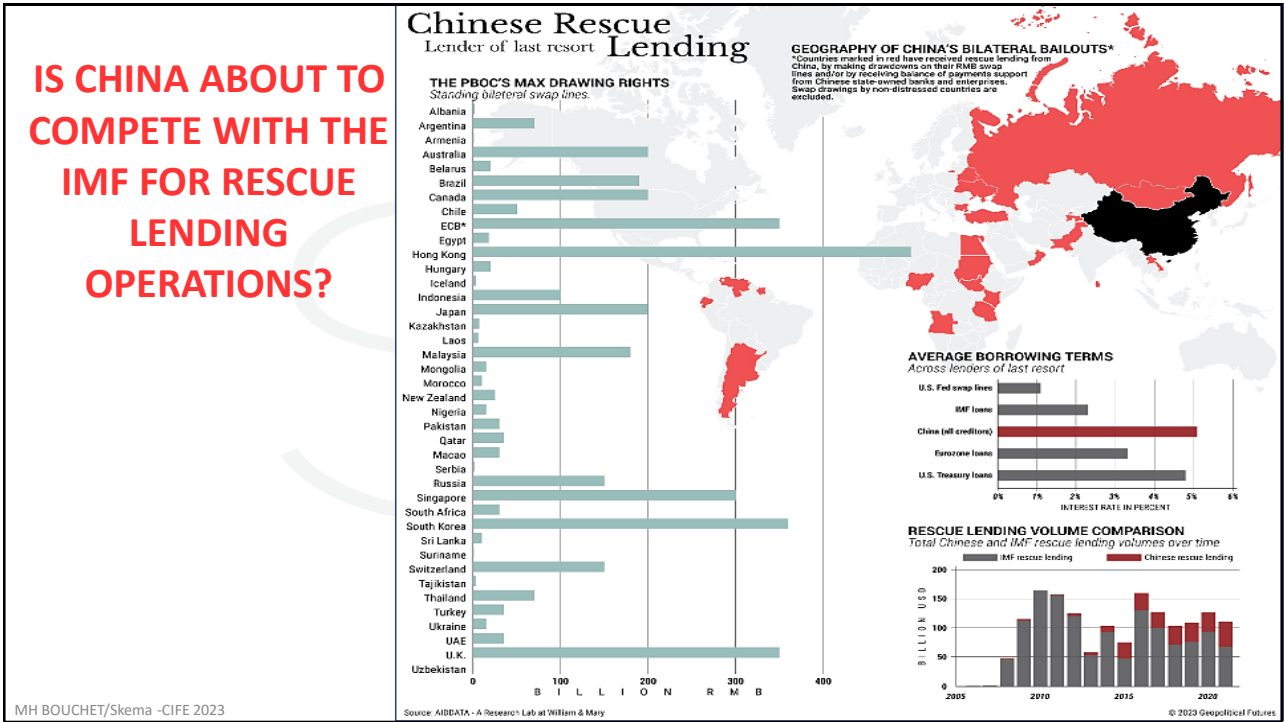
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	2019Q3	2019Q4	2020Q1	2020Q2	2020Q3
Data are in millions					
A1. Loans and other credits (Debt of)					
01_Cross-border loans, by BIS reporting banks	19,951	18,919	18,917	17,142	15,878
02_o/w to nonbanks	16,816	16,381	16,841	15,595	14,401
03_Official bilateral loans, total	..	..	..	..	..
04_o/w aid loans	..	..	..	..	..
05_o/w other	..	..	..	..	..
06_Multilateral loans, total	63,939	64,437	63,737	64,664	65,678
07_o/w IMF	43,508	44,131	43,556	43,904	44,921
08_o/w other institutions	20,431	20,306	20,181	20,760	20,757
09_Insured export credit, Berne Union	17,649	16,697	16,697	15,862	15,862
10_o/w short term	5,132	4,284	4,284	3,590	3,590
11_SDR allocations	2,764	2,793	2,757	2,779	2,843
A2. Loans and other credits (Debt due within a year)					
12_Liabilities to BIS banks (cons.), short term	14,748	14,159	11,892	8,619	8,304
13_Multilateral loans, IMF, short term	1,520	1,490	1,197	1,186	3,121
B1. Debt securities (All maturities)					
14_Debt securities held by nonresidents	..	48,350	..	..	..
B2. Debt securities (short term, original maturity)					
15_Debt securities held by nonresidents	..	860	..	..	..
C. Supplementary information on debt (liabilities)					
16_International debt securities, all maturities	112,182	112,846	111,806	112,290	108,627
17_o/w issued by nonbanks	110,096	110,777	110,007	110,513	106,934
18_International debt securities, short term	5,230	6,002	7,722	14,811	10,374
19_o/w issued by nonbanks	4,885	5,316	7,293	14,389	10,024
20_Paris Club claims (ODA)	..	336	..	..	..
21_Paris Club claims (non ODA)	..	1,863	..	..	..
22_Liabilities to BIS banks, locational, total	22,276	21,390	21,344	19,853	18,578
23_Liabilities to BIS banks, consolidated, total	23,988	23,184	20,370	16,798	15,884
D. Memorandum items: selected foreign assets					
24_International reserves (excluding gold)	45,764	42,193	40,534	39,707	37,629

9



10



11

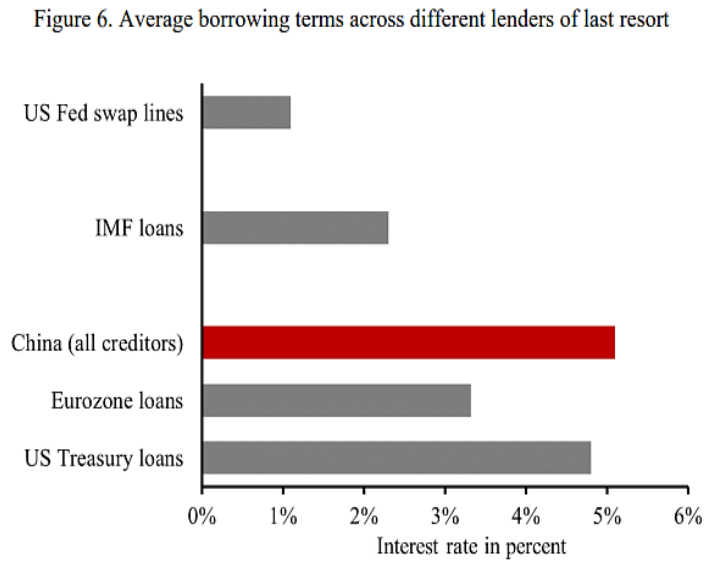
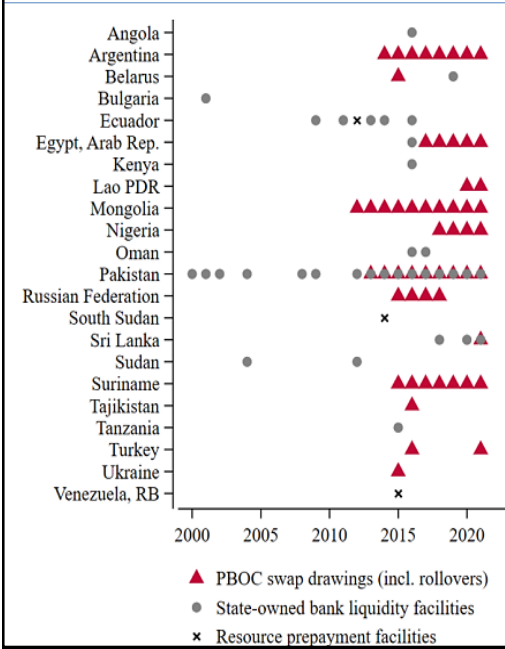
CHINA: GROWING GLOBAL FINANCIAL ROLE IN CRISIS MANAGEMENT & WIDE RANGE OF INTERNATIONAL RESCUE LENDING INSTRUMENTS

	Lending instrument	Example Cases
<p>>20 debtor countries have received \$240 billions in Chinese rescue lending since 2000</p>	<p>Rescue loans (general purpose / liquidity support) Chinese state-owned banks, in particular CDB, have provided USD credit lines that allow recipients to service external debts, increase reserves or finance general budgetary expenditures</p>	<p>Egypt 2016, Belarus 2019</p>
	<p>Commodity prepayment facilities Chinese oil importers have provided large upfront USD cash payments on long-term oil delivery contracts</p>	<p>Ecuador 2009</p>
	<p>Drawings from PBOC swap lines Recipient country central banks have drawn down their RMB swap lines to increase gross reserves</p>	<p>Argentina 2014 - 2020, Turkey 2021</p>
	<p>Central Bank deposit loans Chinese banks and the PBOC have provided USD deposits to foreign central banks to help increase their gross reserves</p>	<p>Pakistan 1997 - 2021</p>

Source: AIDDATA March 2023 Working Paper 124 MH BOUCHET/Skema -CIFE 2023

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CHINA'S FINANCIAL RESCUE PROGRAMS



MH BOUCHET/Skema -CIFE 2023 Source: AIDDATA WP 124 March 2023

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THE LARGER CHINA'S RESCUE LOANS THE LARGER THE RELIANCE ON RMB IN BILATERAL TRADE TRANSACTIONS

RMB share in Swift payments with China

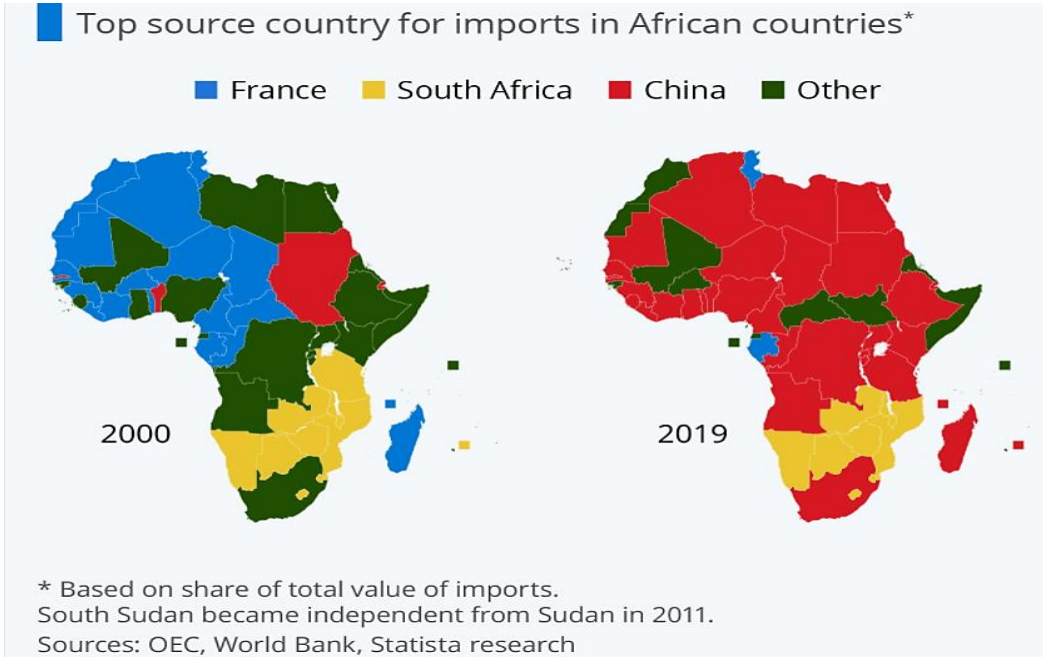


Source: IMF WP23/77 March 2023

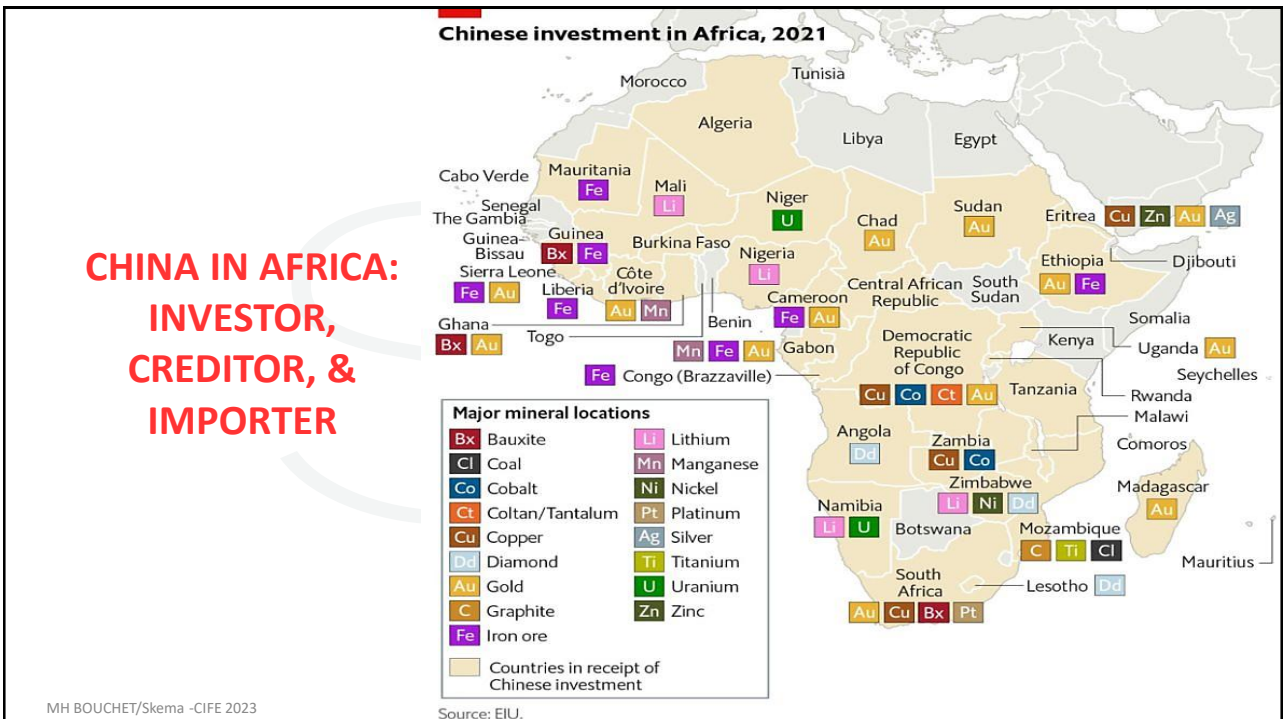
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CHINA HAS BECOME A KEY CREDITOR AND TRADE PLAYER IN AFRICA



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The London Club of debt restructuring



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WHAT IS THE « LONDON CLUB »?

- ▶ Since the 1970s, countries facing default have used the London Club process to restructure sovereign debt owed to banks.
- ▶ The London Club has evolved as an ad hoc forum for restructuring negotiations.
- ▶ Each London Club is formed at the initiative of the **debtor country** and is dissolved when a restructuring agreement is signed.
- ▶ Ad hoc London Club "Advisory Committees" are chaired by a leading financial bank.
- ▶ The IIF plays a key role in London Club meetings: BOP and debt analysis!



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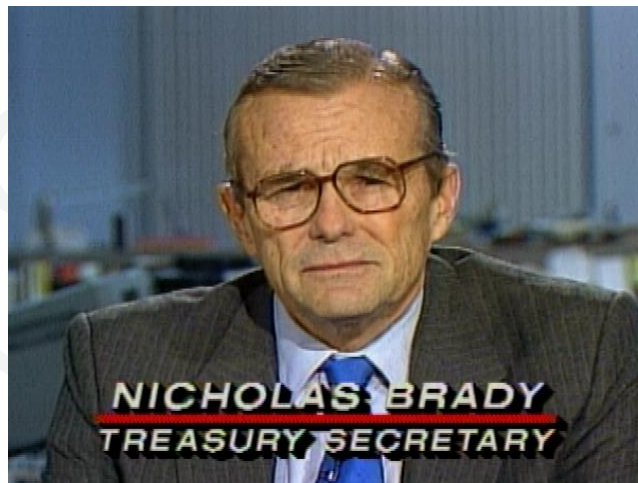
WHAT IS THE IIF?

- ▶ The Institute of International Finance, Inc. (IIF), is the world's only global association of financial institutions.
- ▶ Created in 1983 in response to the international debt crisis, the IIF has evolved to meet the changing needs of the financial community.
- ▶ Members include most of the world's largest commercial banks and investment banks, as well as insurance companies and investment management firms. Among the Institute's Associate members are MNCs, trading companies, ECAs, and multilateral agencies.
- ▶ The Institute has > **450 members** headquartered > 70 countries.

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THE BRADY PLAN OF DEBT RESTRUCTURING



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MENU-BASED DEBT RESTRUCTURING: THE BRADY PLAN AND BEYOND



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THE 1989-2021 PROCESS OF LONDON CLUB DEBT RESTRUCTURING

- ▶ **London Club banks** grant debt relief to debtor nations, in some proportion of secondary market discount through interest or debt stock reduction
- ▶ Accounting and regulatory incentives (loan-loss provisioning)
- ▶ Shift to specific purpose financing and voluntary lending
- ▶ **Debtor countries** adopt tough macroeconomic adjustment programs under the monitoring of the IMF/WB (SALs)
- ▶ Current account financing + Reserve build-up
- ▶ Objective: back to market-access for EMCs or to grants for low-income countries

Means and Tools

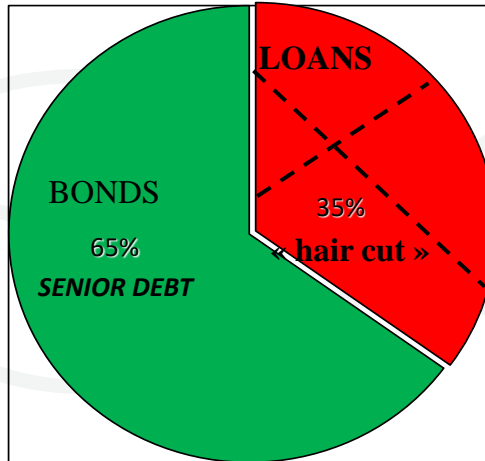
- ▶ Defaulted sovereign London Club debt to be exchanged for easily tradeable **Brady bonds** guaranteed by 30-year zero-coupon US Treasury bonds which the defaulting nation purchases with its reserves and official financing support (IFIs + Paris Club)
- ▶ Principal guarantee + x semi-annual interest payments, whose guarantee is rolled over
- ▶ **Bullet repayment** (e.g., 30 years)
- ▶ **Cross-default clause**
- ▶ **Debt conversion clauses**

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THE BRADY PLAN IN ACTION

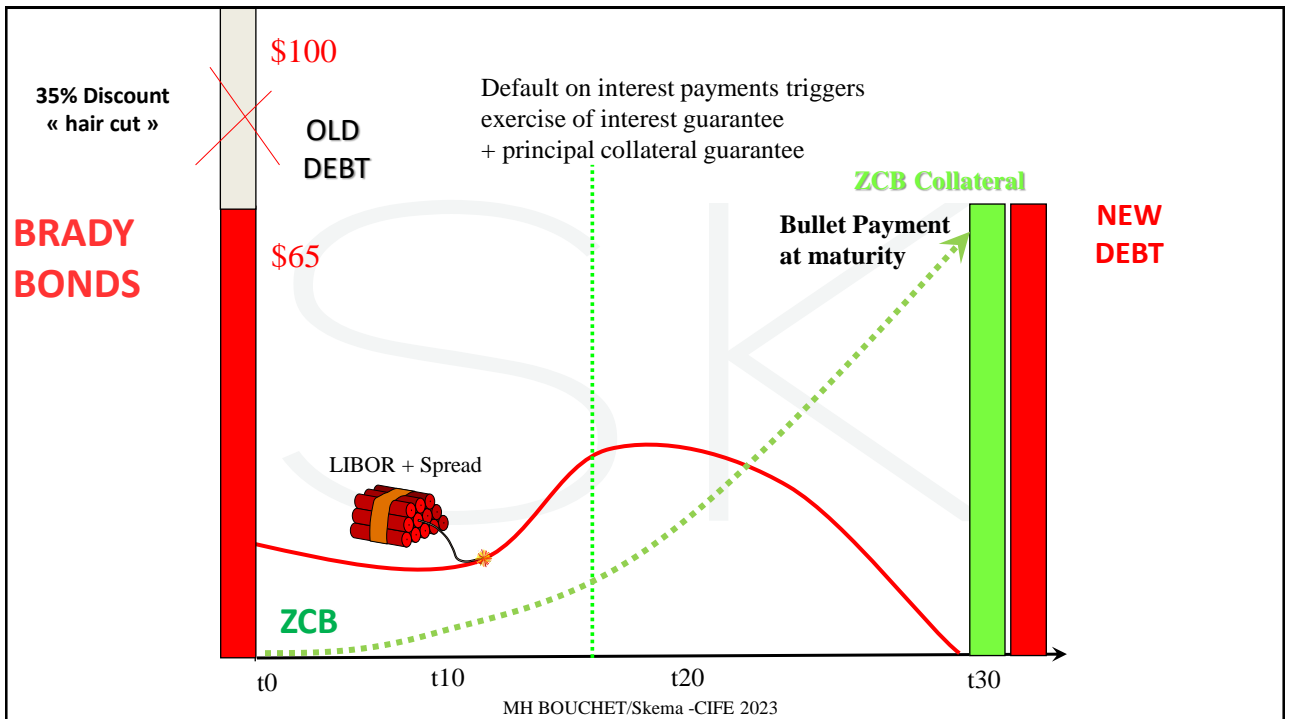
New senior debt with long-term maturity, principal collateralization, rolling interest
Guarantee + cross-default clause



Debt cancellation backed up by commercial banks' reserves for loan-losses with regulatory incentives

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Brady bond deals of the 1980s & 1990s (at the very least Brady-style with a menu of options)

- Baker plan launch 1985
- Brady Plan launch 1989
- Mexico: defaulted 1982, Brady deal 1989
- Costa Rica: defaulted 1981, Brady deal 1990
- Morocco: defaulted 1982, Brady deal 1990
- Venezuela: defaulted 1982, Brady deal 1990
- Philippines: defaulted 1983, Brady deal 1990
- Poland: defaulted 1981, Brady deal 1993
- Uruguay: defaulted 1983 (again in 2003), Brady deal 1991
- Nigeria: defaulted 1982, Brady deal 1992
- Jordan: defaulted 1988, Brady deal 1993
- Argentina: defaulted 1982 (again in 2001), Brady deal 1993
- Brazil: defaulted 1983, Brady deal 1994
- Bulgaria: defaulted 1990, Brady deal 1994
- Dominican Republic: defaulted 1982, Brady deal 1994
- Albania: defaulted 1990, Brady deal 1995
- Ecuador: defaulted 1982 (again in 1999), Brady deal 1995
- Panama: defaulted 1982, Brady deal 1996
- Peru: defaulted 1984, Brady deal 1997
- Ivory Coast: defaulted 1984 (again in 2001), Brady deal 1998
- Vietnam: defaulted 1982, Brady deal 1998
- Russia: defaulted 1998, Brady-like operation 1998

bondvigilantes.com



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VIETNAM = LONDON CLUB DEBT RESTRUCTURING

- Brady debt restructuring (12/97)=
- ▶ (P= 335 million) + (PDI= 515) *interest arrears*
= **\$850 million**
 - ▶ 30-year bonds with 50% discount +
par bonds + buyback at 44%

**Paris Club Debt Restructuring 12/1993:
LONDON Terms = 54% debt reduction**

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LEGAL CLAUSES AND CONVENANTS IN DEBT RESTRUCTURING NEGOTIATIONS

- ▶ Waiver on negative pledge clause: it prevents a borrower from pledging any assets if doing so would jeopardize the lender's security : risk of subordination with regard to a senior status lender!
- ▶ It ensures **financial equality** and democracy in a community of creditors
- ▶ In Brady deals, the Paris Club, the IMF and the World Bank **waived the clauses**

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THE GREEK 2011-15 MENU-BASED « BRADY DEBT RESTRUCTURING » = 65% « HAIR CUT »

1. **Par Bond** Exchange into a 30 year instrument (4% coupon)
 2. **Par Bond** with refinancing of rolling-over maturing Greek government bonds over 30 years
 3. **Discount Bond** Exchange into a 30 year instrument with 20% discount and 5% coupon
 4. **Discount Bond** Exchange into a 15 year instrument with 5,9% coupon
 5. **Buyback** at 35% price (65% discount) of London Club debt (11/2012)
- ▶ For instruments, 1, 2 and 3 the principal is fully collateralized by 30 year zero coupon AAA Bonds.
 - ▶ For instrument 4, the principal is partially collateralized through funds held in an escrow account.

Calculation: IIF & <http://www.voxeu.org/index.php?q=node/6818>

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CHALLENGES OF THE GREEK DEBT RESTRUCTURING WORKOUT 2011-20

- ▶ 1. *Pari passu*: Private investors insist that government bail-out lenders would be treated the same way as the private sector, to lessen the risk of another cut in their payouts down the line
- ▶ 2. New bonds issued to private investors as part of the hair cut to be governed by London rather than Greek law
- ▶ 3. Threat of free riders and legal actions: VEGA Hedge Fund

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IVORY COAST'S BANK DEBT RESTRUCTURING SAGA

- 03/1998 - Ivory Coast issued six bonds totalling \$2.4 billion under the Brady scheme in a restructuring of outstanding external commercial debt.
- 09/2000 - Default on the bonds, following a coup in 1999.
- 03/2009 - The IMF and the World Bank declared Ivory Coast eligible for debt relief under the HIPC (highly indebted poor countries) initiative.
- 03/2009 - Paris Club agreement leading to immediate cancellation of \$845 million in debt (**80% debt relief**)
- 04/2010 - **Debt exchange of the defaulted Brady bonds**, replacing the old bonds with a \$2.3 billion bond **due 2032**, with semi-annual coupon payments and 6-year grace period (2016): discount of 20 percent on the exchangeable debt.
- 11/2010 - Presidential run-off ballot : Gbagbo is declared winner = civil war
- 12/2010 - World Bank freezes funding
- 12/2010 - Ivory Coast does not make \$29 million coupon payment on \$2.3 billion bond. Failure to pay = "event of default"

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UKRAINE'S DEBT RESTRUCTURING 09/2015

- ▶ 20% write off on \$18 billion of bonds, condition for the IMF to press ahead with 4-year \$40 billion package
- ▶ Main creditors: PTG Pactual, T Rowe Price, TCW, Franklin Templeton...
- ▶ Inclusion of GDP-linked instrument
- ▶ Between 2021-40 investors will receive up to 40% of the value of economic growth > 4%



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EMCS SECONDARY MARKET DEBT PRICES

COUNTRY / ISSUE	Low Price	High Price
Africa Hyper-Exotics		
Angola / Trade	50.000%	55.000%
Angola / Loans	55.000%	59.000%
Cameroon / Trade (non-HIPC)	14.000%	20.000%
Congo / Trade (non-HIPC)	22.000%	26.000%
DR Congo / Loans, Trade (non-HIPC)	16.000%	20.000%
Ghana / Trade (non-HIPC)	78.000%	82.000%
Kenya / Trade	39.000%	49.000%
Mozambique / Trade (non-HIPC)	20.000%	26.000%
Senegal / Loans, Trade (non-HIPC)	12.000%	16.000%
Sudan / Loans (non-HIPC)	11.000%	14.000%
Tanzania / Loans, Trade (non-HIPC)	10.000%	13.000%
Uganda / Trade (non-HIPC)	14.000%	16.000%
Zambia / Loans, Trade (non-HIPC)	13.000%	20.000%
Zimbabwe / Trade	1.000%	4.000%

COUNTRY / ISSUE	Low Price	High Price
Latin America & Caribbean Hyper-Exotics		
Cuba / Trade	2.000%	4.000%
Cuba / Loans	5.000%	10.000%
Suriname / Loans, Trade	14.000%	18.000%

COUNTRY / ISSUE	Low Price	High Price
Eastern Europe Hyper-Exotics		
Azerbaijan / Trade	18.000%	23.000%
Bosnia / Trade	36.000%	41.000%
Georgia / Trade	11.000%	15.000%
Serbia / Trade	44.000%	54.000%
Turkmenistan / Trade	23.000%	33.000%
Ukraine / Trade	18.000%	25.000%
Uzbekistan / Trade	20.000%	24.000%

COUNTRY / ISSUE	Low Price	High Price
Middle East Hyper-Exotics		
Egypt Trade	65.000%	75.000%
Iraq / Paris Club	84.000%	89.000%
Iraq / Bonds	91.000%	92.000%
Libya / Trade	25.000%	35.000%
Syria / Trade	6.000%	11.000%

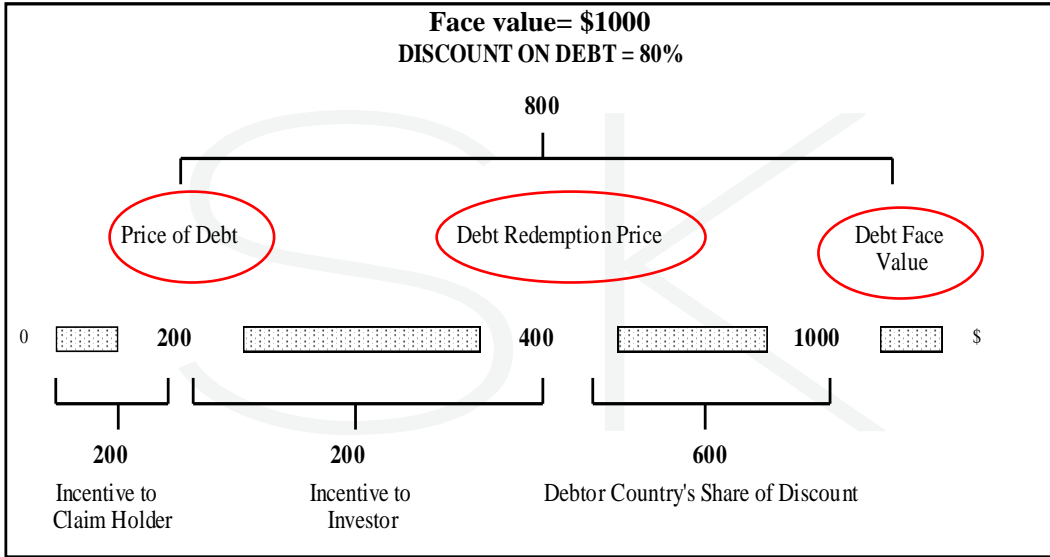
COUNTRY / ISSUE	Low Price	High Price
Asia Hyper-Exotics		
Mongolia / Trade	22.000%	30.000%
North Korea / Loans, Certificates	9.000%	12.000%



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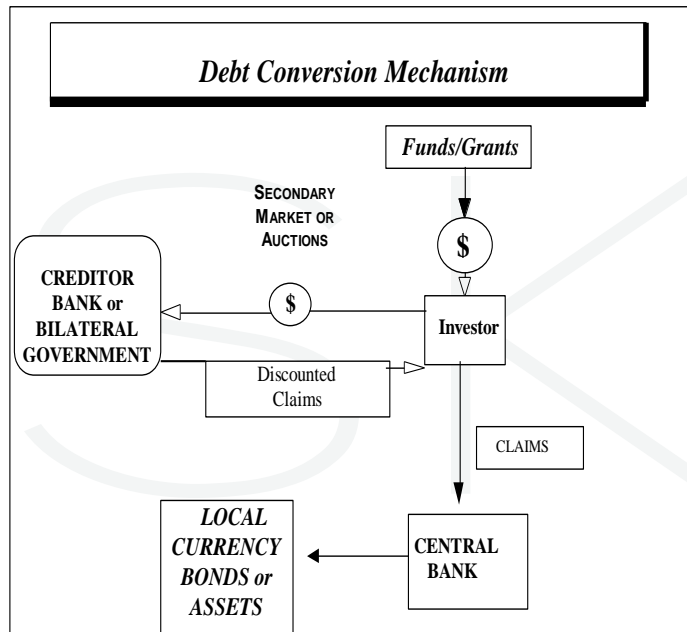
DEBT CONVERSION: A POSITIVE SUM GAME?



Source: Bouchet/OSF

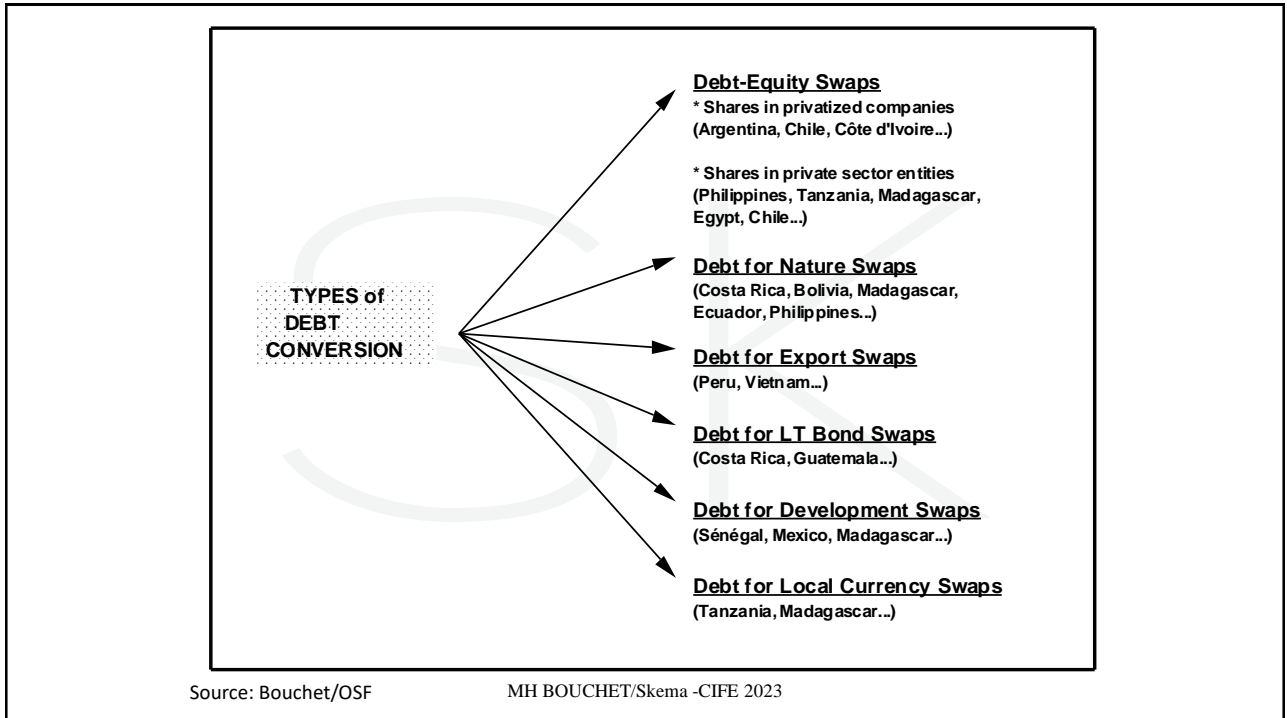
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SEPTEMBER 2021: BELIZE'S DEBT FOR NATURE CANCELLATION

Belize is inching towards a deal with international bondholders after admitting it cannot afford to pay back its debt, and counting on an unusual asset to help: its coral reefs. Earlier this month the Caribbean nation, with its tourism-heavy economy ravaged by the pandemic, agreed to buy back its only international bond from investors at a huge discount, using cash lent by the Nature Conservancy, a US-based environmental group.

As part of the deal, Belize will pre-fund a \$23.4m endowment to support marine conservation projects on its coastline, home to the world's second-largest barrier reef. Some more investors still need to agree to the scale of the buyback discount before the deal is done.

But if Belize can achieve the approval it needs on this \$530m bond, the country could secure the first **green-tinged debt restructuring**, capitalizing on the hunger among big fund managers to demonstrate their commitment to environmental, social and governance-driven investing.

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SEPTEMBER 2022: THE NATURE CONSERVANCY THIRD GLOBAL DEBT CONVERSION IN BARBADOS

Barbados, the country worked with Credit Suisse, who acted as Global Lead Arranger, and CIBC FirstCaribbean, as Domestic Lead Arranger, to raise approximately \$150 million through a dual currency term loan facility. This Blue Loan, which was partially funded via the issuance of Blue Bonds in the capital markets, **funded the buyback of a portion of Barbados' existing debt.**

With TNC and IDB each providing repayment guarantees on Barbados' behalf, the new financing features a lower interest rate than the old debt, and 100% of the resulting cost savings will be channeled into marine conservation.

The innovative financial deal will enable the Government of Barbados to redirect a portion of its sovereign debt service into marine conservation funding in support of the nation's commitment to conserve approximately 30% of its ocean and sustainably develop its blue economy.

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BELIZE'S DEBT FOR NATURE CANCELLATION SEPTEMBER 2021

Investors and advisers say the agreement could serve as a template for future restructuring talks, in which cash-strapped nations use the promise of environmental conservation to drive a harder bargain — in effect creating a mechanism for investors in rich countries to pay poorer nations to protect the natural world. The buyback operation, which is offering investors **55 cents for every dollar of debt** they hold, needs the support of a further quarter of bondholders in order to go through.

A group of investors led by GMO, Abrdn and Greylock Capital, representing half of the bondholders, has already given the scheme its blessing. Carlos de Sousa, a portfolio manager at Vontobel Asset Management — a member of this group holding about 10 per cent of the bond — said the proposal chimes with his company's focus on ESG.

For Belize, whose debt stands at **133 per cent of GDP** despite restructuring its borrowing five times over the past 15 years, the deal offers the chance to mend its reputation as a serial defaulter. Ocean conservation is crucial to the country's economy, with 40 per cent of output coming directly or indirectly from tourism, and one in every 10 workers employed in the fishing sector.

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NOVEMBER 2021
GALAPAGOS ARCHIPLAGO
ECUADOR'S DEBT FOR NATURE SWAP PROJECT

November 2021: President of Ecuador Guillermo Lasso decided to extend by >50% the protected territory of the archipelago of Galapagos during the COP26 à Glasgow. «This decision will lead to debt for nature swap transactions in view of reducing our debt while increasing environment protection expenditures. » Such transactions entail forgiving part of a developing nation's debt in exchange for local investment in conservation programs. The overall territory of the biodiversity reserve established in 1998 is of 130.000 km² and it will grow by 60.000 km².

The country's external debt reaches nearly \$46 billion, equivalent to 45% of GDP, of which 16% is owed to foreign governments and Paris Club creditors, including the UK, the US, and Spain.

(Actually, official data from the Paris Club dated end-2021 give total claims of ... only \$1,185 billion).

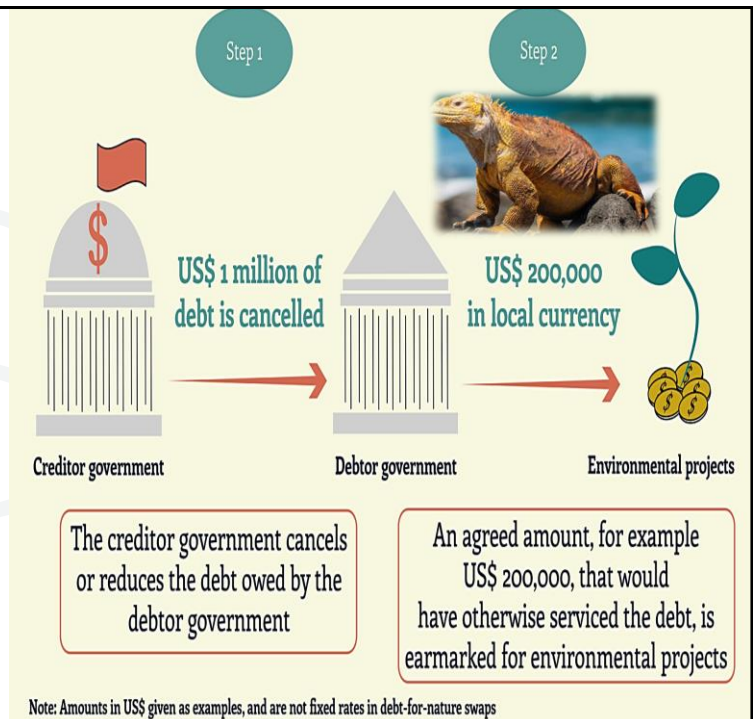
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NOVEMBER 2021
GALAPAGOS ARCHIPLAGO
ECUADOR'S DEBT FOR NATURE SWAP PROJECT

Debt-for-nature swaps are typically a voluntary transaction in which an amount of debt owed by a developing country government is cancelled or reduced by a creditor, in exchange for the debtor making financial commitments to conservation.

In financially distressed countries, the earnings generated through swaps are often administered by local conservation or environmental trust funds.

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POSITIVE SUM GAME!

- ▶ Debtor: debt cancellation with local currency payments while stimulating foreign direct investment and enhancing the role of private sector activity in the local economy (privatization)
- ▶ Creditor: cleaning up of portfolio with upfront cash payment while accounting losses get absorbed by loan-loss reserves
- ▶ Investor: access to local currency at a discounted exchange rate that boils down to an investment subsidy, thereby mitigating the overall country risk and the specific project risk

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