THIRD DRAFT
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Lessons from the 1980s: Sovereign Debt in the Global Pandemic

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On August 12, 1982, the Mexican authorities closed their foreign exchange market. The next day, finance minister Jesùs (Chuco) Silva Herzog arrived in Washington seeking immediate financial assistance from the US authorities and support from the international Monetary Fund (IMF). The visit was not a surprise. Silva Herzog and Bank of Mexico governor Miguel Mancera had been visiting monthly since March. The IMF already had a team in Mexico discussing a possible support program. What followed was the Mexican Weekend of August 13-15 marking the outbreak of the Latin American debt crisis. The authorities of Argentina and Brazil soon also beat their path to the IMF and the US authorities for support. The crisis lasted into the early 1990s.

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Today, the economic and financial effects of the Coronavirus pandemic are expected to trigger global debt crises of greater magnitude and potentially with more severe and wide-spread medium-term consequences on growth and stability in the emerging market and developing countries (EMDC) than the Latin American debt crisis. On March 25, 2020, the President of the World Bank and Managing Director of the International Monetary Fund (IMF) called for a suspension of scheduled debt payments to official creditors by low-income countries through the end of 2020. The Group of Twenty (G20) ministers and governors endorsed their call on April 15. The also proposed that these countries' obligations to private creditors receive the same treatment. Bolton et al 2020, Gelpern et al, 2020, and Gelpern 2020a and 2020b have called for a debt standstill at least through the end of 2021 not only for low-income countries but also for middle-income countries.

Barry Eichengreen (2020) and Stiglitz and Rashid (2020) among others have invoked the 1980s debt crisis as a cautionary tale about the adverse economic consequences of delaying external debt reduction. They urge policymakers to support debt relief for these countries now to enable them to devote scarce foreign exchange and external financing to cover imports of medical equipment and supplies and to meet other needs occasioned by the pandemic.

In this paper, I review the experience of the 1980s and its relevance to policy debates today. I write more than 30 years later from the perspective of having had a ring-side seat at the Federal Reserve Board throughout the period. I was a second-level participant interacting frequently with representatives of the four groups centrally involved in managing the crisis: the borrowing countries, their foreign bank creditors, the authorities of the countries in which those banks were chartered, and the international institutions that were central to the crisis management efforts.

I draw two lessons from the 1980s for today:

I. The initiation of debt-relief will require a broad consensus among the four groups identified in the previous paragraph. In addition, each group must have a de facto leader.

II. Once a consensus is achieved, implementation necessarily will be case-by-case because of differences in the political and economic circumstances of each country.

I first sketch out the economic and financial context to the Latin American debt crisis, noting where the situation today differs. I next address the central question about the evolution of the crisis: Why did it take seven years from the Mexican weekend in 1982 to the announcement of the Brady plan in March 1989 for the debt strategy to embrace reduction in the face value of countries' debts to foreign banks. I conclude by returning to my three lessons and their applicability today.

CONTEXT

Table 1 presents data on the gross external debt of and international bank claims on 17 major developing country borrowers and the year of each country's first IMF program.[1]

Figure 1 presents trends in economic growth during the period. Growth in the dozen Latin American countries in the group of 17 countries plunged in 1981, was negative in 1982,

[1] Those 17 countries were the focus of the Baker plan proposed by the US treasury secretary in September 1985; twelve were in Latin America. Political pressures led to the addition of Costa Rica and Jamaica to the original list of 15 countries. The 17 countries accounted for 48 percent of the external debt of 33 emerging market and developing countries, 78 percent of the long-term bank claims on these countries, and 78 percent of total US bank exposure to these countries (Cline 1995, 40, 61 and 73).

and more negative in 1983. Global growth was minuscule in 1982 after two years of sub-par growth.

Inflation in US consumer prices was 6.1 percent in 1982 but declining. The US prime rate remained in double digits until mid-1985. The average rate of inflation for 11 of the 12 Latin American borrowers was more than 35 percent in 1980 and 1981, more than 45 percent in 1982, and rose to 75 percent in 1983.[2]

These countries were heavily reliant on net capital inflows. The average current account deficit for 10 of them was 5.0 percent of GDP in 1980, 8.9 percent in 1981, and 7.3 percent in 1982;.[3] Their gross external debts had increased by 150 percent from $118 billion in 1977 to $296 billion in 1982. Over those five years, the ratio of their external debt to gross national income rose 25 percentage points to 64 percent on average and would peak in 1987 26 percentage points higher.[4]

The external debt positions of many EMDCs also were problematic before the Coronavirus pandemic shock. The World Bank published a study (Kose et al. 2020) on global waves of debt that focused on a fourth wave starting after the global financial crisis of 2009. Domestic government debt and private international debt are larger components than in the previous waves in the 1970s, 1990s, and first decade of the 21st century. Nevertheless, the latest (2018) data on external debt assembled by the World Bank staff revealed for the Latin

[2] The source, IMF *World Economic Outlook Database,* April 2020, does not provide data for Uruguay and Venezuela.

[3] The source, IMF *World Economic Outlook Database,* April 2020, does not provide data for Argentina, and Venezuela was in current account surplus.

[4] These data are from the World Bank's international debt statistics https://databank.worldbank.org/reports.aspx?source=international-debt-statistics.

American countries as a whole an increase in gross external debt relative to gross national income from 23 percent in 2010 to 38 percent in 2018, and a rise from 24 percent to 36 percent for the countries of Sub-Saharan Africa. In addition, 16 countries outside of those regions had ratios of 60 percent or more in 2018. These countries were the focus of the World Bank/IMF Debt Service Suspension Initiative (DSSI) that the G20 endorsed and expanded to cover debt to private sector lenders to low income countries.

Compared with situation in 1982, the outlook for global growth today is worse for both advanced and less advanced countries as well as highly uncertain for both groups.

On the other hand, the banking systems in the advanced countries are in better shape. Figure 2 presents the evolution of US bank exposures to the 17 major borrowers during the 1980s of the nine largest and of all other US banks. In contrast, in March 2020, the now seven largest US banks had exposures to all non-advanced countries, excluding banking centers, of 83 percent of capital; the exposure of all other US banks was 23 percent of capital (CLES 2020). Financial system stresses should be expected in the wake of the pandemic, but not on the scale of the 1980s.

The IMF also is somewhat better financially equipped in 2020 than it was in 1982. Today it has about $1.4 trillion in gross financial resources. In 1982, its resources were about $80 billion. They were raised to $130 billion in 1983. International trade is now ten times higher [https://www.wto.org/english/res_e/statis_e/wts2020_e/wts20_toc_e.htm]. World GDP (on a PPP basis) is now about eight times higher (IMF 2020). Before the August 1982 Mexican Weekend, the IMF was actively lending (table 1). In March 2020, the IMF had $155 billion in current commitments to 21 members, including five that were among the 17 major borrowers in the 1980s: Argentina, Colombia, Ecuador, Mexico, and Morocco.

DEBT RELIEF IN THE 1980S

The debt crisis of the 1980s unfolded in three phases: The Concerted Lending phase from August 1982 until October 1985. The Baker Plan phase from its unveiling at the IMF/World Bank Annual Meetings in Seoul in 1985 until March 1989. The Brady Plan phase starting with the US Treasury Secretary Nicolas Brady's announcement of his debt-reduction plan in March 1989 continuing until the mid-1990s.

Debt relief broadly defined was central to each phase. In the first phase, debts to international banks were rescheduled. However, the present value of this debt increased because their interest rates were raised. In addition, in the concerted lending phase of the crisis, the major cases the banks were required to make new loans to certain borrowers proportional to their existing exposures as a condition for IMF approval of the programs. In the latter part of the first phase and the second phase, the negotiation of multi-year rescheduling agreements, first by Mexico in September 1974, involved a stretching out of maturities and a lowering of interest rates and a modest reduction in the present value of the debts.[5]

In the second phase, the borrowing countries employed a range of techniques such as buybacks at below par and debt-equity swaps at discounts. Thus, the face value their debt was reduced.

[5] Frequently the interest rate was repegged to the London Interbank Offer Rate (LIBOR) which was 100 basis points lower than the US prime rate previously employed and the margin was reduce to 13/16th compared with margins of 150 basis points and higher previously.

In the third phase, two items were added to the menus offered to bank creditors: (1) securitizing the written down principal of the debt while maintaining something close to a market interest rate (par bonds) and (2) doing so via a present-value-equivalent in which the principal remained intact but the interest rates was substantially below the market rate (discount bonds). The Brady bonds normally were backed by 30-year US treasury zero-coupon bonds and a portion of the interest payments were guaranteed by funds held in escrow. In this phase, banks also had the option of continuing to supply new money.[6]

Although several commentators, most prominently Peter Kenen (1983), called for collective action to reduce the stock of debt early during the Latin American debt crisis, there was no appetite for such an approach among the principal groups of parties in 1982. The borrowing countries were wary of jeopardizing their access to bank financing which they expected would resume quickly. The interim minister of economy of Brazil, Carlos Viacava, commented to the US authorities in December 1982 that Brazil expected to be back in the market within a year. The international commercial banks were opposed to reducing the principal amounts of the claims on the major borrowers, fearing a domino effect spreading to other borrowing countries that would substantially erode their limited capital; see figure 2.

Their authorities shared these concerns as did the IMF.[7] An immediate write down of bank claims was not considered, in part because of concerns about the stability of the global banking system. Avoiding this risk was implicit in the approach that was taken in the first phase

[6] Mexico issued the first Brady bonds. Cline (1995, 222) reports that in the Mexican package 22 percent of the banks by the face value of their claims chose new money while 47 percent chose par bonds (with a reduced interest rate) and 41 percent chose discount bonds (reduced principal with a market interest rate). In the 18 Brady packages that he reviews, Cline (195, 233) reports that new money accounted for only two percent.

[7] Jacques de Larosière (2018) reports that during the Mexican weekend, he convinced Silva Herzog that Mexico should not default on its debt to commercial banks. However, this option was not discussed with US officials.

of the crisis. These shared concerns were instrumental in persuading the major central banks supported by their governments to act collectively to supply short-term bridge loans to several of the borrowing countries.

The initial debt strategy was predicated on the view that the borrowing countries faced a liquidity crisis compounded by macroeconomic imbalances. With appropriate policies of economic adjustment, the borrowing countries would resume growth and regain access to international financial markets. Moreover, it was expected that global growth would pick up as it did. See figure 1. Analysts, including some who later were critical of the debt strategy also pointed to the revival of growth in the world to contribute to a revival of growth in the borrowing countries, allowing them to grow out of their crises (Cline 1983, Cooper and Sachs 1985, and Dooley et al. 1983).[8] These early assessments of the initial debt strategy in the major cases were analogous to the more sophisticated debt sustainability analyses conducted today by the IMF staff. In today's terms, these assessments were positive.

Experience in the 1970s, when many countries faced external financial crises associated with oil price increases, rising global inflation, and fluctuations in global economic performance, suggested that the traditional approach to financing and adjustment would prove adequate to address the economic and financial challenges facing the borrowing countries in the early 1980s.

In this early phase, IMF lending went primarily to cover current account deficits but not exclusively to service bank debt. For the three major Latin American borrowing countries

[8] South Korea, along with Argentina, Brazil, Chile, Mexico, Peru, Philippines, and Venezuela, was the focus of Dooley et al. It was not clear at that time that Korea would not be caught up in the debt crisis.

(Argentina, Brazil, and Mexico), new money loans from the banks totaled $12.7 billion in 1983. They covered about 70 percent of their interest payments due to banks that year and a similar amount in 1984 when the of total amount of concerted lending was somewhat larger.[9]

In January 1984, leaders of 26 Latin American and Caribbean countries met in Quito, Ecuador and issued a statement rejecting a debt moratorium but calling for priority to be given to economic development. Representatives of 11 of those countries met in May in Cartagena, Colombia and declared their willingness meet their debt obligations and at the same time called for recognition that their debts were a political problem. Subsequent meetings of the Cartagena group were unable to table a plan to meet those perceived needs (Boughton 2001, 479).

Contrary to the assumption underlying the debt strategy in this first phase, voluntary financing from the international banks did not quickly return to the affected countries. Concerted bank lending to Latin America was $13.3 billion in 1983, and $15.5 billion in 1984, while so-called spontaneous lending declined from $1.9 billion in 1983 to $0.6 billion in 1984 (IMF 1990).

In July 1985, Alan Garcia became president of Peru. He announced that Peru would devote no more than 10 percent of government revenues to debt service, giving priority to creditors that would lend Peru additional funds. Peru went into arrears with the IMF and, in August 1986, was declared ineligible to borrow from the Fund until it had cleared them. Thus, Peru defaulted on its debts. It did not achieve an agreement to reduce its stock of debt.

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[9] Most syndicated bank loans were based on the prime rate at that time—LIBOR was about a percentage point lower—which averaged 10.75 percent in 1983. With a 2.25 percentage point margin, the estimated interest bill for the three borrowers on their $137.2 billion in commercial bank debt at the end of 1982, was $17.8 billion.

Peru was not alone in beginning to build arrears to banks and other creditors. Meanwhile, the willingness of smaller banks to participate in new money loans declined. Debt fatigue had set in for many borrowers and lenders.

These developments motivated the Baker plan. It was viewed as a midcourse correction to the existing debt strategy. The plan emphasized structural change (such as liberalization of foreign investment regimes and privatization) rather than fiscal adjustment, set target for banks to lend $20 billion to the 17 countries identified with the initiative over the next three years,[10] and called for increased lending of $10 billion by the World Bank and the Inter-American Development Bank to these countries over the same period. Cline (1995, 209) reports that the targets for the supply of external financing were substantially met. However, in 1986 the price of oil collapsed, undermining Mexico's ability to develop a program to take advantage of the Baker plan, while Argentina and Brazil engaged in complex transitions to democracy and inflation in the triple-digits which limited their scope to develop medium-term plans.[11]

In late 1985, none of the four principal parties to the strategy (banks, creditor countries, IMF, or borrowing countries) supported debt relief in the form of writing down the principal of bank claims, nor with a very few exceptions did any influential commentators support such an approach.[12]

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[10] See footnote 1.

[11] Heavily indebted oil producers like Bolivia, Colombia, Ecuador, and Nigeria were also adversely affected by the oil price collapse. Venezuela avoided the adoption of an adjustment program supported by the IMF at that point.

[12] I have been reminded that economists at the Organization for Economic Cooperation and Development argued as early as 1984-85 that the debt strategy was not working, but that organization was not central to policymaking at that time.

In June 1986, Jeffrey Sachs (1986), an earlier advocate of the concerted lending strategy, argued that the earlier optimism about crisis resolution had been disappointed. He advocated a new approach including a substantial debt relief component. He articulated principles to guide selective debt relief that should be limited to those countries most in need , on a case-by-case basis, and linked to internationally supervised programs of policy reforms in the debtor countries. [13]

In January 1987, Jacques de Larosière was succeeded by Michel Camdessus as managing director of the IMF. On his departure, de Larosière suggested that a change in the strategy toward bank claims was needed.

Thinking at the IMF began to change though staff views were divided (Boughton 2001, 481). Dooley (1986), another earlier advocate of the initial debt strategy, wrote that an overhang of external debt with face values that was more than their current secondary market values was a disincentive to foreign and domestic investment in the country and, therefore, growth.[14] Although the empirical foundation of his argument was weak (Cline 1995, 173), the paper was very influential.

Much of the academic work on the topic at this time focused on incentives for both the banks and the countries to cooperate always on a voluntary, market-based approach to reducing the stock. One argument emphasized the division between banks that saw no future in pursuing their claims and wanted to get out and those that were more positive and realized that if the first group reduced the face value of their claims, the remaining claims would

[13] He explicitly excluded Brazil from countries in need.
[14] See also Dooley (1989).

become more valuable. In the event, some banks in the second group opted to provide new loans.

By 1987, as it became clear that the Baker plan was not going to achieve its objectives, the academic community turned its attention to the ways and means of debt relief, and the capital positions of the major banks had improved – see figure 2. Analysts within the official sector had begun to think more seriously about debt stock reduction. I am not able to report on thinking in other countries, but at the Federal Reserve Board, by the middle of 1986 my colleagues began to analyze what we called Plan B involving debt relief. This analysis continued in the first half of 1987. [15] We also actively considered a Plan C that would have drawn on Article VIII(2)b of the IMF charter as a mechanism by which the IMF could permit the imposition of controls on debt payments in support of a member that needed leverage over its bank creditors, including debt relief.

In February 1987, another new Brazilian government announced a moratorium on interest payments on its medium- and long-term debts to banks. But the initiative did not attract followers, and the country spent years getting back into the good graces of the IMF and its bank creditors (Boughton 2001, 458 and 529).[16]

Debt sales in secondary markets increased as banks added to their reserves and unilaterally wrote down the value of their claims on their books and on reports to their regulators. Citibank grabbed headlines in May 1987 by announcing that it was adding $3 billion to its reserves against possible losses on its claims on developing countries.

[15] The memory of my colleagues is that Volcker asked for this analysis, and he certainly was a recipient of it. His term ended in August 1987.
[16] One consequence was that Brazil did not reach a Brady agreement until 1994.

Several small-scale initiatives effectively reduced the principal amount of some countries' debts. For example, after extensive negotiations, Bolivia in early 1988 retired about a third of its bank debt at 11 cents per dollar in a buyback. The official sector did not oppose this initiative or the Mexican-Morgan initiative. In 1987, Mexico with the technical support of Morgan Guaranty Bank made an offer to exchange up to $20 billion in face value of its debts for marketable bonds backed by 20-year zero-coupon bonds. The offer was taken up by banks with only $3.7 billion in claims at a discount of 30 percent, compared with an expected 50 percent discount (Boughton 2001, 490-491). Bulow and Rogoff (1988) were critical of these operations as well as debt-for-equity swaps on the grounds that the borrowing country may have risked scarce resources that would be better deployed at a future date. At their time of writing, the weighted average price of the debt of eight Latin American borrowers was 50.2 cents per dollar of face value ranging from 29 cents for Argentina to 60.5 cents for Chile.

Meanwhile, proposals for systematic debt reduction had already surfaced in the United States and elsewhere. Two examples were plans by Senator Bradley (1986) and Congressman LaFalce (1987). One of their motivating concerns was that the slow growth of the borrowing countries was negatively impacting US exports. Japanese finance minister Miyazawa proposed to the G-7 in June 1987 that a type of exit bond be included with the principal amount of the debt secured by a zero-coupon bond purchased by the borrower with the financial assistance of the official international financial institutions and a carrying a reduced interest rate. At the IMF annual meeting in Berlin in September 1988, the Bank of Japan governor reiterated Japan's support for this addition to the strategy (IMF 1988, 37-43).

US Treasury Secretary Brady, who had replaced Baker, in Berlin expressed “skepticism [about] proposals that may appear to conform to the basic principles of the debt strategy, but which in practice produce only an illusion of progress. . .. [And build] political opposition among taxpayers in creditor countries.” (IMF 1988, 43-47) He was particularly critical of the use of funds from international institutions or other governments to finance debt reduction activities bailing out the banks. Nineteen eighty-eight was a US presidential election year, and the US administration wanted to distance itself from potential calls for use of official funds to finance debt forgiveness for domestic borrowers such as farmer and local governments.

By the end of 1988, the reported exposure of US banks to the 17 highly indebted countries had declined by $20 billion (about 20 percent) from its level at the end of 1982. The decline for the nine largest banks was less than 10 percent, but that for other US banks was almost 50 percent; see figure 2.

Following the US presidential election, the stage was set for a more systematic approach to recognizing reductions in the face value of claims on the borrowing countries. On March 10, 1989, Secretary Brady proposed an amended approach. The Brady plan contained four key elements: (1) a portion of IMF and World Bank loans would also offer financial support to help collateralize the principal amounts of new instruments with US treasury zero-coupon bonds and partial interest guarantees; (2) their new lending also would be used to help countries buy back their debts at a discount; (3) the commercial banks should waive the sharing and negative pledge clauses in their agreements to permit individual debt reduction operations; and (4) the Fund should modify its policy of not lending to members while they were in arrears to their bank creditors, reducing the leverage of banks in their negotiations with borrowers. [17]

[17] The approach that Brady announced differed from the initial proposal of the US Treasury. The earlier proposal minimized the role of the IMF and the World Bank and did not envision building on the menu approach to debt reduction. Subsequently, the IMF did modify its approach to lending into arrears to private creditors on a case-by-case basis subject to several qualifications, including that the countries were negotiating in good faith with their creditors.

Despite US and IMF management support, the Brady plan was not immediately embraced by all borrowing countries, the bank lenders, or all of authorities in the countries in which they were chartered. Individual countries' negotiations of Brady debt-reduction agreements with their commercial banks often dragged on for months. In 1989, agreements in principle were announced with Costa Rica, the Philippines, Mexico, and Venezuela. However, the first Brady bonds were not issued until January 1990 by Mexico. Only nine of the 17 major borrowing countries Baker plan beneficiaries completed Brady packages over the next five years: two in 1990, 1991, and 1992 and one per year 1994-1995.[18] (See last column of table 1.) The Brady plan marked the beginning of the end of the global debt crisis of the 1980s, but it was not a breakthrough. The unveiling of the Brady plan in March 1989 is convenient date for historians to mark the end of the global debt crisis, but it is arbitrary like the use of the Mexican weekend as its start.

In 1991, growth picked up in the major Latin American borrowers on average; figure 1. In the 1990s, emerging market and developing countries gradually regained access to international financial markets. Their access was not to syndicated loans from commercial banks but to the international bond market, which had been eclipsed as a principle source of international finance for developing countries since defaults during the Great Depression; see Cooper and Truman 1971.

[18] Brazil's 1994 package did not conform to the Brady formula because it was not linked to an IMF program and the international institutions did not finance any of the enhancements. The collateral was held at the Bank for International Settlements because the package did not meet the Federal Reserve's standard for facilitating the arrangements. The packages for Peru and Côte d'Ivoire were not completed until 1997 and 1998, respectively.

Reduction of the principal value of international bank claims on borrowing countries became an accepted component of the debt strategy only when a substantial consensus on its desirability had been achieved among the four principal parties to the strategy's continued implementation. Borrowing countries began to press for options to reduce their stock of debt, and Mexico once again led the pack in applying for a Brady package. The balance sheets of international bank creditors had strengthened, and many were anxious to put the exposure to the borrowing countries behind them. The key international institution, the IMF, had revised its thinking. Finally, the United States embraced debt relief as a menu item in negotiations between debtor countries and their banks.

In my view, the historical record does not strongly support the popular view that an overhang of debt to international banks was the principal cause of a "lost decade" of low growth in Latin America or that the pick-up in growth after 1990 was triggered by the inclusion of debt stock reduction in the menu of options. Chile and Colombia did not have Brady agreements. But Chile's compound growth in 1991-1994 exceeded the four-year compound annual growth for every Latin American country with an arrangement in the four years after their bonds were issued.[19] Similarly, growth in Colombia exceeded growth in five of the seven countries that had Brady arrangements.[20]

How consequential was the delay in incorporating debt stock reduction in the debt strategy? A comprehensive answer to this question is beyond the scope of this paper. My view is that it could have occurred earlier, possibly in 1986, probably in 1987 if the shifts in the IMF's

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[19] In 1988, the secondary market price of Chilean debt was the same as that Uruguay (Dornbusch comment on Bulow and Rogoff, 1988).

[20] The exceptions were Costa Rica and Uruguay.

views, the positions of France, Japan and, most important, the United States had come earlier. However, I am skeptical that rolling out the Brady plan or its equivalent in terms of debt relief two years earlier would have a significant positive effect on growth in the borrowing countries in 1988 and 1989, in particular given the lags in implementing Brady packages, in part, because the countries could not meet the associated policy commitments to the IMF.

Many of the borrowing countries faced deep political economy challenges that limited their capacity to adopt policies that would contribute to a resumption of growth. It is possible that the lack of significant debt relief contributed to those limitations. In this context Williamson's (1989) analysis of the ten key policy reforms in Latin American that in combination had a positive impact on economic growth in Latin America is instructive.[21]

LESSONS FROM THE 1980S

The focus of the evolving debt strategy in the 1980s was not on the size of the individual countries' external debts, except with respect to their collective scale and implications for the stability of the international banking system. The later concern helped to mobilize the major countries to coordinate their actions in 1982-1983 to provide bridge loans to IMF disbursements and pressure their banks to participate in financing packages. But the debt was not a major focus after that point. The primary focus after 1984 was restoring the growth of the borrowing countries.

The first lesson from the 1980s on sovereign debt relief is that a four-part consensus is needed. The four groups are the borrowing countries, their foreign bank creditors, the countries in which those banks are chartered, and the international institutions, principally the

[21] These ten reforms made up what came to be known as the Washington Consensus.

IMF. In the absence of a bankruptcy mechanism in which the debtor can initiate action and normally has considerable leverage, the four parties must solve a coordination problem. Their consensus need not be complete, but it must start with the key borrowing countries and receive political support from important creditor countries and institutions.

The establishment of consensus, however, requires credible leaders. In the Latin American debt crisis, without Mexico's expressed and demonstrated interest in debt reduction, without the United States finally putting forward a framework to accomplish it, and without the IMF's leadership shift to embracing that approach, the final chapter of the global debt crisis might have been delayed further.

During the crisis, Mexico was the poster-country for each new phase. Mexico's earthquake in September 1985 and the collapse of oil prices in early 1986 effectively sidelined that country from taking the lead under the Baker Plan. No other major borrowing country was positioned at that time to take its place. Similarly, until the new government of Carlos Salinas took office in late 1988, Mexico was not a major advocate of debt relief.

Would the leaders of Mexico and other major borrowing countries have welcomed a debt relief option in the debt strategy earlier, for example, in 1985? No doubt, some influential people in those countries would have. However, the inability of the Cartagena Group to reach consensus on how the debt strategy should be modified suggests that the borrowing countries lacked cohesion as a group.

Today, the Debt Service Suspension Initiative (DSSI) response to the Coronavirus pandemic illustrates the relevance of this lesson.

To date, no borrowing country has stepped forward to ask for the suspension of debt payments from private creditors. One reason is that the rating agencies, which had no direct role for the borrowers during the global debt crisis of the 1980s, signaled that doing so would probably result in a markdown of their rating for the country's marketable debt that would carry into the future.[22] This fact adds to the disincentive for countries to seek debt relief early. Sean Hagen (2020) among others advocates conditioning access to IMF resources by countries for which their external debt positions is neither clearly sustainable or unsustainable but rather uncertain on that third category of countries seeking a temporary standstill on payments of existing obligations. This approach would impose a similar disincentive because the rating agencies are likely to downgrade the country's bonds as result. The country's loss of market access would be accelerated. Therefore, a borrowing country must conclude that even a mild restructuring of its debts to foreign private sector creditors would be in its medium-term interest. If it decides to tough it out without immediate IMF financial support and the tsunami hits, the economic and financial damage will be greater. These are not easy choices.

These considerations have affected the taking up of the DSSI. As of September 1, 2002, only 39 of the 77 countries eligible under the DSSI had applied to the Paris Club for relief, and

[22] In the 1980s, the rating agencies had a much less influential role. Bank loans were not rated. Banks issued capital market obligations in relatively small volumes. The rating agencies did not downgrade the debt of the eight US money center debts until 1982. In that year, Moody's downgraded five of the eight banks from triple A and from double A for two others. J. P. Morgan's triple A rating survived until 1988. Ratings were substantially lower by the end of the decade (FDIC 1997, chapter 5). While rating agencies were not as influential in the 1980s as they are today. A roughly equivalent role to that of the rating agencies was played in the 1980s by banking supervisors. In the United States, the Interagency Country Exposure Review Committee (ICERC) could and did criticize excessive exposures and potentially require reserves against loans. An international complication was that in each of the countries in which the major banks were headquartered had different regimes and standards. In many European countries, reserves were deductible against taxes, but they were not in the United States.

28 had received relief.[23] Moody's initially placed the rating of the debt of several of those countries on review https://tellimer.com/article/debt-service-suspension-initiative-where-do-w. Moody's made this decision even though Paris Club participants decided not to require comparable debt-service-suspension treatment by private sector creditors of these countries.[24] Moody's has since confirmed it earlier ratings for countries that have received Paris Club relief. However, the agency has indicated, for example with respect to Côte d'Ivoire, that it will review its ratings of the relevant countries if they seek comparable treatment for their bonds.

Current advocates of debt relief also must take account of the crisis strategies of borrowing countries. Those strategies are more diverse than during the 1980s. Failure to do so may be counterproductive. For example, Patrick Bolton et al (2020) cite Mexico as a potential beneficiary from the DSSI, which does not fit its strategy. In the global financial crisis, Mexico sought and received a Flexible Credit Line commitment from the IMF, and that commitment has been renewed. After the Asian financial crises in the late 1990s, the strategy of several of the principal emerging market and developing countries has been to build their international reserve cushions against future crises.

Also relevant to prospects for a rapid agreement on a comprehensive approach to potential external debt problems of borrowing countries is that a larger number of countries have substantial amounts of debt today. As of 1988, 14 of the 17 highly indebted countries

[23] In July, the G20 finance ministers and central bank governors postponed deciding whether the initiative should be extended into 2021.See http://www.g20.utoronto.ca/2020/2020-g20-finance-0718.html.
[24] Seeking comparable debt relief treatment from other creditors is normally standard with the Paris Club.

accounted for 57 percent of gross international debts of 96 emerging market and developing countries. In 2018, their share was only 29 percent (World Bank, World Debt Tables).[25]

Leadership of the countries where the major private international creditors are chartered is also important. By 1988, both Japan and France were on record, along with the IMF, as favoring some form of debt reduction, but it was not until the United States changed its position that the process got underway. In 1989, the major banks were chartered in the G5 countries plus Italy, Netherlands, and Switzerland. The banks of those eight countries held 65 percent of total cross-border claims, and only 17 countries reported their data to the BIS (https://www.bis.org/statistics/about_banking_stats.htm?m=6%7C31%7C637). In March 2020, 39 countries reported on their banks. The same eight countries accounted for 70 percent of the claims, but the banks of four other countries, including importantly China, held more than 2 percent each. The US banks' share shrank by only 1-1/2 percentage points. The United States remains dominant among the countries that are home to major banks, but each of the eight countries plus China has at least one of the global systemically important banks (G-SIBs). China has four of them.

In the 1980s, each major borrowing country had its bank advisory committee often with overlapping bank representatives. One of the most prominent leaders of that effort was William Rhodes of Citibank. They had to balance the financial interests of their own institutions against the need to manage successfully the crisis in the interests of all parties. With more major bank lenders leadership is more complex. The Institute of International Finance played a

[25] Uruguay and Yugoslavia (and its residual components) are excluded from both the numerators and the denominators.

coordinating role in the restructuring of Greek debt in 2012 and the proposed including of private creditor in the SSDI. In the Greek case, success was achieved on the second try. The jury is still out on the SDDI.

The challenge today is also that international banks are not as dominant players in the external debt arena as they were in the 1980s. At the end of 2018, the BIS reporting banks' claims on emerging market and developing economies were 52 percent of the total external debt of 122 developing countries covered by the World Bank's international debt statistics. At the end of 1988, the equivalent percentage for a smaller set of countries was 66 percent. For Latin American countries, the figures were 36 and 67 percent in 2018 and 1988, respectively. For 14 of the 17 highly indebted countries they were 55 and 28 percent, respectively. [26] Moreover, the investors in sovereign debt today include hedge funds and similar entities, and derivative instruments are involved as well. Sovereigns are not the only entities that issue external financial obligations today. These facts pose challenges to restructuring external financial obligations. However, they are not inherently unsolvable.

The IMF and other international financial institutions played an important role in the 1980s and will do so in future crises, but their role is limited to prodding their member countries to act and responding to initiatives or lack thereof by them. However, once consensus has been achieved, the IMF and the multilateral development banks need adequate financial resources to support initiatives. In 1982, the IMF's resources were initially insufficient.

[26] This last group excludes Chile, Uruguay, and Yugoslavia from both sources. As of the end of 2018, based on the World Bank data commercial banks held only 17 percent of the external debt of low-income countries and 33 percent of that of middle-income countries (Gelpern et al. 2020).

That was again the situation in 2007 at the outbreak of the global financial crisis. The Fund's resources were built up in both cases. Today, in contrast, the IMF is much better positioned financially.

The second lesson from the 1980s experience for today follows from the first: the implementation of debt reduction will be implemented on a case-by-case basis, and small borrowing countries will not be pathbreakers. Each borrowing country's economic and financial circumstances differ. Equally important, each country's political circumstances differ. Countries going through political transformations, as was the case in Argentina and Brazil in the 1980s, will have reduced time and political space to devote to debt renegotiation. In other words, issues of political economy are crucial determinants of each borrowing country's approach to its external financial challenges.

Two features of the global economic and financial environment in 2020 do favor the facilitation of a systemic approach to debt reduction.

First, borrowing countries face a common external shock. The external financial impacts of the Coronavirus pandemic differ across countries, but the pandemic has affected each one at roughly the same time even though some countries were more, and some were less, prepared. This should help to support the four parties coming to a consensus about how best to respond to the potential need to restructure sovereign debt. However, any such process will take time.

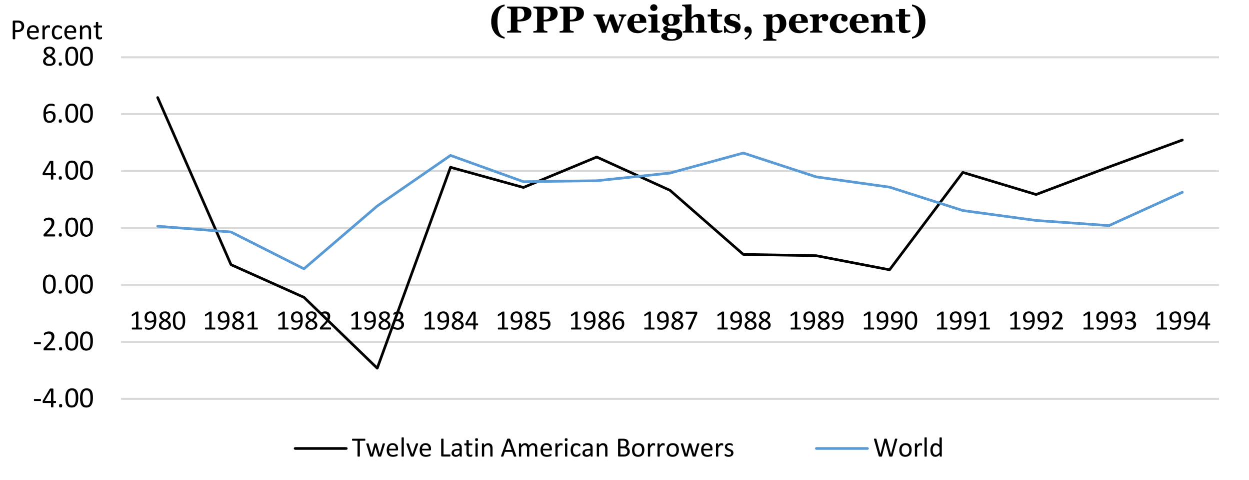
Second, considerations of the financial stability of creditors and the financial systems of the host countries' lenders are a less prominent concern than in 1982.

From the perspective of September 2020, achieving debt relief that results in a substantial reduction in the present value of claims on a broad swath of emerging market and developing countries, middle-income as well as low-income, is a lower priority than in March and April. In the context of low global interest rates and ample global liquidity, several major borrowing countries have maintained or regained access to international credit markets.

Nevertheless, in light of the global persistence of Covid-19 and the likelihood that the global recession will extend well into 2021, priorities may shift again

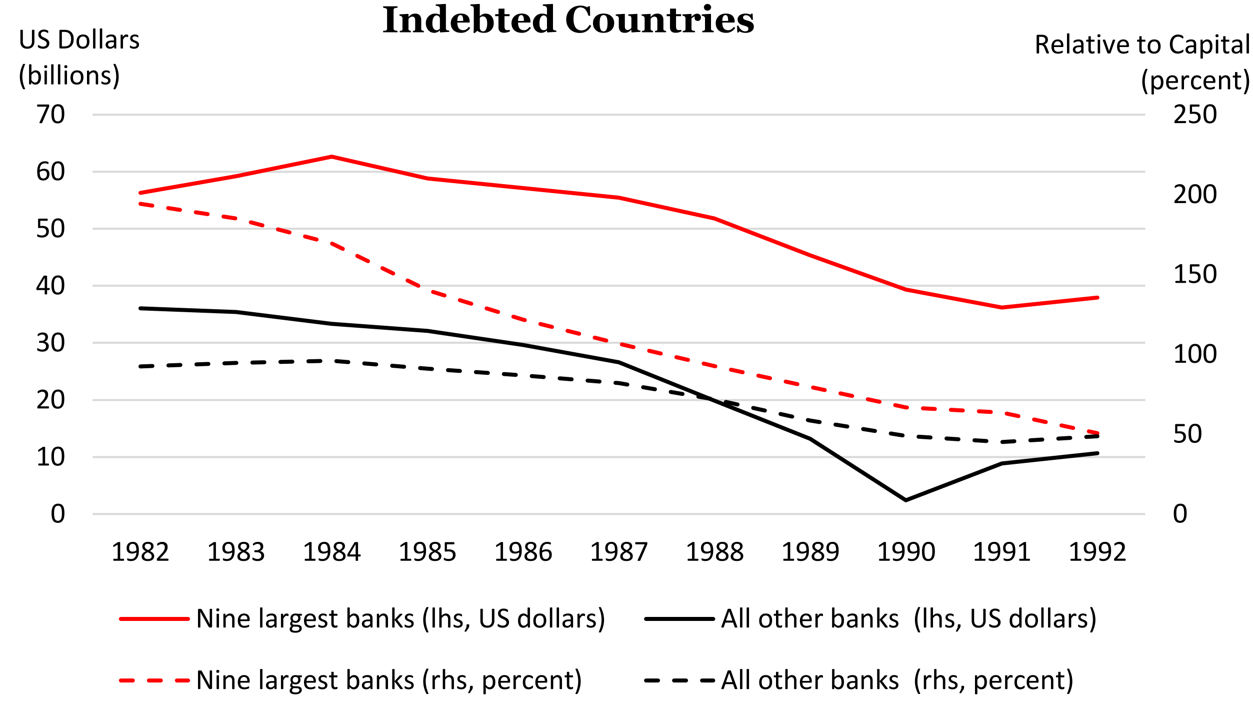
Many observers are optimistic about growth prospects in the advanced countries and expect positive spillovers to emerging market and developing countries. I am less optimistic. If my pessimism becomes reality, debt relief will again rise to the top of the global policy agenda. When it does, policymakers, their advisers, and analysts should remember the lessons of the 1980s.

Figure 1 -- Growth of Real GDP:1980-1994 (PPP weights, percent)



Source: IMF, *World Economic Outlook Database*, April 2020, and calculations by author.

Figure 2 --US Bank Exposures to 17 Heavily Indebted Countries



Source: Author's calculations based on Cline (1995) tables 2.10 and 2.11

Table 1 -- Programs and debts of 17 heavily indebted countries

COUNTRY	First IMF program	Gross external debt (USD billions) 1982	1985	1989	1993	International bank claims (USD billions) 1982	1985	1989	1993	Brady Bonds Issued
Argentina	1983	43.6	50.9	65.3	74.5	22.2	29.0	32.4	30.4	1990
Bolivia	1986	3.3	4.8	4.1	4.2	0.7	0.6	0.3	0.4	&
Brazil	1983	93.0	106.1	111.4	132.7	56.1	76.9	70.8	69.0	1994
Chile	1983	17.3	20.4	18.0	20.6	10.4	14.3	9.1	10.0	none
Colombia	1985 *	10.3	14.2	16.9	17.2	5.5	6.5	6.6	7.6	none
Costa Rica	1982	3.6	4.4	4.6	3.9	0.7	0.8	1.1	1.2	1990
Cote d'Ivoire	1981	8.9	9.6	14.1	19.1	2.9	2.9	3.3	2.2	1998
Ecuador	1983	7.7	8.7	11.3	14.1	4.1	5.2	4.6	3.2	1995
Jamaica	1981	2.8	4.1	4.6	4.3	0.5	0.7	0.7	0.5	none
Mexico	1983	86.1	96.9	93.8	118.0	59.03	74.5	70.1	69.0	1990
Morocco	1982 **	12.5	16.5	21.6	21.4	3.6	4.8	5.2	5.0	none &&
Nigeria	1987	13.0	19.6	32	32.5	7.0	9.1	7.4	4.1	1992
Peru	1982 **	10.7	12.9	18.6	20.3	5.2	5.6	4.1	3.2	1997
Philippines	1983	24.4	26.6	28.7	35.3	8.3	13.4	9.6	6.6	1992
Uruguay	1985	2.6	3.9	5.2	7.3	1.2	2.0	2.0	2.7	1991
Venezuela	1989	32.2	35.3	32.4	37.5	22.7	25.8	24.1	17.4	1991
Yugoslavia	1981	19.9	22.5	19.1	11.3 ^	9.3	10.5	7.5	3.9	none
Total	n.a.	392.1	457.3	501.7	574.3	219.4	282.6	259.1	236.3	n.a.

* Did not have an IMF program. Program with the World Bank was monitored in part by the IMF.

** Programs approved before the Mexican weekend.

^ Excludes Croatia, Macedonia, and Slovenia.

& Had a debt buyback in 1988.

&& Negotiated a Brady arrangement but did not meet the conditions for issuance.
Sources: International Monetary Fund, *Transactions with the Fund*, country pages, Boughton (2012, 414-415), Cline (1995, Tables 2.1 and 2.8), and Das et al. (2012).

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