**Vultures in Paris: Bilateral creditors achieve deal with Argentina**

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Added 05/Jun/14

Argentina and its bilateral creditors, coordinated by the Paris Club, have [reached a deal](http://www.clubdeparis.org/sections/communication/communiques/argentine) to settle outstanding loans that were in default since 2001. According to the agreement made on 29 May, Argentina is going to pay $9.7 billion over the next five years.

This finally closes another chapter in the 2001/02 Argentine debt crisis. It is a step towards normalising Argentina’s financial relations and facilitating the return to global financial markets. However, the deal has its downsides as it is overly costly, violates the principle of treating creditors equally, implies repaying illegitimate dictator debts, and might pave the way for a new debt crisis. In fact, the deal provides new evidence that the international regime for sovereign debt restructuring needs a fundamental overhaul.

**The Paris Club – Winner at last …?**

When Argentina defaulted in 2001, the affected debt included official bilateral loans worth $4.7 billion – with Japan (30.6%), Germany (27.7%) and the Netherlands (8.7%) as the largest creditors. The lion’s share of Argentina’s $95 billion debt default came in the form of government bonds owned by private investors, however. While the Paris Club was ‘holding out’, private debt was subject to a major debt restructuring in 2005, which involved private creditors writing off roughly 75% of their claims’ value. Still, the vast majority participated in the debt restructuring. Some of those who did not sold their claims to vulture funds, which are [currently suing Argentina](http://www.eurodad.org/Entries/view/1545984/2013/09/02/Vulture-funds-US-court-ruling-on-Argentina-enrages-debt-justice-campaigners) for full payment.

The agreement reached on 29 May means that the Paris Club’s holdout strategy was successful. Argentina not only agreed to pay back the full amount of defaulted debt from 2002, it agreed to pay accrued interest and penalties so that the amount due to Paris Club creditors has now surged to $9.7 billion.

That Argentina gave in is even more remarkable, as much of the Paris Club debt is due to export credits and [dates back to dodgy deals](http://cadtm.org/La-deuda-con-el-Club-de-Paris) of Western firms and governments that propped up the military dictatorship of Jorge Videla. His regime ruled Argentina from 1976 to 1981, quadrupling the country’s debt and murdering an estimated 15,000 to 30,000 citizens. Debt justice groups had expected Argentina to declare these claims illegitimate and repudiate repaying the blood money.

It now turns out that speculating on Argentina’s misery was obviously a good investment, as the yield since the default in 2001 was about 7% annually. In particular, triple-A creditors such as Germany can refinance themselves cheaply, the yield on Germany’s ten-year bonds fell below 1.5% lately, which means that the money lent on to Argentina yielded a net profit of up to 5.5% for the German treasury.

Eurodad has repeatedly criticised Europe’s official creditors, who enrich themselves by extending [profit-making loans](http://www.eurodad.org/Entries/view/1546131/2014/01/15/A-matter-of-high-interest-Assessing-how-loans-are-reported-as-development-aid) to poorer countries, and to debt crisis countries in urgent need of money, such as [Greece](http://http://eurodad.org/files/pdf/532c03f068dba.pdf).

**… Or fooled once again?**

The Paris Club had to make one concession, however. The repayment plan stretches over five years, and it is backloaded, meaning that the installments increase towards the end of the plan. Just $1.15 billion is due to be paid during the first year. This means that the Paris Club also speculated that Argentina will remain solvent over the next five years, which is far from certain.

Argentina’s desire to reopen the possibility of borrowing on financial markets has been triggered precisely by the fact that the nation’s borrowing needs are high. A huge balance of payment deficit, due mostly to profit repatriation of foreign corporations, debt service on restructured bonds, energy imports and capital flight threatens to deplete the nation’s currency reserves. Argentina intends to fill gaps through new borrowing. The arrears with the Paris Club had to be removed first to enable this. But even if legal obstacles or procedures are removed, the cost of credit remains prohibitively high. According to [Bloomberg data](http://www.bloomberg.com/news/2014-02-03/argentina-bust-lures-bass-led-investors-in-200-years-of-defaults.html), Argentina currently pays a risk premium of 10.85 percentage points over US Treasuries on existing dollar-denominated debt.

This also implies that the sustainability of Argentina’s debt is questionable, and the fact that the recent deal added $9.7 billion to the bill certainly did not help to improve the situation. So the deal might just have opened a new cycle of surging debt levels, crisis, default and restructuring. This was [the ninth agreement](http://economia.elpais.com/economia/2014/05/29/actualidad/1401381735_857546.html) between Argentina and the Paris Club since the 1950s, as noted by Spain’s newspaper El País. The tenth agreement might not be too far away.

**International Monetary Fund – the biggest loser?**

Argentina’s red line in the negotiations was that the deal must exclude the International Monetary Fund (IMF). This succeeded, which was a political victory for the government of Cristina Fernández de Kirchner. In contrast to most other Paris Club agreements, this one does not come with the condition of implementing an IMF-designed structural adjustment programme. However, the economic price was high, as this also removed the option for Argentina to receive actual debt relief under the Paris Club’s [Evian terms](http://www.clubdeparis.org/sections/types-traitement/reechelonnement/approche-d-evian), for which IMF involvement is a condition.

Moreover, Argentinian experts such as Professor Alan Cibils, who was interviewed by Eurodad, argue that there is no point in formally excluding the IMF, when at the same time the government is starting to implement the same policies that the IMF would recommend. This includes raising central bank interest rates, cutting subsidies to reduce the fiscal deficits and upholding payment obligations to foreign creditors at any cost.

**Implications for global debt crisis management**

That the Paris Club applied a similar holdout strategy as vulture funds – and was successful – might have severe repercussions for the reform of the legal and policy framework for sovereign debt restructuring that is ongoing at the IMF and the UN. The holdout strategy of the vulture funds that are currently suing Argentina at New York courts for full payment is a key central reason why the current system urgently needs an overhaul, [according to the IMF](http://eurodad.org/1545535/). Now the private vultures have been joined by an official counterpart. Voluntary debt restructuring will no longer be possible when holdout creditors get their way: if they get paid in full, why would any creditor participate voluntarily and write off their claims?

What is happening now in Argentina is new evidence that holding out is a profitable investment strategy. The participating creditors were the useful idiots whose collaboration restored Argentina’s solvency and freed up the finance to start paying the Paris Club holdouts.

The lesson learnt is that, in order to make future sovereign debt restructurings more effective, a new debt workout mechanism should legally bind all creditors, including official creditors under a comprehensive treatment, and be able to enforce participation in a case of sovereign bankruptcy. For the majority of the world’s countries, developing such a new debt workout mechanism is a priority reform, as recent [interventions by the Group of 77](http://www.un.org/esa/ffd/hld/HLD2013/statement_G77.pdf) and China at the UN’s Post-2015 and Financing for Development processes have shown.

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