Debt Issues of the Trade and Development Report

by

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The views expressed are those of the author and do not necessarily reflect the views of UNCTAD
Sovereign Debt Workouts: Roadmap and Guide

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Current Gaps in sovereign debt restructuring processes

- Efficiency deficit - 'too little too late'
- Fairness deficit - unclear and non-transparent processes; asymmetric burden sharing
- Coherence deficit – legal fragmentation and lack of coordination (inter-creditor, creditor-debtor, inter-debtors); arbitrary decisions

➔ Unhealthy mix of uncertainty and biases; damaging economic and social costs when shock hits and crisis follows
Main challenges to be met

Improving bond contracts: strengthening commercial law

Keeping the *public interest* at the heart of global concerns - there is a need for:

– More legitimate processes capable of providing a fresh start to debtor states without denying creditor rights;
– Normative coherence at the international level that reduces uncertainty
– Clarification of processes in a transparent way for all that can reduce costs of restructuring;
– Impartiality of process which does not depend on narrow points of view and interests
Sovereign Debt Workout Principles

• Sovereignty
• Good faith
• Transparency
• Impartiality
• Equitable treatment
• Legitimacy
• Sustainability
• Majority restructuring

• GA Resolution 69/319: consensus-based, would apply to all debt instruments, greater coordination than market-based approaches
• non-binding, with no guarantee that a critical mass of parties would adhere to it
Restructuring Steps

Four steps:

• Decision to restructure
• Preparing for negotiations
• Negotiations
• Restructuring and post-restructuring issues

And one overarching challenge: Implementation
Debt workout mechanism

• UNCTAD has been a long-standing advocate of a multilateral debt workout mechanism drawing on national bankruptcy laws.

• Such a mechanism should meet 2 objectives:
  – prevent financial meltdown
  – Provide forum to facilitate an equitable restructuring
Preventing meltdown

• A temporary standstill, whether debt is public or private, and regardless of whether the servicing difficulties are due to solvency or liquidity problems (a distinction which is not always clear-cut); an automatic stay on creditor litigation.

• Standstills should be accompanied by exchange controls, including the suspension of convertibility for foreign currency deposits and other assets held by residents as well as non-residents.

• Provision of debtor-in-possession financing, automatically granting seniority status to debt contracted after the imposition of the standstill. IMF should lend into arrears for financing imports and other vital current account transactions.

• Debt restructuring including rollovers and write-offs, based on negotiations between the debtor and creditors
Merits of the UNCTAD approach

• Deals with process from a substantive point of view beginning with a set of principles (instead of focusing on an institutional debate)
• Acknowledges the political nature of sovereign debt workout processes (instead of treating it as a purely commercial endeavor) - and the importance of public interest
• Is Inclusive (across the spectrum of stakeholders' opinions) and comprehensive (from beginning to end of debt workouts)
• Provides a flexible instrument needed in a complex and ever-changing financial environment
• Identifies institutional gaps: case for a Debt Workout Institution
Thank You

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