

PANEL DISCUSSION: REFINANCING OF THIRD WORLD DEBT

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PROF. GOLDIE: Welcome to the regional meeting of the American Society of International Law. Today's topic, Refinancing of Third World Debt, will be broken into two discussions, the first dealing with the private sector; the second with the public sector. We will begin our first session by comparing the credit worthiness of the Second World, the Communist world, to that of the developing countries that we call the Third World.

PROF. LILLICH: Current newspaper accounts show a certain degree of concern over the obligations of the Communist bloc, or the Second World.¹ There are substantial political considerations with respect to the debts of these Communist countries, particularly in the case of Poland.² This situation has produced all kinds of internal stresses. The necessity of stretching out, rescheduling or renegotiating the debts of these countries presents problems of a slightly dif-

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1. *N.Y. Times*, July 28, 1977, §1, at 2, col. 3; *id.*, June 17, 1977, §4, at 12, col. 1; *id.*, April 4, 1977, at 45, col. 1; *The Times (London)*, Jan. 27, 1977, at 23; *Wall St. J.*, April 14, 1977, at 35, col. 3; *id.*, March 16, 1977, at 24, col. 6; *id.*, Feb. 22, 1977, at 1, col. 6; *id.*, at 20, col. 2.

2. See *N.Y. Times*, April 4, 1977, at 45, col. 1.

ferent degree than the problems of the Third World countries.

It is usually accepted in the business world that the Communist countries are very solid borrowers. With the exception of North Korea, we have not had any difficulty in the collection of Communist countries' debts.³ But, I do recall that we still have claims arising from the Soviet nationalizations of 1917 through 1919, on which interest has accrued over the last fifty years in a sizeable amount. The Soviets made only a partial payment under the Litvinov Assignment.⁴ I wonder why this is not perceived to be as great a problem. Because the problem is not a result of the oil price increases of 1973 and 1974 it may not have received the attention that the Third World problems have.

MR. HAWLEY: There has not been a case of default in recent history. The Eastern European countries and the Soviet Union clearly recognize the necessity of being punctual and proper in meeting every letter of the loan agreements to continue to reap the benefits of access to Western capital markets. Not all of the Second World countries can borrow effectively in the West. Those that can have an asset they would not likely throw away.

The North Korean case is an anomaly in the sense that United States banks are not involved, but some European banks do have a problem.⁵ I think we are operating, not just on the assumption that the past is always a guideline to the future, but rather on the recognition that one cannot focus exclusively on past or present conditions. Second World countries have to recognize that they are going to have capital needs in the future and that the Soviet bloc cannot easily manage its affairs without access to Western capital markets. This strong determinant tends to keep their payments on schedule.

MR. BELLER: The major question that a banker would ask before extending credit to a sovereign is, can he repay it? The Eastern bloc countries to which we are extending credit are countries that we are confident will be able to repay us. These countries have centralized economies which can be manipulated to insure the availability of foreign exchange to repay the bank when payment comes due. Most of the lending, if not all of it, is done on a short term basis, which is safer for the bank. This is partly a result of the

3. The Times (London), Jan. 27, 1977, at 23c. See also *id.*, Jan. 11, 1977, at 15g.

4. Sack, *Diplomatic Claims Against the Soviets (1918-1938)*, 16 N.Y.U.L.Q. 253, 262-64 (1939).

5. The banks involved in the North Korean case are primarily Australian, British, French, Belgian, and West German institutions. N.Y. Times, April 4, 1977, at 45, col. 1.

Johnson Act,⁶ which prevented U.S. banks and other U.S. citizens from lending money to countries that defaulted on their debts to the United States or U.S. citizens, except to finance short term trade.⁷ So, Russia, for example, can only receive short term trade financing, which is inherently a little safer from the bank's point of view than extending them five or ten year loans.

My bank maintains a bank in Rumania and, so far as I know, it is the only Western bank in that area of the world. The relations have been excellent. It has been a mutually satisfying relationship. There are common motivations which prompt these countries to live up to every promise that they have made. We believe that they will continue to do that.

MR. ROBERTSON: The public position of the Eastern European countries, with respect to the issues that the Third World has raised in the United Nations, is that they are not in any way responsible for the economic disruption of the last few years. Since Eastern European countries have centrally planned economies and are not subject to the capitalist market forces that the rest of the world is subject to, they do not feel any particular responsibility to aid Third World countries. The Eastern European countries did agree to participate in the United Nations Conference on Trade and Development (UNCTAD),⁸ but they made it clear that they were participating as observers and were not to be actively involved in creating a system for debt renegotiation.

PROF. GOLDIE: Dr. Adede, would you like to make some general comments?

DR. ADEDE: The record of repayment of Western commercial bank loans has been almost perfect. We understand that when one of the countries gets into trouble, the Kremlin helps the particular country make its payment on time.

MR. TRIMBLE: The principal problem encountered in talking

6. Johnson Debt Default Act, ch. 112, 48 Stat. 574 (1934), as amended by ch. 399, § 9, 59 Stat. 516 (1945) (current version at 18 U.S.C. § 955 (1976)).

7. 42 OP. ATT'Y GEN. No. 27 (May 9, 1967); 42 OP. ATT'Y GEN. No. 15 (Oct. 9, 1963); 37 OP. ATT'Y GEN. 505 (1934).

8. UNCTAD was established as a permanent organ of the United Nations General Assembly on December 30, 1964, G.A. Res. 1995, 19 U.N. GAOR, Supp. (No. 15) 1, U.N. Doc. A/5815 (1965). The primary objective of the Conference is to develop a coordinated set of policies to be adopted by all member states, with a purpose of stimulating the economic development of developing countries. *Id.* For an evaluation of the work UNCTAD has engaged in with respect to the debt problem of the developing world, see Adede, *Loan Agreements Between Developing Countries and Foreign Commercial Banks—Reflections on Some Legal and Economic Issues*, 5 SYR. J. INT'L. L. & COM. 235, 236 (1977).

about Soviet or Eastern bloc lending policies, or debt problems, is the rigid wall of secrecy with which they surround their financial dealings. We have for years tried to get the Soviet Union to give us some indication of their foreign exchange position or their foreign reserve position. In all of these cases, we have enormous difficulty in getting any official confirmation of hard figures which governments or banks can use to make reasonable estimates of what the lending limits ought to be. The only other thing that might affect U.S. Government loans would be the political sensitivity that loans to Eastern bloc countries would have. There is still a great political sensitivity to lending to East European countries and forcing repayment.

Hungary has just repaid a long standing obligation growing out of World War I in order to avoid the Johnson Act.⁹ I expect that now they will be coming to Mr. Hawley's and Mr. Beller's doors to take advantage of this new-found liberation. We made them pay interest in accordance with the original one percent loan agreement plus three or four percent. The interest constituted a large part of the payment. The original principal obligation was almost insignificant.

PROF. GOLDIE: I would like to first ask Mr. Beller, and then Mr. Hawley, their views on Dr. Adede's distinction between borrowers and those who may be called partners.¹⁰

MR. BELLER: I would use the word partner in a context which has a more limited application. "Unity of interest" is really a more appropriate term. Partner implies a certain legal relationship. I do not think a debtor-creditor relationship is in any way a partnership from a legal point of view. From a practical point of view, there is certainly unity of interest.

After the loan proceeds are paid, the banker has performed his legal obligation. The only obligation left to be performed is the borrower's repayment of the loan. In that aspect the banker is a partner with the borrower. If any calamity befalls the borrower, or any other type of detrimental thing happens, the lender is unlikely to get repaid on schedule, or may be unlikely to be paid at all. In this situation, there is a unity of interest, because the lender now becomes interested in seeing that the borrower remains healthy and has a cash flow sufficient to repay his obligations. For this reason,

9. Johnson Debt Default Act, ch. 112, 48 Stat. 574 (1934), as amended by ch. 399, § 9, 59 Stat. 516 (1945) (current version at 18 U.S.C. § 955 (1976)).

10. Adede, *supra* note 8, at 239.

unity of interest is really a more appropriate term. Partner implies certain legal relationships.

MR. HAWLEY: Bankers do not start with a loan agreement drawn up with the intention of finding problems that allow declaring someone in default. That is not the nature of the business. We are not in business to declare people in default. In fact, the opposite is probably true. We end up delaying a declaration of default in many cases.

From the beginning, we try to take a different view, particularly when lending to governments. Countries do not disappear when they have serious financial problems in the way that corporations do. Countries do not easily go bankrupt. A country with resources, trained population, growing economy, improving standard of living, and so forth must be looked at in a longer term view than simply the monetary difficulties it may be having in the balance of payments.

We establish in national negotiations ways which will allow our relationship to achieve the purposes intended. When there are balance of payments difficulties, and foreign exchange constraints, our reaction is not to suggest immediately that we reschedule all of the debt. Rather, we look at the whole economic management and stabilization program of the country. We respond to questions on what it will take to regain ability to borrow from private lenders around the world.

If the country determines that it does need refinancing, because of reversals, because of changes in terms of trade, or other factors, we will sit down and work with that country to shape a program of which our refinancing would be a part. We regard our refinancing as part of a larger program. We refinance only when it is clear that a new program is underway and is actually being carried out with the political will necessary to put it through. Otherwise, we do not regard ourselves as obliged to pump that new money into the country.

We are often perceived as having a hostage relationship to the borrower. This is because we either have large funds which we have made available in past loans on which there may now be a problem developing, or because of some other aspect of our relationship with the borrower. It may be that we have a branch network which includes a significant branch in a given country. History shows that we have pulled out of countries when we faced blackmail threats against a branch. The operation of a branch is not considered that important in the patterns of international lending today. It is not

an essential or vital piece of our operation. When countries want to exert greater control over foreign investors, they put pressures on a foreign bank that is present and operating there. Under circumstances where we lose our freedom of action, and the kind of control that we feel that we ought to have over our own operation, we prefer to withdraw.

PROF. GOLDIE: That was a very full and comprehensive answer, and I am very glad you took the opportunity to go back to your hostage analogy and characterize a partner as a hostage. Before we move on to the next series of questions, I would like to give the floor to Professor Franck to discuss the recent refinancing regarding Peru.

PROF. FRANCK: I want to ask either Mr. Hawley or Mr. Beller to explain a subject treated very extensively in Dr. Adede's paper. How is your role different from that of the International Monetary Fund (IMF)?¹¹ Is it just a question of emulating the policy you would like to have the debtor country follow? The Monetary Fund is probably inclined to put its conditions on the table, while you seem to

11. The International Monetary Fund, established in July of 1944, was the final product of the United Nations Monetary and Financial Conference at Bretton Woods, New Hampshire. The Articles of Agreement of the IMF, the principal legal basis of the Fund, entered into force on December 27, 1945. These Articles constitute "organic" law of the Fund and are aimed at stabilizing international currency and investment relationships on a multilateral basis. The express purposes of the Fund, as outlined in Article I of the Articles of Agreement, are:

- (i) To promote international monetary cooperation through a permanent institution which provides the machinery for consultation and collaboration on international monetary problems.
- (ii) To facilitate the expansion and balanced growth of international trade, and to contribute thereby to the promotion and maintenance of high levels of employment and real income and to the development of the productive resources of all members as primary objectives of economic policy.
- (iii) To promote exchange stability, to maintain orderly exchange arrangements among members, and to avoid competitive exchange depreciation.
- (iv) To assist in the establishment of a multi-lateral system of payments in respect of current transactions between members and in the elimination of foreign exchange restrictions which hamper the growth of world trade.
- (v) To give confidence to members by making the Fund's resources available to them under adequate safeguards, thus providing them with opportunity to correct maladjustments in their balance of payments without resorting to measures destructive of national or international prosperity.
- (vi) In accordance with the above, to shorten the duration and lessen the degree of disequilibrium in the international balances of payments of members.

Articles of Agreement of the International Monetary Fund, *opened for signature* December 27, 1945, 60 Stat. 1401, T.I.A.S. No. 1501, 2 U.N.T.S. 39. For further discussion, see H. AUFRICHT, *THE FUND AGREEMENT: LIVING LAW AND EMERGING PRACTICE* (1969); H. AUFRICHT, *THE INTERNATIONAL MONETARY FUND: LEGAL BASES, STRUCTURE, FUNCTIONS* (1964); J. GOLD, *THE STAND-BY ARRANGEMENTS OF THE INTERNATIONAL MONETARY FUND* (1970).

drive at asking the government to come up with a new way of looking at things. And you seem to reserve judgment until you are satisfied that they have been able to formulate an acceptable approach.

MR. HAWLEY: When a government comes to us to explore the possibilities of further borrowing, for balance of payments purposes, that country is exhibiting a choice, or at least is exploring its options. Not every country is willing to go with the International Monetary Fund. Some countries will immediately go to the Fund as their first line of defense in a balance of payments jam and make use of the credit tranches that they have there. The early credit tranches, the first ones drawn on, can be drawn on with very little commitment towards following any specific changes in an economic program. When more money is borrowed from the Fund, the conditions become stiffer. These conditions are not codified in the charter of the IMF or written down in any regulatory manual that the Fund has issued. Each one of these stabilization programs that the Fund imposes as a condition for higher credit tranches borrowings is a negotiated agreement worked out between the Fund and the borrowing government. Recent authorization to borrow by the United Kingdom from the Fund was really a program proposed by the U.K. and worked out with the Fund in the negotiation process. The Fund is rather flexible, and some people will even say that it is too soft in the kinds of programs it imposes under difficult circumstances. The Fund is also criticized because its programs do not adequately take into consideration the development finance requirements of the country, but simply considers the balance of payments equilibrium goals of a particular action.

Some governments fear going to the Fund and using what many regard as last ditch reserves. There are countries that will go immediately to foreign countries but will only go to the Fund as a last resort. The case of Peru is interesting because of the way in which the government of Peru worked with a number of private banks.¹² The government of Peru was involved in serious difficulties with large needs for balance of payments financing. The government was very reluctant to go to the International Monetary Fund. They went to the banks. The banks did not find evidence of a new economic program or a commitment to better management. We saw no indication down the line that we could give our national bank examiners any logical reason for extending a loan at this point in time, under

12. See Adede, *supra* note 8, at 241 n.27; Bellivean, *What the Peru Experiment Means*, INSTITUTIONAL INVESTOR, Oct. 1976, at 145.

these circumstances, as a balance of payments financing loan.

We sat down and said you are going to have to come up with some kind of program. We cannot dictate a program to you, but before we can marshal enough private market support by going to a number of international banks, and pulling together the kind of money that you are talking about, the kind of magnitude you are talking about, there is going to have to be a public perception of a real reversal of performance in improving the economy. They came back with a program, we looked at the program and said that it had some merit but did not yet satisfy what we thought the market would require. We told them we would have a tough time going out on the market with this plan and raising money because everyone would look at it and see that there were no real teeth in it. They went back, redrafted the plan and toughened it up.

The question is who is dictating what. What we were doing at Peru's request was determining for them what the market would require from them if they needed funds. We nurtured their economy by requiring performance under the new program before we would release the funds under the loan agreement. The International Monetary Fund operates somewhat in the same way. On that specific point, the IMF also requires a track record. The IMF phases its payments on a schedule that it determines. Only when it sees a showing of continual performance, in line with the program that it has approved, will it continue to release further funds. I think this is something we probably learned from the IMF. We worked this out as a logical way of making funds available to Peru, which otherwise would probably not have been available at all. As a result of requiring performance under a specific plan in Peru, the developing countries realize that they cannot go to the banks to borrow without any condition on repaying, without any improved economic program. In fact, these countries may now figure it is easier to go to the International Monetary Fund.¹³

PROF. FRANCK: I must disagree with Mr. Hawley and his misrepresentation of the IMF's type of intervention compared with the commercial banks' type of suggestion. After all, the Monetary Fund is based upon an agreement signed by all our debtor nations. And in that agreement it merely maintains the right to suggest almost anything in the field of fiscal policy, monetary policy, exchange rate, import-export control, and so on. No commercial bank ever

13. For an analysis of the IMF conditions recently imposed upon Italy in return for a \$530 million loan, see *ECONOMIST*, April 2, 1977, at 84.

signs such an agreement with a debtor. This explains some of the feelings of the Peruvians.

Go back five years ago when they walked out of the negotiations. Why? They were told you must devalue. There is a difference of what might be called articulation as to what the Monetary Fund can propose, and that is an important difference. The Monetary Fund, in contrast to the private banker, has more actual leverage in its hands. All minor nations have paid in, like a credit union, certain amounts of money. They are tied to the Fund in a much more direct fashion than they would be to a commercial bank. This needs to be emphasized, because it puts a different light on the interference or intervention rights.

PROF. AUERBACH: I would just like to make one further point on how the IMF operates. The IMF is an international agency constructed by governments and it has a structure unique from other international institutions outside of the Bretton-Woods group. The voting rights, and one could argue the political influence of member governments, is not one state-one vote. It is a weighted voting scheme where each member's vote is weighted according to its subscription and participation in the Fund. A number of studies have shown that the way the Fund, and to a large extent the World Bank, operates makes it less of an autonomous institution and more in concert or in parallel with the major governments that are members. Needless to say, the voting weights provide for the United States, Japan, German Federal Republic, France, and the United Kingdom as the major actors. So we quickly move into the area of political economy.

While it is true, I suppose, that the banker making a loan to an individual might assess credit worthiness, one must ask how you go about assessing the credit worthiness of a state. Clearly, political calculations must go into assessing credit worthiness. But then one has to ask what goes into the calculation of political credit worthiness and what is political credit in the context of international financial activity. We have seen a number of instances in which decisions were made favoring certain states as far as IMF and World Bank loans are concerned. The decision not to lend is just as political as any other kind of foreign policy decision that the United States Government, or any other government, might make.

MR. TRIMBLE: I think it is significant that the IMF does not have any competitors. I am sure that competition puts a restraining factor on the kind of conditions or interventions that a bank would propose to a government.

MR. HAWLEY: The charge that lending institutions are in a dominating position, able to intervene and somehow work changes in domestic affairs of other countries which are theoretically none of their business, would be indeed a very serious matter if there were no alternate sources of funds. But, when governments are faced with balance of payments problems, they talk to more than one bank. They approach the international agencies, including the International Monetary Fund, and then try to make rational choices as to what is in their national interest to do. No single bank can fill the balance of payments gap of one of the major developing countries. We try to describe to a country like Peru what it will take for it to get back into the private markets and be able to borrow. The fact that there are several potential sources is very relevant.

MR. BELLER: Dr. Adede, in his paper, mentioned the possibility of future collaboration between private commercial banks and the IMF.¹⁴ The suggestion deserves an important amount of attention on our part. Cooperation with the IMF would make a greater amount of funds available. The IMF can require the development of economic policies which a private commercial bank could not be able to possibly even suggest.

Cross default clauses would provide the private banks with a certain amount of protection. With a cross default clause, if there was a default to the private bank, it would be considered a default to the IMF. Private banks would be protected to some extent because any default would affect the defaulting nation's credit with the IMF. I think collaboration between private commercial banks and the IMF may be the trend of the future.

PROF. AUERBACH: We must remember that the IMF, the World Bank,¹⁵ and the private financial institutions are not unrelated.

14. Adede, *supra* note 8, at 246.

15. The International Bank for Reconstruction and Development, also known as the World Bank, was also the product of the Bretton Woods Conference of 1944, *supra* note 11. From time to time the Bank has organized Consultative Groups, such as the Consultative Consortium on Aid Flows, from developed, capital-providing countries and international organizations for the purpose of coordinating the flow of finance and technical assistance to developing countries. The express objectives of the Bank, set out in Article 1 of the Agreement, are:

- (i) To assist in the reconstruction and development of territories of members by facilitating the investment of capital for productive purposes, including the restoration of economies destroyed or disrupted by war, the reconversion of productive facilities to peacetime needs and the encouragement of the development of productive facilities and resources in less developed countries.
- (ii) To promote private foreign investment by means of guarantees or participations in loans and other investments made by private investors; and when private capital

Both the World Bank and the IMF are sort of articulators of who is a good risk and who is a bad risk. These are highly independent agencies and institutions acting and interacting. We are not dealing with the Adam Smith approach to financing. It is not as if we have an infinite number of suppliers in a market arrangement. These are highly independent agencies and institutions acting and interacting.

An analogy might be that of two large enterprises confronting each other in a negotiated order. One comment on a negotiated order. The IMF has the threat of nonagreement with any proposed program of fiscal monetary belt tightening, so that from a country's point of view, which is seeking assistance from the IMF, there is already a past record. It may not be stipulated in a book that if you have these problems then we have a specific course of action. Whether or not there are stipulated IMF or World Bank conditions in advance may not make all that much difference.

PROF. LILLICH: First, I would like to comment about what has been said so far. Then, I would like to shift our discussion to another area.

Political conditions have always been laid down by major banks. In the last century the influence of the Rothchilds is an example.¹⁶ Sophisticated bankers, like Mr. Hawley, realize that it can be political dynamite if there is any rupture with the borrowing country. Linking the efforts to influence economic policies by private banks to the IMF, rather than having them articulated only from the bank, is an exceptionally interesting development.

is not available on reasonable terms, to supplement private investment by providing, on suitable conditions, finance for productive purposes out of its own capital, funds raised by it and its other resources.

(iii) To promote long-range balanced growth of international trade and the maintenance of equilibrium in balances of payments by encouraging international investment for the development of the productive resources of members, thereby assisting in raising productivity, the standard of living and conditions of labor in their territories.

(iv) To arrange the loans made or guaranteed by it in relation to international loans through other channels so that the more useful and urgent projects, large and small alike, will be dealt with first.

(v) To conduct its operations with due regard to the effect of international investment on business conditions in the territories of members and, in the immediate post-war years, to assist in bringing about a smooth transition from a wartime to a peacetime economy.

Articles of Agreement of the International Bank for Reconstruction and Development, *opened for signature* December 27, 1945, 60 Stat. 1440, T.I.A.S. No. 1502, 2 U.N.T.S. 134.

16. For a comprehensive analysis of the impact of the House of Rothschild on European politics, see COUNT EGON CAESAR CORTI, *THE RISE OF THE HOUSE OF ROTHSCHILD* (1928).

I would like to move our discussion to another area of Dr. Adede's paper. I was intrigued with his analysis of the internationalization of loan agreements. Dr. Adede questions whether concession agreements, in effect, give rise to some instantaneous international right.¹⁷ If it can be shown that breach of a loan contract gives rise to a property right, a bank may be able to get the assistance of the foreign office of the country involved. Parenthetically, it is interesting that Mr. Trimble tells us that a contract is interpreted by the Department of State as a property right for rescheduling purposes. Therefore, we have to get congressional consent. Yet, the assistant legal advisor for international claims will tell us the contract right is not a property right when it comes to the government espousing a claim. In other words, the government, as in so many areas, wants to have it two ways. Dr. Adede's analysis, both his descriptive analysis and his own approach, is certainly sound. His only problem is that he stops about ten years ago and doesn't continue the debate, either in the literature or in the analysis, up to the present day. It seems to me that the attempt of the articles that he cites in his paper is to, in effect, make a concession agreement an international treaty. This argument has never gotten anywhere, either in the debates of the American Law Institute, or certainly from the point of view of convincing the officials in the Department of State. We are talking about a private loan, a loan by Citi-Bank, for example, to a developing country. When there is a breach, or a potential breach, the situation is not automatically elevated into an international matter.

I have a second comment on Dr. Adede's paper. I do not think that recent developments in the area of sovereign immunity have been influenced by the debt problems of the Third World. The whole trend for the restrictive theory of sovereign immunity developed in Belgium at the turn of the century when there were not any Socialist states. There were not any Third World states, there were just European states and colonies and territories. Aside from the Soviet bloc, the last stronghold of the absolute theory of sovereign immunity, Great Britain, appears to be breaking down. Dr. Adede asserts that because there is a trend towards relaxing the sovereign immunity doctrine, a trend towards allowing suits against foreign governments, we have more effective legal remedies.¹⁸ Frankly, I

17. Adede, *supra* note 8, at 249.

18. *Id.* at 259.

think Dr. Adede overrates the restrictive theory of sovereign immunity.

It was good to see the new bill discussed in Dr. Adede's paper adopted in the United States.¹⁹ It is nice to see Great Britain finally falling in line. I think we all have to realize that this is a very marginal thing which may help a given creditor in a given moment, but it is hardly the type of remedy that any creditor, much less a multinational bank, would be interested in having. In this area, we really do not have very effective remedies. If we take a look at the whole history of the international law surrounding not only loans in the past, but also foreign investment in the past, we find marginal measures of enforcement. Enforcement is not achieved through the use of legal machinery and traditional doctrines of customary international law. Loan payments are made because of a variety of economic and political factors. Some of the political, and indeed, military factors are no longer present. We have new factors that today play a role, but it seems that customary international law and traditional doctrine are only marginally relevant.

MR. HAWLEY: On the question of jurisdiction, my institution would not require New York law exclusively. We might accept United Kingdom law and certain others. Our choice is not restricted to the United States. The decision on jurisdiction and the national law to be used in resolving a debt difficulty, which is worked into the loan agreement initially during the negotiations, is not primarily based on the kind of considerations that Dr. Adede lists. He states that our decision stems from our skepticism that the developing country's judicial system can do justice. We do not make a judgment on the level of sophistication of the borrowing country's system. In all cases we want a jurisdiction somewhere not under the control of the borrower.

I turn now to the topic of political conditions, which as Professor Lillich mentioned, have always been imposed by the lender's nation. But in situations where no political conditions have been placed on the lender by the country it is in, the lending has never, in my own experience, involved a judgment that was affected by approval of a political system. Now this is something quite different from saying that there are not, or are, political considerations involved in the analysis of the credit worthiness of the country. We will consider whether or not a government that has just embarked

19. Foreign Sovereign Immunities Act, 28 U.S.C. §§ 1602-1611 (1976). For Dr. Adede's discussion of the Foreign Sovereign Immunities Act, see Adede, *supra* note 8, at 255-57.

on a new economic stability program is likely to be overthrown next week because it is so weak and the social instability of the country is so great. We will question the political stability of a certain government to decide whether we can rely on commitments made. This is the kind of political analysis that is very definitely reflected in our judgments. But under no circumstances do we impose political conditions.

DR. ADEDE: I mention internationalization of state contracts, which was tried on the basis of state concessions, because it should be examined whether or not it would be applicable in the case of loan agreements. I came to the conclusion that the doctrine cannot be applied in this context.

I am not saying that sovereign immunity is not relevant. I mention in the paper that some loan agreements do require that a particular borrower government waive its sovereign immunity. Eastern countries consider this request an affront, though I understand there are some cases where they have agreed on financial agreements where there is a limit on this aspect.

I am unwilling to discount completely the role of international law. Some of us are still forced to say this again because of what has happened to the law of taking of foreign properties abroad or expropriation.

In disagreement with Mr. Hawley, I believe lenders choose United States law because they are not familiar with the law of the borrowing state. I am not sure that many United States bankers would even accept English law. The bank officers would have to rely on the English lawyers to tell them what the law is, to enable them to enter into meaningful discussions with their stockholders in assessing whether or not they can make the loan.

A stigma exists in the back of the minds of many people that the local law of a borrowing developing country is rejected because of lack of confidence in the ability to use it to do justice. In the loan between Denmark and Malawi, Denmark decided that the law applicable would be the law of Denmark. The lenders did not want to expose themselves to the laws of Malawi. Great Britain is also very cautious. While their loan agreements do not specify that the law of England is applicable, they provide that any disputes are subject to the law where the bank is located.

PROF. GOLDIE: I would like to ask Mr. Hawley to talk about the political aspects of lending.

MR. HAWLEY: We are not yet affected by any congressional or regulatory action in this area. An attempt could be made, either

through the federal regulatory network or through legal legislative action, to try to have some impact on commercial bank lending by injecting political requirements. But right now I think it would be a mistake. Any human rights weapon in the hands of the Carter administration is of limited value if a country's major borrowing is from private banks and the country seems to have unlimited access to private bank lending. Private banks appear to be providing a loophole. This is a very real issue in Congress now. The objectives of the U.S. Government in international economic policy are not restricted to achieving one goal. Congress is attempting, as always, to balance the achievement of goals specified in several bills. This is merely one of many areas where the attempt to accomplish one goal begins to interfere in the accomplishment of others. For example, in terms of the discussion of sovereign immunity, we have a policy that whatever the laws state in terms of giving comfort through the legal interpretations on what types of cases are, or are not subject, we do not depend on those changes in legislation for our loan agreements. We stand by an absolute requirement that the borrowing government waive its sovereign immunity. Without the waiver, we have no assurance that the loan is sound and from my institution at least, there will be no loan made without a waiver of sovereign immunity.

PROF. LILICH: The new statute is important, though, because before a waiver meant nothing. Now the waiver means something that is very important in the United States.²⁰

MR. TRIMBLE: In the area of nationalization and foreign investment abroad, where traditionally the value and support of international law has been cited as important to the conduct of business abroad, I would be very surprised if any lender really took into account, as even a marginal factor, the potential value of State Department or foreign ministry intervention on its behalf to help collect the loan. I would similarly be very surprised if you didn't also have an absolute rule requiring the loan agreement to be governed by New York law and payable in New York. This idea of the internationalization of a loan agreement is unrealistic.

PROF. FRANCK: Before the human rights legislation was introduced or informally used, the United States Government, in its

20. Section 1605(a)(1) of the Foreign Sovereign Immunities Act provides that a foreign state shall not be immune from the jurisdiction of the courts of the United States if the foreign state has waived its immunity either explicitly or by implication. 28 U.S.C. § 1605(a)(1) (1976).

lending decisions, was not oblivious to the political orientation of the debtor country. Commercial banks of the United States have been indirectly drawn into the same wake. The United States Government now is taking the lead in voicing its opinion in the council of the United Nations agencies, such as the Monetary Fund and the World Bank. Whenever the Monetary Fund takes a lead and comes to some kind of agreement with the debtor government on what the next steps in managing their economy will be, the commercial banks have not asked for more. In fact, I think they have been satisfied with less. If that decision from the Monetary Fund was in any way influenced by political consideration, then I cannot see how the commercial banks can avoid being drawn into the same considerations. Once the majority of the Monetary Fund goes along with whatever proposal the debtor government makes, and then approaches the commercial banks, I do not see how the commercial banks can say they will not go along. If we accept the proposition that the Monetary Fund is indirectly in control of political considerations of some of its leading voting members, then we must accept the fact that commercial banks are indirectly affected by such political considerations.

MR. HAWLEY: There are difficulties faced by many countries at this time in meeting their payments, their requirements for external capital, and finding external capital sources. However, this does not mean that there is something wrong with the world system because these people have to continue to borrow. Developing countries continue to borrow because of the nature of the development process. These countries cannot grow without capital coming into the country. That does not mean that there are not some fluctuations in the ease with which they can handle that burden and in the financing needs that they face. There is something almost inevitable about the continuing borrowing, but it does not mean that there is anything wrong with the world economic system. Developing nations cannot generate within their own countries enough savings to fund continued growth. The alternative is no growth. We are not promoting that solution.

When we run into the need for debt refinancing, there are many things we try to do before we attempt rescheduling the debt. Borrowing countries will face balance of payments difficulties from time to time on a temporary basis. Refinancing is only one, and probably not the initial step, that you begin with when working with borrowing countries.

MR. BELLER: The question is, what do you do when a country

runs into difficulty? First, when faced with a country having balance of payments problems, certain structural changes within the economy are suggested. If that fails, a restructuring of the existing debt, either on a public level or on a private level, is considered.

What I would call a disorderly debt relief has not occurred more than twice in the last twenty years. Disorderly debt relief means a unilateral moratorium on debt collection. The real thing bankers like to do when they see a deteriorated situation, whether it be a commercial loan or a sovereign loan, is to try to work it out. They try to extend a little expertise to prevent the situation from deteriorating to the point where rescheduling would be required.

PROF. LILLICH: I disagree with both Mr. Hawley and Dr. Adede. The reason why banks do not want to be referred to the law of the borrowing country is not because of lack of certainty of that law. We can always get lawyers to tell us whether that law is crystal clear or not. Try to find out what the fiduciary obligations of corporate insiders are here in New York, under the New York blue sky law, and you will find something that is more confused than the measure of compensation in international law. I do not think that the problem is a lack of knowledge. Additionally, I do not think that Dr. Adede's suggestion about the low level of administration of justice in a particular country is necessarily a key factor.

Everyone wants to know what the rules of the game are and wants not to have the rules changed. This is the key factor from the bankers' point of view. If you go into a loan agreement here and you subject yourself to Malawi law or Italian law, and they reserve the sovereign prerogative to change the law, change the rules of the game after you have started to play it, difficulties are created. Substantively, the rules of the game can always be changed, according to the sovereign prerogative of the state, here the borrower. You are nonsuited from the point of view of getting any diplomatic protection or procedural backing from the outside. This is the combination of eliminating any standard of compensation in the nationalization area on the substantive side and, of course, denying anyone of what the International Court of Justice has called an elementary principle of international law. This is the reason why you have references, as we did in the recent settlement with Peru, to the law of New York. If the developing states want to have loan agreements here that are equitably negotiated, they're going to have to be equitably enforced, and that cannot come by taking Article 22C thinking and translating it into this area. And this is why I think you will continuously see references to the law of New York.

PROF. GOLDIE: I would like to call on Professor Lillich to speak on the development of international financial institutions in this area, particularly from the public point of view.

PROF. LILLICH: I would like to comment briefly on Dr. Adede's recommendation for a new tribunal for debt rescheduling and Mr. Robertson's reference to something like an international bankruptcy court, or at least a court for rescheduling. Dr. Adede's paper goes into some detail about the International Center for the Settlement of Investment Disputes, holding it out as a possible model. As far as I know, there has been no real development, either in the literature, or by people in government on this particular problem. One of the points that Dr. Adede makes in his paper is that we need to develop some principles or norms or guidelines, for dealing with the rescheduling of debt obligations which take into account the myriad factors brought forth this morning. As Dr. Adede's paper pointed out, we are dealing with all kinds of different Third World non-oil exporting countries and they all have to be handled differently to some extent. Nevertheless there should be certain normative guidelines and some kind of process orientation rather than the kind of ad hoc creditors clubs that meet from time to time. Actually my observations are not as much observations as reflections upon the inadequacy of the present structures and requests for further development of these ideas presented by Dr. Adede.

PROF. GOLDIE: Thank you. Before we go into our second item, I will first ask Dr. Adede whether he would like ad hoc to show some guidelines and outlines on his thoughts in addition to his paper.

DR. ADEDE: As Professor Lillich has pointed out, one has to sit down and compare the models and work out something that is worthy of presenting. The paper just points to these issues and makes suggestions. One needs to spend a great deal of time trying to work with these models while exploring the reasons why there has been little development in the financial world of these central issues. By isolating these Third World problems, one would increase development of this model that has been suggested. This is an issue that ought to be examined and not be discussed lightly. I see an international tribunal as a suggestion which should be given some thought.

MR. ROBERTSON: The proposal has been tentatively approached by the Third World at the North-South dialogue,²¹ but there should be some sort of permanent institutional machinery to

21. N.Y. Times, May 31, 1977, § 3 (Business and Finance), at 1, col. 6.

which individual developing countries could go for help in renegotiating their financial arrangements with creditors. Behind this idea is the problem that it is difficult for a developing country to obtain the same concessions from all of the different types of creditors it has. If the fundamental goal of a particular renegotiation procedure is the reinstatement of a particular country's development progress, the approach taken is, first of all, to determine what the overall financial requirements are for that country to maintain a particular level of imports. At this stage of the proceedings, it does not matter what the source of those potential funds are. You need to obtain a certain rate of growth which is presumed to be adequate.

The next stage is to determine from where those finances are going to come. The idea is to have a permanent institutional framework that would bring together all of the different suppliers of finance into one forum. The result would be more equitable financing agreements. The idea is not any more concrete than that at the present moment. I might add that in this view of the situation, the distinction between public and private does not break down, but remains very much a problem.

MR. TRIMBLE: I would strongly question the need for such framework. If a country wishes to refinance existing debt or arrange new financing, there is no mystery as to how to go about it. And there really, in my own personal view, is no need for any sort of an institutional mechanism, particularly any mechanism that would set preconditions as to the terms in which the loans could be negotiated. As I understand the proposal, this institution would be set up in such a way that it would be a mechanism to which a country could come and demand that the existing debt be rescheduled. Its needs would be defined in accordance with criteria evolved within that institution, that would be gauged to development, not necessarily financial needs, and that concessional terms would be part of the program. So we have the same basic problem we discussed earlier in the guise of a kind of neutral institutional framework.

MR. ROBERTSON: The idea is more than there would be a commitment within this institutional framework, on the part of the creditors on the one side and the debtor on the other side, to abide by certain rules of the game, which would include estimates of capital requirements for that country to maintain a certain development path. Now that is not to say, necessarily, that debt rescheduling is the solution. It may be additional finance, there may be changes in domestic policies that are required, or what have you. It's just that the framework would be development oriented.

PROF. LILICH: I just leave you with Polonius' advice: Never a borrower or a lender be.²²

MR. HAWLEY: Without going into a detailed discussion of these proposals, the question of a forum in which discussions are undertaken to tackle debt problems is one of the critical issues which is being raised in many quarters now. I would base any inspection of these proposals, in whatever form they may take, on the warning that we do not begin to construct rigid, codified rules; initiatives which have the opposite of the effect we intended to achieve. Mixing the private creditors with the official creditors in a common forum is very difficult at this moment to achieve in an effective way without having an eroding impact on the willingness of the private lenders to lend further.

I do not want to be in the position of saying we cannot improve on the present. Obviously, there are some improvements that could be made. There could be improvements in the way official debts are handled among governments, perhaps by further refining the Paris Club arrangements, which have recently been a very last minute, somewhat confused exercise. These kind of improvements could be made. But when you talk about the linkage between the official and private creditors, you are moving into an area where there could easily be a damaging impact rather than an improving impact. The fundamental point is to find a solution that facilitates the continued flow of capital to these countries and even the expanded flow of capital, rather than a solution that begins to erode confidence, and, therefore, begins to dry up these flows.

PROF. GOLDIE: Thank you very much, Mr. Hawley. Now we come to the question before this panel, namely, is the whole problem not one of debt servicing, but of chronic balance of payments deficits. The question then becomes, is the problem likely to go away? If not, are we likely to be faced with a geometric progression of increasing indebtedness and servicing costs?

PROF. FRANCK: The agenda, as presented this morning, didn't allow for an extensive treatment of this question. We did present, shall we say, embryonic data to show that the problem is indeed linked to the balance of payments deficit on current accounts which Mr. Hawley and myself suggested will be an enduring feature of countries in the process of development. This is nothing to be condemned and does not reflect mismanagement necessarily. In a few

22. *Hamlet*, Act I, Scene III.

cases there was evidence of mismanagement or bad management, but in most cases it is simply an excess of the foreign exchange over what the economy of the less developed countries can now produce. To be specific, the World Bank just put out separate G.N.P. figures for low-income countries earning less than two hundred dollars per capita.²³ There are a billion people living in those countries. Their per capita income has been stationary for four years at ninety-one dollars,²⁴ an estimate put out by the World Bank. These same countries are now owing thirty-two billion dollars.²⁵ Determining what internal adjustment would be necessary to discharge this debt service on thirty-two billion dollars is where the problem is. Some countries are facing serious adjustments on the internal front. Unless foreign external resources are available, until these countries are over the development hurdle their problems will be compounded. The last Chase Manhattan report for 1976 that was put out indicated that they were getting at least as much in 1975 from private banks.²⁶ At the same time, the judgment of the Chase Manhattan Bank on this issue is that the non-oil LDCs have utilized the amount of unused borrowing capacity that was available to them and the 1976 borrowing increased their debts by another fourteen billion dollars. As a result, the ability of the LDCs, either to postpone the adjustment to higher oil prices or to follow a statute of gradual adjustment, is becoming increasingly limited.

In other words, they worry that there will be a gradual, more rigorous application of credit criteria as the amount of outstanding debt created by balance of payments deficits begins to make some lenders nervous.

Some of these countries happen to be politically important to the United States, and, therefore, the United States Government now becomes worried about their economic, financial stability and viability in relation to the political objectives of the State Department. When they see financial troubles undermining the stability of a country, reinforced by obvious signs of deliberate instability, they begin to worry. There is reason to worry. It is a combination of development hurdles, as well as difficulties of finding an indefinitely external resource. The OPEC countries are now using up increasing

23. [1976] INT'L RECONSTRUCTION & DEV. BANK ANN. REP. 1.

24. INT. RECONSTRUCTION & DEV. BANK, WORLD DEBT TABLES (April, 1977).

25. N.Y. Times, May 15, 1977, §3 (Business and Finance), at 13, col. 1.

26. *Id.*, April 20, 1977, §3 (Business and Finance), at 49, col. 8.

amounts of their own surpluses, and in 1976, only Saudi Arabia and Kuwait maintained continuous surpluses. Others have gradually increased their import capacity with sufficient rapidity so that less will be available to other countries involved through the round-about channel of the European dollar market. Saudi Arabia and Kuwait, the only ones left, are both pushing the capacity for import and signing contracts to build new installations. I do not feel that we can count indefinitely on the fueling of bank resources in Europe, or on OPEC.

MR. HAWLEY: I have some comments on the points that Professor Franck has just made. On numbers, I would be cautious. I have not looked at the Chase report in detail, but we have to continue to draw a distinction when we refer to the World Bank numbers on the countries with per capita incomes at the lowest end of the scale. We must once again break down the kind of debt we are talking about. In this case we are talking about almost entirely official credits to those countries. We are talking about a problem that is to be faced by intergovernmental groups, the World Bank, the International Fund, and other groups through which we all express our political will and decision making. The Chase numbers were referring only to private bank lending and we are referring to all the LDCs. Once again, it is just an example of the complexity of dealing with these numbers and keeping constantly aware of what is behind each number in order to accurately ascertain the consequences. One final comment, it is true that the OPEC surplus may decline, but if the OPEC surpluses decline, counter-balancing deficits are thrust on the less developed countries and they will benefit by this situation, either directly or indirectly. Our problem has been that the OPEC countries have not been able to import enough to stimulate and to contribute to the trade balances around the world. But this should begin over a longer period of time to have some helpful impact.

PROF. GOLDIE: Thank you very much, Mr. Hawley. Barry Beller wishes to make a very brief comment about lending limits.

MR. BELLER: Some of the congressional restraints that U.S. public agencies have with respect to lending were mentioned earlier. I want to mention that U.S. banks also have legal lending limits, so even for argument's sake, if we felt that a particular country was credit worthy to the extent of a billion dollars, for example, a particular bank may only be able to lend it a hundred million. It should be emphasized that there are legal constraints upon the banks which determine how far they can go regardless of credit worthiness or lack of it.

MR. TRIMBLE: Another way of looking at the basic problem is that it is caused by the price of oil, an increase which was unjustified by market forces, and continues to be unjustified by market forces, or by any concept of equity. That was the cause and remains the cause. The ultimate solution is to decrease our dependence and this pertains particularly to the United States. It is not until we really do that and get serious about it that there is going to be any long term answer to this disequilibrium problem. In the meantime, what happens? One answer is that we will continue the process. The international system has worked, and has been quite remarkable in the last three years. The increase in private lending has taken up a lot of the gap, and there is no reason to assume that this will not continue. But the countries that are benefiting by this are not the Indias or the Pakistans. The less developed countries in the world have to rely on either reducing their imports or otherwise taking what can be drastic internal measures. Or they have to look to public loans, concessional loan, or old style foreign aid. To the extent that there is any meaningful answer to their problems in the immediate term, official lending, official assistance, increase in the World Bank capabilities, perhaps expansion at the International Monetary Fund, concessional facilities and things of this sort are the only relief.

PROF. AUERBACH: One of the underlying assumptions of the whole conference is that this debt which has been undertaken for "development" will some day lead LDCs into a position where they might not need further debt. I am trying to think of some other LDCs that have gotten off the ground, and not too many come to mind. It goes to the nature of what is the development process. The economists have debated for years and there is no agreement yet.

The World Bank has argued that capital intensive development is the road to go, that is to say if enough capital is pumped into a country, the increase in GNP and growth rates can be predicted fairly well. It provides a good statement as to how well off that country is becoming. That has not worked all the time and now the Bank itself is moving to a different set of standards or criteria. Robert McNamara, the president of the Bank, articulated some years ago this notion that we must be concerned with equity, or in other words, the poorest forty percent. I am talking about the World Bank itself, not the International Development Association, which is its soft credit agency, nor the International Finance Corporation. I am concerned with the Bank, which operates more or less as a bank with fairly strict market competitive interest rates. Even now the

World Bank, in its project analysis and proposal is looking to whether a project is going to make any difference on the poorest forty percent or not. This is a radical departure for the Bank on how it not only analyzes projects but also in deciding which projects it will front. In the most recent Bank report that I saw, McNamara parades the fact that Bank lending in the agricultural sector has improved two or three times over the past few years. This may not necessarily help the poorest countries.

Presumably, what it means is that there will be a different purpose for these bank loans. This is important because it may indicate an alternative model for the development process.

Forgetting about the Bank for a moment, there is an existing alternative model, the Chinese model of self-reliant growth. From the few press reports I have seen, it seems that the recently elected government of India is at least making noises towards self-reliant growth. We will have to wait and see what it does. The alternative that seems to be implicit here between no growth and capital intensive growth is not quite accurate. As part of this different Bank lending policy, there has been an agreed upon increase in the annual rate of bank loan commitments. There is already in the works a selective capital increase in the Bank's capitalization, which, once it gets passed, will increase as well available Bank lending resources.²⁷

MR. HAWLEY: Two brief comments on this trickle-down and ripple effect before we move on, because I do not want them confused. The OPEC surplus causes a corresponding deficit among the rest of the world, if it is looked at in simplified terms, and I obviously oversimplified before. It does not help very much to think of it in this simplistic way, but many people do. The rest of the world divides, in some ways, shares of the corresponding deficit. We have tried in many of the public institutions and governments to figure out ways of making that burden as easy a burden as possible on the developing countries. This was one of the reasons behind the Carter administration and the Trilateral Commission's early policy moves toward trying to stimulate the major economies, the United States, Germany, Japan, and so forth, so that the major countries would not be running surpluses as well and pushing more and more deficits onto the LDCs. The way this works, and admittedly it is

27. INTERNATIONAL RECONSTRUCTION AND DEVELOPMENT BANK ANNUAL MEETING, Res. 314, 315, *adopted by the Board of Governors*, [1977] INT'L RECONSTRUCTION & DEV. BANK ANN. REP. 202-05.

indirect, is that as the OPEC surplus declines, and there is less of a deficit that has to be shared, the immediate stimulus takes place in their purchase of manufactured goods directly from the West. But the stimulated demand for that equipment in turn is what drives the demand for the commodities from the LDCs up.

PROF. AUERBACH: Well, fortunately for Europe, the Russians came along, in a sense, one could make that argument. After the perceived threat to Western Europe it became quite clear to Congress and to the Executive that we have to help reconstruct Europe and we can not wait for the International Bank for Reconstruction and Development to do this. The Marshall plan came along, and NATO came along, and we had economic development, political stability, and a military alliance. There is not that commitment to the Third World. The West does not see the perceived risk. If there was a similar perceived risk to the American interests, as a similar risk was perceived in Europe, you might get a different response. But I am not convinced that Congress is all that hesitant, in some respects they are, and in some other respect I think they're not.

PROF. GOLDIE: I will call on Professor Franck who will be interested in speaking to this point.

PROF. FRANCK: Let us recall how the Dawes Debt was handled.²⁸ There was a decision in terms of the risk perceived that if you pressed Germany too hard on those World War I debts you may create more damage to the whole international community than any financial benefit that may come out of this. So without too much trouble, the Dawes debt was cancelled. Take a look at the lend-lease debt. We would be willing to close our eyes to some of those carry-overs for political reasons again. There may be a reason why in certain parts of the world the risks mentioned will be perceived, hopefully soon.

MR. TRIMBLE: One of the most significant things that we could do now would be to agree in the multinational tariff negotiations to a very substantial cut in the tariff levels of semi-processed, semi-manufactured products. That would probably be as beneficial to the economic future of the less developed world as anything we could do. We may actually be able to do that, because we have fairly broad authority under the existing trade act. But the problem is that we are in an age of very incipient protectionism, and, if you follow the workings of the International Trade Commission, you will

28. The Dawes Debt was the result of reparations from the First World War.

notice that there is a definite trend of very restrictive import relief. The procedures under which the Commission works impose severe import relief. The President can refuse the advice and do something less restrictive but that is subject to override by Congress. There is always a deterrent held by the Congress that puts us very near a wave of protectionism. Any time you do something to help the LDCs, if it is going to cut into American industry jobs, you skate on very thin ice, particularly at this time. This reinforces the absence of any sort of political or ideological commitment such as we had to Europe.

PROF. GOLDIE: I will now call on Mr. Hawley, and I think we can make this the closing presentation.

MR. HAWLEY: There is a recent case which seems to illustrate many of the problems which we have touched upon today and fits right into the main topic of discussion. The country of Zaire, dependent heavily on copper exports, got into severe balance of payments difficulties in 1975 and went into arrears on large amounts of external debt to a mixture of creditors all over the world: governments, private banks, mainly in large bank syndicates. The Export-Import Bank was involved in many major projects in Zaire to help them expand the copper facilities and the supporting electric power infrastructure for copper production. The world economy and internal problems overwhelmed the best efforts of the country. The country fell into arrears in making its debt payments. We were faced with a major problem which fits precisely into our topic today, one that differs very much from some of the other examples, such as the Peruvian example where the country really never did get into arrears on payments. In most of these cases the banks and the other creditors have been able to work together with the borrowing government in a way that anticipated the problem and avoided a specific rescheduling conference. In this case there were communication problems and great uncertainties as to the intentions and the capabilities of the government involved in terms of meeting its various obligations, which were a very complex mixture of official and private obligations. The initial outlook tended to use one number as a rough estimate of the total debt of the country. There was no early attempt to segregate the types of debt involved or to break them apart for serious analysis of what would be a more productive solution to the problem than initially appeared intuitively obvious.

The first groups to move toward a solution, because they were the first groups to which the government of Zaire went in search of debt relief through official creditors, were quite logically the govern-

ments. This was done in negotiations that took place in Paris in an informal forum, known as the Paris Club. This group of government creditors grew up in the early days of refinancing back in the 1950s and was concerned with international monetary questions before the payment system had evolved to the point where it has today. It was designed to handle other kinds of problems, but gradually evolved into a debt renegotiation club, the group's primary preoccupation today. Governments gathered in Paris in June, 1976, and hurriedly negotiated an agreement describing the type of new scheduling. In this case, we are talking about a rescheduling in the sense of a stretching out of the maturity schedules and repayment schedules, on Zaire's official and officially guaranteed debt. No participant in the room, that I have been able to find, actually knew how much debt they were talking about. There was no central record anywhere of precisely who were the creditors nor of the amount of all the debts and maturity schedules. The governments agreed on the general outlines of the settlement and then adjourned leaving the detailed negotiations to be carried out bilaterally between each government, the borrowing government and the central bank.

Not long after that everyone was waiting to see what the banks would do. In Washington, the conventional wisdom was that since the agreement in Paris all that was left to be done was to take the same schedule and stretch the debt out the same way. There was a general expectation this would be done. It was true at the Treasury and the State Department; it was true at the International Monetary Fund and in the Central Bank of Zaire, which also assumed that we would take the same model and stretch the debt out. Indeed, we sat down with the Central Bank of Zaire and began to examine this question in light of the comments I made this morning, namely the search for a solution that looks to the future and tries to rebuild the country's access to needed sources of financing, rather than a solution that endangers future sources of financing in the private market. We pointed out that if there is a way to avoid a conspicuous failure in their obligations to the private creditors, if there is a way to actually make those payments, there may be a way to recreate the credit ratings of the country as part of an effort to get the economy moving again. Granted, there were many assumptions and much hoping involved in this. There are assumptions on the course of the world economy and on the course of movements, political events in central Africa and many other things. All of us agreed it would be worth the effort to make the most detailed examination of the numbers possible, of the balance of payments ac-

counts, all the trade accounts, export figures, what the market seemed to call for, and how the next year or so seemed to look. The agreement that this was an avenue to explore was quickly reached and explored in great detail by working closely with the government of Zaire from the beginning.

There is the distinction made, which I feel is critical to a productive solution to these problems, and that is the distinction between official credits and private credits. The distinction being important because of what we perceive to be the different impacts on a country's future access to finance on their failure to make commitments to official creditors as opposed to failure to meet commitments to official creditors. We decided not to follow the Paris model, but rather to explore the possible course of action that would involve repayment of the debt. We first had to measure and see what portion of the debt really was private credit and whether it was manageable. It was determined that it was manageable, under certain assumptions, given a reasonable course of events in and outside of Zaire. Zaire agreed to take certain actions, which were again along the lines of the discussion we had earlier about Peru.

The question put to us was basically is there a chance of restoring our credit ratings? If so, how would you describe what we would have to do in order to be able to go into the market again and be able to get access to private funds some time in 1977? Once it was determined to be fiscally and financially possible that they would repay all the interest, we worked out an agreement with them bringing themselves up to date on interest payments. This agreement was reached before the end of 1976. They agreed to pay their principal arrears within a short time period over the first few months of 1977. At the same time, they began a series of self-imposed measures determined to improve the management and performance of the domestic economy and also established a new debt management office at a senior level of the government to get a better handle on the numbers and better control over their external accounts, particularly borrowing from abroad. We pointed out that in order to raise the kind of money they were going to need, they would have to have some kind of a credential to show not only that they asserted they were trying to improve their economic situation in their country, but something that would be a card of entry, more or less, back into the financial markets. We determined with them that the most appropriate way in this case would be to apply for and to be granted eligibility to draw on the higher credit tranches of the IMF. This was done not so much with the idea that they would draw the money,

but simply because we wanted the world to perceive Zaire as having qualified as being eligible to draw that money which certified a certain level of performance. Once these conditions were met, we then undertook to use our best efforts to raise the large amount of money in the international market that we determined Zaire would need. This agreement combined a number of lessons that we talked about today. It showed the lender and the borrower working together to reach a solution that was productive rather than destructive in the market perception of the country, and which tries to maximize their position for future financing of their continued balance of payments deficits. This illustrates the way in which the private institutions already work closely with the International Monetary Fund, however, never blurring the important distinction between private credit and official credit, which I stressed at the outset. Any policy moves that may now be taken, either within the U.S. Government or within the international institutions, to formalize a linkage between private creditors and either government or international institutions has to be drafted very carefully in order to retain the flexibility that is required, by not only diversity within the countries, but also the fact that every one of these individual situations we have faced over the past twenty years has differed significantly from the others. They all had unique characteristics, and I hesitate to endorse a rule, code or linkage that would reduce our flexibility in coping most effectively with these problems.

PROF. GOLDIE: Thank you.