

Argentina's quest for the moral high ground in its recent restructuring

Steven Kargman
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Steve Kargman

In the first of a four-part feature, **Steven Kargman**, founder and president of the eponymous New York-based international restructuring advisory firm Kargman Associates, examines Argentina's strategy in its recent debt negotiations with foreign bondholders. Kargman concludes that in order to claim the moral high ground in the restructuring, Argentina relied on "the three P's": the pandemic, the professoriate, and the Pope.

As a serial debt defaulter with its record ninth default in late May of this year, Argentina has obviously not been a stranger to sovereign debt restructurings. The restructuring deal that Argentina reached in principle with its foreign

bondholders in early August with respect to US\$64 billion of its foreign law debt was only the latest in a long line of Argentine restructurings over many years. But unlike some of Argentina's earlier restructurings, the most recent restructuring deal was overwhelmingly accepted by Argentina's bondholders in the recently completed bond exchange, according to the results announced by Argentina at the end of August.

Prior to this latest episode, Argentina's most recent sovereign debt restructurings in 2005 and 2010, arising from its US\$100 billion debt default in 2001, were not a distant memory at all for the participants in the most recent restructuring. After all, it was only in 2016 that Argentina finally reached a settlement with a small but determined group of holdout creditors from those earlier restructurings.

Indeed, those earlier experiences growing out of the 2001 default, where both Argentina and its holdout creditors in particular came in for some sharp criticism for the way in which they handled the restructuring process and the related ensuing litigation, was characterised by no small degree of acrimony. Those experiences were probably seared not only into the memories of many of the participants in those restructurings but also into the memories of other players involved in the business of trading and investing in emerging market debt generally.

Yet, as Argentina wended its way through the recently concluded negotiation process for its latest sovereign debt restructuring, it seemed to be taking a different tack than it has taken in its restructurings of the recent past. Specifically, Argentina appeared to have made a concerted effort to claim the moral high ground vis-à-vis its creditors.

In other words, Argentina seemed to want to fight the debt restructuring not just at the negotiating table, bargaining with creditors over the relatively dry, fairly technical financial and economic considerations and modeling that inevitably are central to the development of any sovereign debt restructuring plan. Rather, it seemed to be intent on influencing the overall atmospherics surrounding the debt restructuring discussions with the apparent aim of putting itself in a better position to achieve its overall objective of what it would consider

a fair and just restructuring outcome under the circumstances then facing the country.

Argentina seemed to be interested in not simply achieving a restructuring that could essentially only be justified on narrow economic or financial grounds. Instead, it appeared that Argentina wanted to influence interested parties in the debt restructuring to understand Argentina's overall objectives, and, to the extent possible, to convince those parties to be at least somewhat more sympathetic (or perhaps even just less hostile) to Argentina's perspective.

To put it mildly, in its sovereign debt restructurings in 2005 and 2010 and in the subsequent litigation that stretched on for many years thereafter until a settlement was reached in early 2016, Argentina generally did not necessarily come across as the most sympathetic party. Argentina certainly did not engender much goodwill from market participants, particularly in the latter part of this process under the leadership of its then-President Cristina Fernández de Kirchner. But by the same token, some of the holdout creditors, especially those US-based hedge funds that waged a long-running and very contentious battle against Argentina in the US courts, did not necessarily appear as the most sympathetic parties to many observers either.

In the just-concluded restructuring negotiations between the foreign bondholders and Argentina, the target audience for Argentina's messaging would appear to have included a broad range of parties – including large institutional investors in Argentine debt (i.e., parties involved in the restructuring itself), national governments (such as those in the G-7 and G-20 groupings), multilateral institutions (e.g., the International Monetary Fund (IMF), the World Bank, etc.), and non-governmental organisations.

In such a high-profile sovereign debt restructuring, it is not clear, for example, that major financial institutions including leading asset management firms holding billion dollars of Argentine debt—and there were a number of such institutions in the recent restructuring—would have wanted to be completely heedless of public opinion. This would have been especially true for institutions that wished to maintain some credibility on broad public policy issues (whether on matters related to environmental, social, and governance (ESG) investment

criteria or otherwise) and to position themselves as leaders in the financial world on such issues.

By way of example, in early May not long after Argentina had formally presented its first debt restructuring proposal, at a point that was relatively early in the course of the restructuring discussions, one such player, the world's largest asset management firm BlackRock, which held several billion dollars of Argentine debt, reportedly urged its fellow creditors to accept greater losses as part of an effort to reach a deal with Argentina. But later as the negotiations reached a stalemate in the latter part of July, Blackstone's CEO, Larry Fink, basically told Argentina that it was time to sign up to a deal that the creditors had recently put on the table.

Then, finally, a few days later when BlackRock had reportedly reached an agreement with Argentina on the final terms of a restructuring deal that was acceptable to both BlackRock and Argentina, BlackRock apparently called around to its fellow major creditors urging them to join BlackRock in agreeing to the new deal, according to recent news reports in the *Financial Times* and *Bloomberg* among others.

Argentina's strategy

As will be discussed more fully below, in its effort to claim the moral high ground in the recent restructuring, the Argentine government, under its new president Alberto Fernández, essentially relied on the *three P's*: the pandemic, the professoriate, and the Pope.

First, the arrival of the covid-19 pandemic in Argentina allowed the country to shift the narrative of the debt restructuring negotiations from discussions of simply financial and economic matters to a broader discussion that included an emphasis on the urgent need for the Argentine government to protect its people from the spread of the then newly arrived coronavirus. In effect, the idea propounded by Argentina and its supporters was in essence that Argentina should not be forced by the terms of any debt restructuring deal to divert resources for debt service that could otherwise be used on behalf of the Argentine people for critically needed public health efforts directed against the coronavirus.

Second, the professoriate gave Argentina's negotiation position a stamp of approval from heavyweights in the field of economics and other academic disciplines from many countries around the world, a group that featured some Nobel laureates in economics. Argentina on its own could have argued all it wanted that its negotiating position was reasonable. However, having a veritable small army of leading professors of economics and other disciplines on board with its position was designed to give Argentina's views greater legitimacy and respectability with its creditors and possibly even with the international financial community more generally.

Finally, in its effort to achieve a fair and reasonable restructuring, Argentina sought to benefit, to the extent possible, from the moral authority and stature of the Pope. Obviously, the Pope was completely removed from and was not involved at all in the actual debt restructuring negotiations themselves. Yet, significantly, the Pope met with President Fernández at the Vatican in late January, and then just a few days later in early February the Pope participated in a conference at the Vatican (in which Argentina's Economy Minister also participated). At that conference, the Pope made some pronouncements on issues of debt and development that could be seen as being broadly sympathetic to the situation facing sovereign debtors such as Argentina.

At a minimum, those interactions by the Argentine government with the Pope and the Vatican could not have hurt Argentina in the court of public opinion or even perhaps in the corridors of power around the world. Perhaps, given the unique global standing of the Pope, such interactions even strengthened Argentina's hand and its standing in the eyes of parties such as national governments and international institutions, not to mention private financial institutions, that were following those interactions.

Impact of Argentina's strategy

It should be noted that this four-part feature does not specifically argue that there was necessarily a direct cause-and-effect relationship between the three P's and the precise terms eventually agreed upon in the restructuring negotiations. Rather, it posits that, seen from a broader perspective, the three P's could have been factors that, to one degree or another, helped influence the overall tenor and trajectory of the restructuring negotiations generally. As a

result, Argentina perhaps achieved a better overall outcome in the negotiations and perhaps sooner than it would have otherwise absent the three P's.

In this regard, the pandemic may have been the most influential of the three factors, especially in underlining for the creditors (as well as for other interested parties) the urgency of the situation facing Argentina. Yet, as will be discussed below, the other two factors – the professoriate and the Pope – may have also played important supporting roles in their own ways.

As a practical matter, one might argue from a certain vantage point that the negotiating process may have ended up roughly where it did without regard to the three P's. After all, as Argentina and the foreign bondholders headed into what eventually turned out to be the final stage of the negotiations, they were not that far apart in terms of the recovery values for the creditors that they could accept (although at the outset of the process they were obviously much farther apart). Apparently, Argentina said that it could not contemplate permitting a recovery of more than 53.5 cents on the dollar, whereas the creditors indicated they could not accept a recovery of less than 56.5 cents on the dollar. Thus, the final deal which gave creditors a recovery of roughly 55 cents on the dollar was exactly halfway between the respective final negotiating positions of Argentina and the creditors. (Of course, putative creditor recovery values are only one basis for evaluating a restructuring plan; there are many other dimensions to restructuring plans that are important to both creditors and sovereigns.)

Nonetheless, this final result was ultimately achieved only after many twists and turns in the negotiating process, with certainly no guarantee of success as the negotiations proceeded. Argentina and the creditors exchanged a series of competing proposals and counter-proposals over a period of several months, there were a number of extensions in negotiating deadlines since no deal had been reached by those deadlines, and the talks came close to veering off track or even collapsing at certain points over the course of the negotiations.

As the negotiations dragged on into early August (as an 4 August deadline was rapidly approaching), Argentina's overall strategy, particularly the pandemic prong of its strategy, may have ultimately affected the willingness of the creditors to prolong the negotiations to achieve even more favourable terms for

themselves (assuming that Argentina was even willing to continue to engage in continued negotiations with the creditors, which was not at all entirely evident). The creditors might well have risked incurring a serious backlash in terms of public opinion if they continued to hold out for better terms, especially since only a few cents in recovery value separated the recovery values indicated by the creditors' restructuring plan and that indicated by Argentina's restructuring plan.

If the creditors had persevered further, they might have been seen in some quarters in an unfavourable light for prioritising a maximisation of their recoveries, literally at the expense of the health and general well-being of the Argentinean people who were then grappling with both the public health crisis created by the pandemic as well as a major economic downturn. As political analyst Nicolás Saldías was quoted as saying in the *Wall Street Journal* after the restructuring deal had been struck in early August: "For the creditors, it would look bad if you are asking in the middle of the worst economic recession since the Great Depression and a pandemic which is killing hundreds of people ... in the country for an exorbitant amount of money."

Moreover, while Argentina of course had to make some concessions in order to reach agreement with the creditors on a final set of terms, broadly speaking it was able to accomplish some (but certainly not all) of its main objectives that were laid out early in the restructuring process. Importantly from Argentina's perspective, it was able to achieve roughly the amount of cash flow relief that it had sought from its initial proposal in April: approximately US\$37.9 billion over the 10-year period from 2020-2030. One of the major ways that Argentina was able to achieve this result was through a significant lowering of average interest rates from roughly 7% in the old bonds to roughly 3% for the new bonds incorporating the restructuring terms.

At the same time, as part of the compromises that led to the final deal, Argentina was able to increase the recovery rate for creditors allowing them to sign on to the deal, and yet it was able to maintain the amount of cash flow savings the sovereign would achieve in the restructuring. In the final negotiations in early August, Argentina agreed to move forward certain interest and principal payment dates (with semi-annual payments payable on 9 January of each year instead of 4 March, and on 9 July of each year instead of 4 September) as a

means of increasing the recovery value for creditors (by virtue simply of the concept of the time value of money). However, this compromise helped “boost creditors’ recovery value without changing the aggregate amount [Argentina] pays out,” as noted in the *Financial Times*.

Another key objective from the outset of the negotiations was to obtain a several-year grace period in debt service payments in light of the very uncertain prospects for Argentina’s economy over the next few years. As part of this goal, Argentina had originally sought a three-year grace period for interest payments, but in the final deal it did not achieve any grace period at all for interest payments.

Yet, Argentina’s original ask for a three-year grace period may have served a useful function as a bargaining chip, whether by design or not, since it had three years of grace period it could ultimately give away in the negotiations. Argentina was in effect able to give up one additional year of grace period at certain key points in the negotiations, presumably to move the negotiations forward and/or get some concessions from the creditors in return.

On the other hand, Argentina did achieve multi-year grace periods on its amortisation payments on the new bonds, and as a result and importantly for Argentina, it will not have to make any principal payments for the next several years. For example, Argentina will have a grace period on amortisation payments of just under four years in the case of one set of new bonds, namely, the so-called New 2030 USD/Euro bonds, and a grace period on amortisation payments of just under seven years in the case of another set of the new bonds, namely the so-called New 2038 USD/Euro bonds.

In the next instalment, Kargman will look more closely at two of the “P’s” that he says Argentina relied on during its negotiations: the pandemic and the Pope.

Argentina's quest for the moral high ground: challenges during a pandemic

Steven Kargman
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Credit: shutterstock/1662121993

In the second instalment of his four-part feature, **Steven Kargman** of Kargman Associates begins his exploration of the “three P’s” relied on by Argentina during its recent restructuring negotiations, focusing on the roles played by the covid-19 pandemic and the Pope.

The pandemic

Argentina had begun work on developing the outline of a restructuring proposal even before the arrival of covid-19 in the country (the first case in Argentina was

reported in early March). But it seems fairly clear that, whether directly or indirectly, the Argentine government in effect sought to use the arrival of the pandemic to its advantage in the recently concluded debt restructuring negotiations.

Obviously, the pandemic was a most unwelcome and unfortunate public health and economic development in Argentina. The country was already facing immense social and economic challenges, including, among other things, very high poverty rates and a serious recession that had already lasted at least two years.

As in other countries around the world, the pandemic in the short term has posed twin strains on Argentina's balance sheet. On the one hand, it has forced sovereigns to make unanticipated public health expenditures to support the broad array of public health responses to the coronavirus, from testing to personal protective equipment (PPE) to medicines to contact tracing and so forth.

On the other hand, the pandemic has forced sovereigns to fund economic stabilisation or recovery programs (whether targeted at businesses or individuals), especially to offset the effects of lockdowns of national economies – including, in particular, any resulting economic slowdowns. (Separately, an economic slowdown such as that induced by the pandemic means that national economies will ultimately generate a lower level of tax revenues for their respective national governments, thereby putting additional stress on the balance sheet of sovereigns. A similar dynamic will also likely play out around the world for local governments, whether states, provinces, or municipalities.)

By many accounts, the Argentine government at least initially handled the coronavirus outbreak fairly well. Within a few weeks of the first case of covid-19 in Argentina – a point at which Argentina was reported to have had approximately only 150 cases – the Argentine government on 20 March imposed a shutdown of all non-essential economic activity.

Thus, the Argentine government was seen as moving fairly quickly and decisively to address the pandemic. In fact, as noted by the World Health Organization (WHO) in late July: “At the start of the pandemic, Argentina stood out in the region for its no-nonsense, quick response to the virus.”

The Argentine government certainly appeared to have handled the outbreak of covid-19 with greater competence and efficacy than its much larger neighbor, Brazil, where the coronavirus seemed to spin out of control and led Brazil to having the second highest death toll worldwide (behind only the US). Furthermore, at least in the first few months after the pandemic arrived in Argentina, it also appeared to have performed better in controlling the coronavirus than its neighbours Chile and Peru.

However, even though Argentina received plaudits for its initial handling of the outbreak, there have been some worrisome outbreaks of covid-19 and a spike in cases in Argentina in the last few months, and this has been a major cause for concern on the part of the Argentine government.

Since late May or so, there have been outbreaks largely in the capital, Buenos Aires, particularly in its crowded slums, as well as in the broader area of the province of Buenos Aires, but unfortunately the greater Buenos Aires metropolitan area (with approximately thirteen million residents) is where nearly 29% of the Argentine population is concentrated. As a result of those continuing outbreaks, the Argentine government delayed the scheduled lifting of its lockdown a few times, and, most recently, the government extended a lockdown in Argentina's most densely populated areas until the end of August.

As of 26 August, Argentina was reported to have approximately 360,000 coronavirus cases and had suffered approximately 7,700 deaths from the coronavirus, but just a few days later as of 31 August, there were reported to approximately 408,426 cases and 8,457 deaths. On a per capita basis in light of Argentina's population of approximately 45.2 million people, Argentina's overall figures for covid-19 cases and deaths may seem relatively low. However, as of late August the pandemic in Argentina, as measured by the number of cases and deaths on a daily basis, remained on an unmistakable upward trajectory and indeed a fairly sharp upward trajectory at that.

Unfortunately, it appears that Argentina has not yet achieved anything approaching a so-called "flattening of the curve." It is the sharp upward trajectory in cases and deaths which must be very troubling for the Argentine government as it considers the impact of the pandemic on Argentina's citizens.

Nevertheless, in terms of the debt restructuring process itself that was already underway when the coronavirus arrived in Argentina in early March, Argentina essentially sought to use the pandemic as a basis for justifying its position in seeking more generous debt relief from its creditors. The underlying idea was that, without such generous debt relief, Argentina would not have the necessary resources to stave off the worst effects of the pandemic, both from a public health and economic standpoint. Instead, Argentina would have to devote those much-needed resources to making debt service payments on its outstanding debt.

The economic rationale for this position was clearly articulated by economist Mark Weisbrot in a New York Times op-ed in mid-May in which he stated that “[i]f governments are forced to use scarce foreign currency to make unsustainable debt payments, they will not be able to afford the health care, testing, medical equipment, and even ‘social distancing’ measures to contain the coronavirus pandemic.”

Professor Joseph Stiglitz of Columbia University, who acted as a very strong and leading supporter of Argentina’s position in the recent debt restructuring negotiations, was quoted expressing a similar thought but in even starker terms. According to a BBC article from early May, Stiglitz was reported to have stated quite bluntly that Argentina “wants to pay what they owe to the extent they are able to pay but you can’t ask people to die to pay creditors....”.

It is worth noting that, in some of the commentary following the recently concluded restructuring deal for Argentina, the issue of the pandemic has moved to centre stage in the broader ongoing discussions of the economic and financial prospects for the emerging markets generally. For example, a Wall Street Journal article on 4 August carried the headline “Argentina Debt Deal Illustrates Coronavirus Pandemic’s Blow to Emerging Markets.”

The Pope

To the extent possible, the Argentine government appears to have sought to benefit from some of the moral authority of the Pope and his teachings, particularly as they relate to matters of debt, development, and globalisation. By attempting to associate itself with the Pope who over time has made various

socially-oriented pronouncements on such matters, Argentina at least implicitly sought to buttress its case that, as a general matter, the recent Argentine sovereign debt restructuring negotiations needed to take account of the social and human needs of the Argentine people.

Argentina did not seek to draw the Pope into the nitty-gritty details of debt restructuring negotiations between Argentina and its creditors but rather into the overall sovereign debt restructuring debate at a very high, indeed almost a symbolic, level. Argentina tried to accomplish this by having President Fernández meet with the Pope at the Vatican in late January and having its Minister of the Economy Guzman participate at the Vatican in a conference in early February on the theme of “economic solidarity”, where the Pope was a principal speaker.

The apparent aim on the part of Argentina was to benefit from the moral authority of the papacy in general and this Pope in particular. That was especially the case in light of Pope Francis’s oft-expressed concerns for social justice and the plight of the downtrodden as well as his concerns about the impact of unbridled capitalism, particularly its impact on developing countries and the populations of those countries.

Just when Argentina has been undergoing one of the most high-profile restructurings of the last few years, the people of Argentina have been fortunate to have a compatriot, Pope Francis, in the Vatican. As has been pointed out by several observers, Pope Francis had previously seen Argentina try to grapple with a debt default, a sovereign debt crisis, and the accompanying economic crisis.

Specifically, from 1998 through the time of his appointment as Pope in 2013 (the first Pope ever from Latin America), Pope Francis served as archbishop of Buenos Aires and was named a cardinal in 2001. In that role, he had a front-row seat to Argentina’s last major episode of a debt default and economic crisis in 2001 and in the subsequent years, and he no doubt witnessed first-hand the human suffering that was so pervasive in Argentina at the time.

When Argentina’s relatively new president, Alberto Fernández, embarked on a European tour earlier this year, he made the Vatican the first stop of his trip on

31 January. Fernández met with the Pope and apparently discussed Argentina's debt situation, a problem that Fernández had inherited from his immediate predecessor, Mauricio Macri. As related by Fernández following the meeting, the Pope "had promised him...to do everything that he could to help with his homeland's debt crisis," according to an article in Reuters.

The Vatican released a much more neutral statement indicating simply that the Pope and Fernández had discussed a range of issues, including, among others, "...the overall situation of [Argentina], with particular reference to the economic-financial crisis, the fight against poverty, corruption....," according to the Vatican News.

Regardless of whether the Pope in fact promised Fernández anything in their meeting as Fernández asserted (a matter as to which the Vatican's statement was notably silent), the mere image of the Argentine-born Pope warmly greeting the new President of Argentina made for a good photo opportunity for Fernández. The meeting and photo opportunity probably did not hurt Fernández from a political standpoint either, domestically or on the international stage. At the very least, the meeting and the apparent goodwill flowing from it seemed to represent a fairly sharp contrast with the reportedly frosty relations that existed between Pope Francis and the previous Peronist president of Argentina, Cristina Fernández de Kirchner.

Concretely, though, the meeting with the Pope came at a particularly opportune time for President Fernández since he was about to embark on a tour of European capitals during which he was expected to discuss Argentina's debt problems with European leaders, and he was therefore in a position leave the Vatican with a head of steam behind him. As stated by Marcelo J. Garcia in a New York Times op-ed in late January: "...Argentina's debt recidivism can *use the moral patina of [Pope] Francis' progressive economic language....*" (emphasis added).

Moreover, the fact that the Vatican's official statement on the meeting did refer to the meeting's discussion of "the economic-financial crisis" (plus, in virtually the same breath, "the fight against poverty") confirmed, perhaps not surprisingly, that the Pope was acutely aware of the serious travails facing his home country. Furthermore, the Pope's recognition of the "economic-financial

crisis” existing in Argentina set the stage in a way for what followed shortly thereafter—namely, a broader discussion of global debt issues at a then-upcoming Vatican conference.

On 5 February, just five days after the meeting between the Pope and Fernández, the Vatican, under the auspices of its Pontifical Academy of Social Sciences, hosted a conference on global debt and development issues centered on the specific theme of “economic solidarity.” The Pope himself participated in that conference as did the new managing director of the IMF, Kristalina Georgieva. Finance ministers from throughout Latin America, Argentina’s Economy Minister, Martin Guzman, and various economists such as Professor Joseph Stiglitz of Columbia University also participated in the conference.

During that conference, the Pope spoke to the assembled audience and stressed the need for a “new form of solidarity” to help indebted countries, saying “we are not doomed to universal inequality,” as reported by Reuters. The Pope said specifically that “[p]oor people in heavily indebted countries bear overwhelming tax burdens and cuts in social services as *their governments pay debts contracted insensitively and unsustainably...*” The Pope added that a country’s debt policy “*can become a factor that damages the social fabric,*” according to Reuters (emphasis added).

The Pope’s words must have especially resonated with the Argentine government. The Pope was describing in broad terms exactly the type of predicament that Argentina was then facing, namely addressing sovereign debt issues while at the same time confronting fairly bleak socio-economic conditions, particularly as reflected in its very high poverty rate.

Even before the conference at the Vatican in February got underway, Minister Guzman and IMF managing director Georgieva had the opportunity to hold a private meeting that reportedly lasted two-and-a-half hours. At the conference itself, Guzman said: “Fiscal austerity in situations of unsustainable debt doesn’t work. On the contrary, it’s self-defeating.” Guzman also told the conference that under no circumstances would Argentina, in the words of the Reuters report, “continue servicing debt that was unsustainable and that pushed the country deeper into recession.”

For her part, IMF managing director Georgieva stated at the conference that “[i]t is very important moment for Argentina to put in place policies that are going to stabilize the economy, lead to successful debt restructuring and *respond to the expectations of people that those who are most vulnerable not be left out*” (emphasis added).

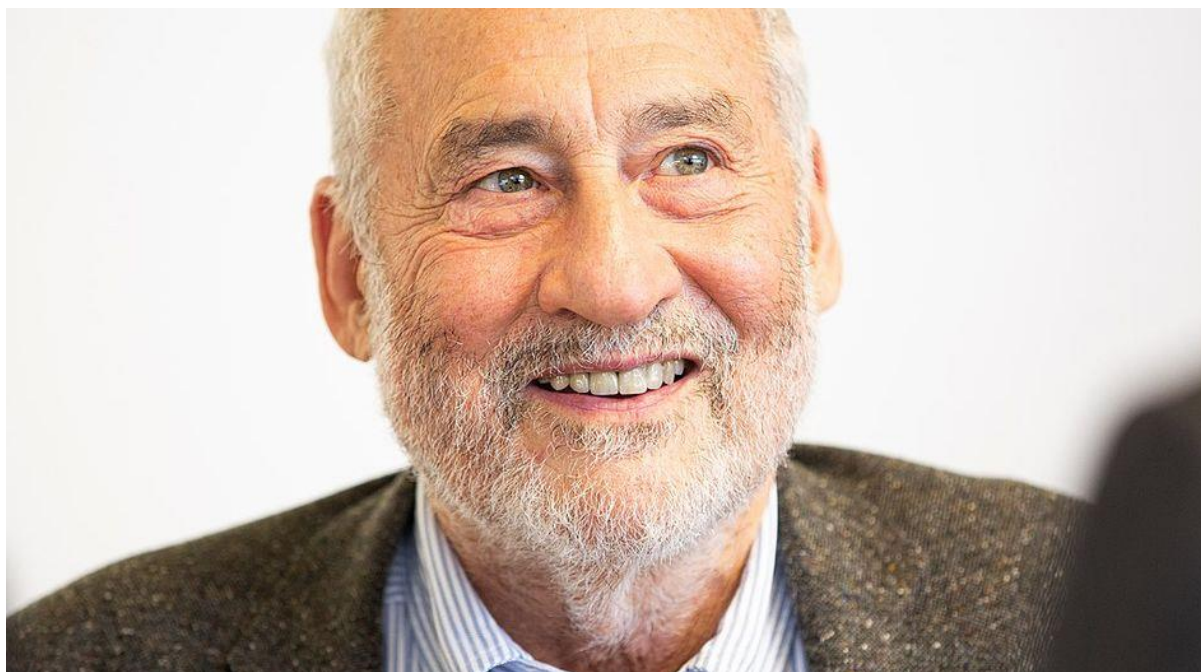
By way of update, when the Argentine government announced on 31 August that 93.4% of creditors voted for the government’s exchange offer, which had the effect of binding 99% of the outstanding old bonds, President Fernández singled out “Pope Francis, an Argentine, and the leaders of Mexico, Germany, France, Spain and Italy for their support during their negotiations,” according to a Financial Times article on 1 September. Thus, Fernández directly recognised the support provided by the Pope, as well as the support provided by leaders of various European countries, each of which was part of the itinerary for the European tour in early February following his visit to the Vatican and the meeting with the Pope.

Further, in singling out the president of Mexico, Andrés Manuel López Obrador, perhaps Fernández was recognising the role that López Obrador was reported to have played behind the scenes, according to articles in Reuters and Bloomberg. López Obrador apparently served as an intermediary behind the Argentine government and reportedly lobbied BlackRock CEO Larry Fink to support Argentina’s debt restructuring proposal on the table at the time.

In the next instalment, Kargman will look at how leading academics from the third ‘P’ – “the professoriate” – influenced the debt negotiations, with particular regard to their views on debt sustainability matters in Argentina’s proposals, as well as the type of collective action clauses that should have been included in the underlying bond documents for the restructuring.

Argentina's quest for the moral high ground: the professoriate weighs in

Steven Kargman
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Joseph Stiglitz, Ecole Polytechnique (Credit: WikimediaCommons/JeremyBarande)

In the third part of his feature examining Argentina's "quest for the moral high ground" in its recent restructuring negotiations, **Steven Kargman** of Kargman Associates looks at the role played by some of the world's leading academics and Argentina's position on debt sustainability and collective action clauses.

A number of leading lights from the professoriate, especially from the economics field, mobilised to provide an imprimatur from academia for some of the broad positions that Argentina was taking in its restructuring negotiations, particularly as to the overall reasonableness of the positions taken. These

academics co-signed a few open letters voicing strong and essentially unequivocal support for the overall Argentine negotiating position.

The first open letter from the professors was released in early May and was co-signed by 138 professors from approximately 20 countries around the world. The roster of professors signing the letter included, among many luminaries, at least two Nobel laureates in economics, Professors Joseph Stiglitz and Edmund Phelps (both of Columbia University). It also included other well-known academics such as Thomas Piketty, Carmen Reinhardt (a sovereign debt expert at the Harvard Kennedy School who shortly thereafter was appointed chief economist at the World Bank), Jeffrey Sachs of Columbia, and Dani Rodrik of the Harvard Kennedy School, among many others.

In the first open letter, the professors opined on the overall reasonableness of the restructuring plan proposed by Argentina on the basis of their assessment of Argentina's debt repayment capacity. As the letter stated: "Argentina has presented its private creditors a responsible offer that adequately reflects the country's repayment capacity: a three-year grace period with a minor cut in capital and a significant cut in interest."

To support their position, the professors invoked the IMF's earlier staff analysis in March on the debt sustainability of Argentina's outstanding debt burden. As IMF managing director Kristalina Georgieva stated, summarising the staff analysis: "In particular, staff's analysis shows that considering this debt-carrying capacity, and the existing debt burden, a *substantial debt relief from Argentina's private creditors* will be needed to restore debt sustainability with high probability" (emphasis added).

Furthermore, the open letter framed the recent Argentine restructuring as a test case for the international financial system in its ability to face up to the economic fallout from the pandemic for sovereigns. The letter stated: "At this exceptional moment, Argentina's proposal also presents an opportunity for the international financial community to show that it can resolve a sovereign-debt crisis in an orderly, efficient and sustainable manner."

It should be noted that it seems as if Professor Stiglitz was a prime, if not the prime, mover behind these open letters as he was the lead signatory. And that

is perhaps not surprising in light of his preeminence in the field of economics, including subjects related to development economics. Among his many public service-oriented activities apart from his teaching responsibilities at Columbia University, he has served as former chief economist at the World Bank and chairman of the Council of Economic Advisers under President Bill Clinton. He also served as chair of various commissions of experts appointed by the OECD and as president of the United Nations General Assembly, and he is widely considered to be one of the leading authorities on sovereign debt issues.

Martin Guzman, prior to becoming Argentina's minister of the economy in President Alberto Fernández' cabinet, was affiliated with Columbia University and worked very closely with Professor Stiglitz on articles, books and conferences on sovereign debt matters, including a co-edited volume entitled "Too Little, Too Late: The Quest to Resolve Sovereign Debt Crises". At that time, Guzman was a research associate at Columbia Business School and also served as a professor at the University of Buenos Aires, and before that Guzman had earned a PhD in economics at Brown University where his dissertation was entitled "The Causes and Effects of Financial Crises".

Whether or not they directly affected his posture in the negotiations, Guzman had well-developed views on the issue of debt sustainability from his academic career. In a paper analysing Argentina's 2001 default and subsequent restructurings, Guzman said that one of the lessons from that experience was that restoring debt sustainability in the debt restructurings was a prerequisite to restoring economic growth in the years following the restructurings. In other writings, he emphasised, for example, that it is not only economic considerations that bear on some of the key variables in a debt sustainability analysis, such as the notion of what constitutes a "feasible primary surplus". On this issue, he expressed the view that this concept involves the "definition of the *minimum government expenses that can be tolerated, an issue that goes beyond economic considerations, and that requires assessing what is essential for a society*" (emphasis added).

CACs

In early July, there was a second open letter from a group of approximately 75 prominent professors in support of Argentina's negotiating position, again

including some Nobel laureates and again with Professor Stiglitz as one of the lead signatories. In that letter, which was issued as the negotiations between Argentina and its creditors seemed to have reached a stalemate, the professors expressed their views on a technical, but very important matter related to the type of collective action clauses (CACs) that should be included in the underlying bond documents for the restructuring.

As their name suggests, CACs are designed to deal with the collective action problems that can arise in sovereign debt restructurings. Specifically, the problem is that a restructuring plan may be supported by the vast majority of creditors who believe it is in their best interest to agree to such a plan, but a small but determined group of holdouts may be able to thwart the will of the majority and prevent the restructuring plan from being approved and successfully implemented.

CACs address this collective action problem by permitting a supermajority of creditors to approve modifications to the payment-type and other specified key terms, technically known as “reserved matters”, that are the crux of a restructuring plan. CACs stand in contrast to so-called unanimous action clauses that require 100% approval of the creditors for modification of certain specified matters such as payment-related terms.

Indeed, that was the fate of Argentina’s restructurings growing out of the 2001 default where cumulatively over 90% of the creditors approved the 2005 and 2010 restructurings. However, a relatively small group of selected hedge funds held out against those restructurings and pursued fairly aggressive litigation against Argentina that lasted for many years until a settlement was eventually reached in early 2016.

In the second open letter, the professors firmly opposed the proposal by some creditors that the indenture for the new bonds being issued as part of the 2020 restructuring should be based on the indenture from the 2005 bonds. The 2005 indenture contained the same type of CAC that applied in Argentina’s 2005 and 2010 restructurings, for the purposes of governing how any future modifications could be made to the new bonds.

In Argentina's CACs issued under the 2005 indenture, an aggregate vote of 85% was required across all series of bonds, and a vote of 66.66% was required for each affected series in a series-by-series vote. There were thus two limbs to the approval process and the voting thresholds for each limb of the CAC had to be satisfied in order for the restructuring to be approved. This type of CAC is often referred to as a "dual-limb" CAC.

Those CACs under the 2005 indenture stood in contrast to the CACs that were included in the bonds from 2016 onward when Mauricio Macri was president of Argentina (hence their name as the so-called "Macri bonds"). As discussed further below, the CACs in the Macri bonds had, as one of the available voting options, a single-limb feature where the votes of a specified universe or pool of bonds of different series were aggregated and had to meet one specified threshold (ie, 75%) for the requested modification to the bonds to be approved, subject to a "uniformly applicable" requirement described below in connection with a discussion of the ICMA model CAC.

The professors homed in on one of the two limbs of Argentina's CAC under the 2005 indenture, namely the series-by-series voting feature. They said they believed series-by-series voting opened the door to holdouts blocking a restructuring, which was otherwise supported by a supermajority of creditors. Holdout creditors can accomplish this by acquiring a blocking position in a particular series of bonds, such as by amassing a 34% position in a series where, say, 66.66% approval for each series of bonds is required under the relevant CAC such as the CACs issued pursuant to Argentina's 2005 indenture.

In their second letter, the professors favored the "single-limb" aggregated CAC that was one of the voting options included in the 2016 indenture for the Macri bonds, where a 75% aggregated vote of the entire specified pool or universe of outstanding bonds of different series is required, subject to a "uniformly applicable" requirement discussed below.

The professors said they believed Argentina should use state-of-the-art CACs, specifically something known as "enhanced CACs". In particular, they endorsed the use of an enhanced CAC that was developed and promulgated by a private sector trade organisation, the International Capital Market Association (ICMA),

in 2014. That was the type of CAC included in Argentina's 2016 indenture applicable to the Macri bonds.

The enhanced CAC was developed in consultation with stakeholders from both the private sector and the public sector, including representatives from the US Treasury Department and the IMF. The ICMA model CAC essentially became the market standard for CACs as of 2014 and was endorsed by the G-20, and it will become the standard for eurozone-area sovereign bonds from 2022 onward.

In an ICMA-style enhanced CAC, as one of three options available to the sovereign, there is the possibility of a single vote of the entire aggregated pool of bonds for achieving approval of the proposed modifications to the bonds, ie, a "single-limb" vote. The ICMA-style CAC provides that a single 75% vote of the entire aggregated pool of bonds is required to approve the changes to the bonds. This single-limb voting mechanism, though, is subject to an important proviso that the proposed modification being voted upon is "uniformly applicable", a term of art in the ICMA model clause, which essentially means that all series of bonds have to be offered the same instrument or the ability to select from the same menu of new instruments.

(The ICMA-style CAC, as another one of the voting options available to the sovereign, also contains a dual-limb voting mechanism that requires the sovereign to obtain 66.66% of the entire specified universe or pool of bondholders, as well as 50% of the outstanding principal amount of each individual series of bonds.)

Addressing the creditors' preference for the dual-limb CAC provided for under the 2005 indenture, the professors stated: "The creditors' proposal is to replace enhanced CACs that prevent, or at least discourage ... opportunism with older arrangements that could lead to the vulture-fund predation that an increasing number of countries have faced in the last decade."

Essentially, the professors recognised that the enhanced ICMA-style CACs had become the market standard and effectively represented an important part of the international financial architecture for dealing with sovereign debt crises. In their view, a move back to the version of the dual-limb CAC in Argentina's 2005

indenture would have represented an unfortunate departure from that market standard.

Short of the existence of a global sovereign bankruptcy regime (which is a desired objective of Professor Stiglitz and certain other sovereign debt experts), the professors seemed to believe that a robust contractual framework for sovereign debt, with enhanced CACs at its heart, constitutes the best way to deal with the collective action/holdout problem arising in sovereign debt restructurings. They argued that the “move backward will exacerbate the collective-action problems in sovereign debt workouts ... and make pragmatic and viable solutions to sovereign insolvency much more elusive.”

Mark Sobel, who was instrumental in the development of the ICMA model CAC and who formerly served as the US executive director at the IMF and as an official at the US Treasury Department, similarly warned against reverting to the version of CACs issued under the 2005 indenture. “It would set a damaging precedent for other countries if Argentina were to accept the indenture requested by creditors,” he said according to *La Política Online*.

In the final restructuring deal that was agreed, neither Argentina nor certain creditors who had been pushing for use of the 2005 indenture achieved everything they wanted. On the one hand, Argentina and the creditors agreed that new bonds issued in exchange for bonds issued from 2016 onward (i.e., the Macri bonds) would provide for a CAC with the possibility of single-limb aggregated voting such as that provided in the 2016 indenture. On the other hand, it was agreed that new bonds issued in exchange for older bonds under the 2005 indenture (i.e., the bonds issued in Argentina’s 2005 and 2010 restructurings) would provide for a dual-limb CAC such as that provided in the 2005 indenture.

Redesignation and Pac-Man strategies

Nevertheless, after addressing the relative merits of the 2016 CAC versus the 2005 CAC, the professors implicitly seemed to wade into a separate, possibly more controversial aspect of Argentina’s negotiating position on CACs. They seemed to endorse the use of bold strategies known as the “redesignation” and

the “Pac-Man” strategies as a means of outflanking possible dissenting creditors in determining creditor votes under an ICMA-style CAC.

Under the “redesignation” strategy, the sovereign could decide after each series had already voted whether to expel a particular bond series from the voting pool. Under the “Pac-Man” strategy, the sovereign could use the single-limb voting procedure not just once but rather several times in successive votes to sweep up any remaining dissenting creditors (as long as the sovereign met the “uniformly applicable” requirement discussed above).

However, there were questions among creditors and certain observers whether the redesignation and Pac-Man strategies were consistent with the original intent behind the ICMA-style CAC. With respect to the redesignation issue, some observers thought that the model ICMA clause was supposed to give the sovereign only one chance, before votes were cast and not after they were cast, to designate which series of bonds should be included in the aggregated voting pool for purposes of determining whether the applicable voting thresholds had been met.

Similarly, with respect to the Pac-Man issue, some observers thought the single-limb voting mechanism in the ICMA-style CAC meant the sovereign was not supposed to be afforded the chance to have multiple, successive single-limb votes to mop up dissenting creditors.

Nevertheless, in their second open letter, the professors seemed to implicitly express their support for the redesignation and Pac-Man strategies. Although the professors did not directly refer to the strategies by name, they seemed to be referring to the possibility of Argentina employing them in the letter since it was published after the redesignation/Pac-Man controversy had already surfaced and become a flash point between Argentina and the creditors. The professors stated in their open letter that, “[n]ow that [the creditors] have discovered in practice the strength and flexibility of the new [ICMA-style] CAC, *they are upset that Argentina is using the clause deftly to preempt holdout behavior*, exercising against non-cooperative creditors its contractual rights to the fullest extent” (emphasis added).

In the final analysis, under the terms of the restructuring deal agreed upon by Argentina and the foreign bondholders and set forth in the exchange offer, the new bonds issued as part of the recently concluded exchange offer will permit the redesignation and the Pac-Man strategies. Importantly, however, those strategies will be subject to limitations in order to protect creditor interests.

In addition, the provisions in the new bonds permitting the redesignation and Pac-Man strategies will be considered “reserved matters” (which already encompassed payment-type provisions) requiring supermajority approval under the applicable CACs. The result is that the provisions in the new bonds related to these two strategies cannot at some future date be modified by a simple bare majority vote, as is the case for modifications of matters other than reserved matters, providing an important safeguard for the creditors.

It should be noted that in the recently concluded restructuring, Argentina originally triggered the whole redesignation/Pac-Man controversy when, as part of the 2020 restructuring exchange offer, it initially proposed to amend the 2016 indenture in order to permit redesignation. However, since Argentina argued that the proposed amendment permitting redesignation did not touch upon a “reserved matter” under the 2016 indenture, it asserted that the redesignation amendment could be approved by a mere bare majority of the outstanding principal of each series of bonds. In other words, Argentina claimed that a supermajority vote of each series of bonds would not be required for approval of the proposed amendment as would be the case if it had involved a reserved matter within the meaning of the 2016 indenture. The creditors objected strenuously to this because they believed that a change to important terms of the CAC, such as the proposed amendment to the indenture permitting redesignation, should not be capable of being approved by a mere bare majority vote.

In the final part of the feature, Kargman will examine what lies ahead for Argentina as it prepares for a fresh round of negotiations – this time with the IMF.

Argentina's quest for the moral high ground: the road ahead

Steven Kargman
17 September 2020



Cristina Fernández de Kirchner (Credit: Shutterstock.com/ymphotos)

In the final part of his feature examining Argentina's strategy in its recent debt negotiations with bondholders, **Steven Kargman** of Kargman Associates looks at what lies ahead for the country as it prepares for a fresh round of negotiations with the IMF. Kargman asks whether the country will be able to develop a sustainable economic strategy for the coming years, or whether it will continue to lurch from one economic (and sovereign debt) crisis to another.

Even with the restructuring deal that Argentina reached with its creditors and which has now been overwhelmingly approved by its foreign bondholders in the

recently completed exchange offer, Argentina still has a very tough row to hoe. Argentina's social indicators are fairly dismal, as the country has, for example, an overall poverty rate of approximately 35% and a youth poverty rate of over 50%, according to World Bank data.

Argentina's economic indicators are not much better. Importantly, as part of the overall slowing of the global economy associated with the coronavirus, the Argentine economy is expected to shrink by 9.9% in 2020, according to the IMF's World Economic Outlook from late June. This projected decline in Argentina's economic output is even greater than the average real GDP decline of 4.9% forecast by the IMF for the global economy as a whole, and a decline of 3% for emerging markets and developing countries.

Nonetheless, even though covid-19 has made a major dent in the Argentine growth rate, it should be remembered that Argentina has been in a recession for at least the last two years, well before the pandemic arrived. In 2018 and 2019, Argentina experienced GDP declines of 2.5% and 2.2% respectively.

Furthermore, Argentina has been suffering from very high inflation. In 2019, it recorded annual inflation of nearly 54%, its highest rate of inflation in nearly three decades. For 2020, Argentina is expected to have an annual inflation rate of approximately 40% or slightly higher, a very high rate of inflation for any normally functioning national economy.

Argentina has also suffered from high unemployment, with the unemployment rate reported at approximately 10.4% in the first quarter of 2020. The IMF has projected a 10.9% unemployment rate for 2020 as a whole.

Argentina's national currency, the Argentine peso, has also suffered a major depreciation vis-à-vis the US dollar. The Argentine government has put strict capital controls in place in an effort to stem further declines in the value of the peso. But the peso is currently trading for much less against the dollar on the black market than on the official market. This divergence between the black-market and official rates suggests that Argentine peso may potentially be due for a major depreciation against the US dollar in the not-too-distant future from the peso's already weak exchange rate against the US dollar.

Even before a restructuring deal was reached between Argentina and its foreign creditors in early August, there was skepticism in some quarters that the deal would prove to be unsustainable over time. As was noted in an [article](#) in *Euromoney* in late July, there was some concern at that time that, even if Argentina's position on the debt restructuring were to be adopted, it was not clear it would be able to meet its debt service obligations in the deal, given its uncertain prospects for economic growth in the next few years.

Of course, one of the overriding objectives of the recently concluded debt restructuring negotiations was to help put Argentina back on a more solid economic footing so that it can resume economic growth in the next few years. But the real question going forward is whether President Alberto Fernández' administration will be able to implement an economic plan that will provide Argentina with sustainable growth over the medium to longer term, in contrast to its very uneven economic performance in recent decades.

More specifically, a central question is: will Argentina be able to develop an overarching and sustainable economic strategy, or will it continue to lurch from one economic crisis to another (and, indeed, from one sovereign debt crisis to another) as it has done on a fairly regular basis in the last few decades? Among other key issues of economic policy, will Argentina be able to develop a strategy that focuses on developing or expanding sectors of its economy that will enjoy a comparative advantage in international trade and commerce, with the potential for generating much-needed foreign exchange, as well as a large number of jobs?

The challenge for the Argentine government in the coming period will be whether it can develop an overarching economic strategy that will provide for a solid and sustainable economic base for Argentina going forward. If no such broader overarching economic strategy is developed by the current (or any future) Argentine government, it would not be at all surprising if Argentina continues to have financial/economic crises and sovereign debt crises, as well as debt restructurings, on a recurring basis in the future – just as it has had on a fairly regular basis in the past.

With the foreign creditor debt negotiations now behind it, Argentina will shortly move on to negotiations with the IMF on what should be done with the IMF's

existing outstanding loan of US\$44 billion to Argentina, the total disbursed amount out of the IMF's original loan authorisation of US\$57 billion (when President Fernández came into office last December, he decided that Argentina would not avail itself of the remaining, undrawn disbursements of the original authorized loan).

In the recently-concluded restructuring negotiations with its foreign bondholders, Argentina benefited from technical analyses produced by the IMF on matters of debt sustainability that ended up proving helpful to its negotiating position vis-à-vis its foreign bondholders. For example, in March, IMF stated that Argentina's pre-restructuring debt burden was unsustainable and that "[r]estoring public debt sustainability with high probability will require a decisive debt operation, with a *meaningful contribution from private creditors*" (emphasis added). The IMF weighed in again on 1 June when it said that Argentina's revised debt restructuring proposal of 26 May would restore debt sustainability with "high probability", and that Argentina had "*only limited scope to increase payments to private creditors*" (emphasis added).

Of course, in the past, Argentina has had a relatively rocky relationship with the IMF, with many Argentineans blaming the IMF for some of its earlier economic and financial woes. In fact, as recently as early February, the former Peronist president (and current vice president) of Argentina, Cristina Fernández de Kirchner, was quoted as making comments that were antagonistic to the IMF. According to news reports of a visit she made to Cuba in early February, she reportedly stated that Argentina would not repay the IMF "one cent" while it is in a recession.

Perhaps even more provocatively, Vice President Kirchner was quoted as saying that the loan from the IMF to the Macri government was "illegal" because – as she apparently said according to news reports – it was used to support capital flight. Since she claimed the loan was illegal, she argued that Argentina should be entitled to a haircut.

Nonetheless, in the coming months, Argentina will now find itself across the negotiation table from the IMF, an institution that has, traditionally, firmly resisted taking haircuts on its loans to sovereigns. As a matter of policy, the IMF has relied on its "preferred creditor status", which effectively puts the IMF ahead

of other creditors in terms of a debtor's repayment obligations to private (or other official) creditors, so that the IMF can get repaid in full and therefore not suffer a haircut in any sovereign debt restructuring. Moreover, for Argentina, the IMF is truly its lender of last resort, as the IMF's role in the international financial architecture has been traditionally conceived.

If President Fernández follows the playbook that he relied upon for the negotiations with the foreign bondholders, he may try to keep Vice President Kirchner in the background in Argentina's upcoming negotiations with the IMF so as not to antagonise and potentially derail them. In the recently-completed negotiations with the foreign bondholders, President Fernández was the public face of the Argentine government (along with Minister Guzman), and Vice President Kirchner did not participate in the negotiations.

President Fernández may have calculated that Vice President Kirchner's presence in the negotiations with the foreign bondholders would not have moved them forwards, but backward or sideways at best. In the period when Kirchner was president (2007 to 2015), she had a fairly toxic relationship with the bondholders/holdouts and was generally viewed as anathema by foreign creditors and investors. In a Financial Times article on 5 August, Kirchner was characterised as "*the mercurial populist who had been branded a market pariah* by the end of her eight-year stint in power in 2015 due to frequent clashes with investors" (emphasis added).

President Fernández probably did not want to replicate that earlier experience in his recently-completed negotiations since he was eager to reach a deal. He may therefore attempt to pursue the same approach of keeping the vice president away from direct participation with the IMF.

Nonetheless, although she is currently serving as vice president and not in her former capacity as president, it is widely believed Kirchner continues to hold great sway in the government. For instance, it was reported that after a tentative deal was struck by Argentina and BlackRock in early August, Minister Guzman brought the tentative deal to Vice President Kirchner for her crucial and apparently indispensable approval, with some suggestions that she may have had de facto veto power, according to post-mortems of the deal in the Financial Times, Bloomberg, and elsewhere.

The precise parameters of any negotiations that will take place between Argentina and the IMF are not yet clear, particularly as Argentina has only in late August made a formal request to the IMF for a new funding arrangement and serious discussions have not yet started. Recently, though, there has been some speculation that Argentina might enter into a new standby arrangement (SBA) with the IMF to replace the SBA from 2018, or that it might enter into a longer-term arrangement with the IMF, such as a so-called extended fund facility (EFF), which typically comes with more conditions than an SBA. Only time will tell what exact form any new arrangement may take.

But one way or another, major adjustments will need to be made in the structure of the IMF's outstanding US\$44 billion loan to Argentina. For instance, under the loan as it currently stands, Argentina would be required to make major debt service payments from 2021 to 2023. Obviously, however, based on current expectations for the Argentine economy in the next few years, as well as the dwindling amount of Argentina's available foreign exchange reserves (reported to be presently under US\$40 billion), the country would not be in a position to make those upcoming payments, which are estimated to be approximately US\$23 billion in 2021 to 2022 and an additional US\$19 billion in 2023 alone. At a minimum, such payments would effectively need to be rescheduled for a later date in whatever form a new arrangement between the IMF and Argentina takes.

Since Argentina apparently does not have any major payments due to the IMF between now and 2021, there is no great urgency for them to come to a new agreement. In fact, Argentina has mentioned March 2021 as a possible target date for when it would hope to have completed a new arrangement.

If and when the IMF extends any new financing to Argentina and/or effectively reschedules, refinances or otherwise restructures the existing US\$44 billion loan, it may well impose new conditions on Argentina. Such conditions might include possible further belt-tightening or austerity measures (often referred to as "fiscal consolidation" measures) as part of an overall "adjustment" program and might also include possible "structural reforms" for its economy.

However, the IMF may create an opening for Argentina if it goes down the road of prescribing overly harsh austerity measures – or at least something that could

be portrayed as constituting overly harsh austerity measures. In such a situation, the sovereign might try to generate sympathy for itself – and thereby attempt to seize the moral high ground once again – by arguing that the proposed austerity measures go too far and impose too high a cost, particularly if the pandemic is still continuing to have a major deleterious impact on Argentina's society and its economy.

Under such circumstances, Argentina might find itself to be well-served by the prior academic views of Professor Joseph Stiglitz of Columbia University and Argentina's minister of the economy Guzman as reflected in some of their earlier writings and presentations on sovereign debt. In the past, Stiglitz and Guzman supported what might be considered an anti-austerity view of how sovereign debt restructurings should be handled, particularly when the economy in question is contracting or in recession. Specifically, they were highly critical of the approach that was taken, for example, in the Greek debt crisis.

They argued in essence that the fiscal austerity prescribed for Greece by the official sector – the so-called “troika” consisting of the European Commission, the European Central Bank, and the IMF – only served to exacerbate the economic contraction that Greece was facing at the outset of the crisis. The result, they argued, was that Greece ended up facing a much steeper and much more prolonged economic contraction than it originally faced, a contraction that in fact ultimately deepened into an economic depression. Stiglitz and Guzman believed on the contrary that the proper policy responses in such situations were pro-growth or expansionary fiscal policies.

Of course, whether or not it has a good substantive reason for taking a particular stance in any given negotiation, Argentina's uncanny ability in negotiations to get its creditors riled up – be they private creditors or public creditors such as the IMF – should not be underestimated. This ability was evident most recently in the redesignation/Pac-Man controversy in Argentina's just-concluded negotiations with its foreign bondholders, as well as in Argentina's earlier conduct in the restructuring/litigation process subsequent to Argentina's 2001 default.

But, so far at least, President Fernández has tried to keep Argentina's relationship with the IMF on a relatively even keel, and they appear to have had relatively smooth and business-like consultations over the past several months, despite the president stating in an interview in mid-August that, "I am not in a condition to accept any conditionality [from the IMF]. I am not in a condition because Argentina is not in a condition to," according to an article in the Buenos Aires Times. Whether President Fernández meant that statement to be taken at face value or whether, for example, it was primarily for domestic political consumption remains to be seen.

Nonetheless, an Argentine strategy of attempting to seize the moral high ground in its negotiations with the IMF could well prove to be a more difficult undertaking than it was with foreign bondholders. For instance, the IMF might argue that it is acting prudently in imposing conditionality on Argentina, including any austerity measures that it prescribes for the country. The IMF might well assert that such conditionality represents an appropriate means of protecting any financing that it extends to Argentina and is therefore designed to safeguard its overall resources as an institution, especially in its capacity as a lender of last resort for distressed sovereigns.

On the other hand, the origins of the outstanding loan to Argentina might put the IMF in a slightly awkward position. The loan was recommended by the then-IMF managing director, Christine Lagarde, now president of the European Central Bank, and was originally approved in June 2018 for approximately US\$50 billion, but was then increased to US\$57 billion in September 2018. It was the largest loan authorisation ever in the IMF's history (as well as being the 21st arrangement between the IMF and the Argentina since Argentina joined the IMF in 1956).

At the time of the loan, Argentina's economy was suffering from, among other things, a major currency crisis, including a run on Argentine the peso, and high inflation. The loan was widely seen as an effort to prop up or stabilise the Argentine economy under Argentina's former (non-Peronist) president, Mauricio Macri, who was pursuing a set of economic policies that were considered more market-friendly than those of his Peronist predecessors. The loan came with various conditions, such as a commitment by Argentina to a

zero deficit in 2019 and an agreement that Argentina's central bank would only intervene in currency markets in extreme circumstances.

Clearly, though, in the ensuing months and through the change from the Macri to the Fernández administration in December 2019 and even continuing to the present day, the Argentine economy has continued to weaken and it still faces major problems as discussed above. The IMF's implicit gamble with its record-setting loan that the Argentine economy would be able to straighten itself out, and that Argentina would be able to repay the IMF, did not pan out. But the fact that the Argentine economy did not turn around has now put the IMF's outstanding loan of US\$44 billion in jeopardy and at risk of default if action is not taken to effectively restructure, reschedule, and/or refinance it.

The IMF bet may have had some parallel in the bet that investors made in the Macri-era bonds issued post-2016, which was a bet that also went awry. As the professors stated in their first open letter discussed in part three of this feature: "Since 2016 when the country regained access to international markets, external creditors made a bet by acquiring debt with high coupons, but compatible only with extremely robust growth rates that did not materialize."

The one thing Argentina has going for it in the current situation is that the IMF loan was not approved under the current managing director, Kristalina Georgieva, but rather under her predecessor, Lagarde. That might give Georgieva slightly more wiggle room to be more understanding of the predicament facing Argentina and how the outstanding loan should be addressed. Further, in the eyes of the IMF Board, it may put more distance between any recommendations that may ultimately be made by Georgieva and the IMF's senior staff (particularly in the Western Hemisphere Department), on the one hand, and the circumstances surrounding the 2018 IMF loan, on the other hand.

After all, Georgieva was not responsible for recommending the approval of the ill-fated loan in the first place. She was therefore not the one who was instrumental in having the IMF making a bet effectively that, despite the major economic challenges Argentina was facing in 2018, the Argentine economy could turn around under the Macri government and that the-then peso crisis could be stemmed with the IMF loan.

Perhaps not surprisingly given the change in political parties from Macri to Fernández, the current Fernández government has been highly critical of the IMF's 2018 loan. In a recent letter to the IMF requesting a new program, Economy Minister Guzman and Central Bank Governor Miguel Pesce wrote: "We hope that the discussions and the new [IMF] program will not repeat what the Administration considers to be flawed assumptions of the 2018 Program."

Of course, as Georgieva is relatively new in her position as managing director of the IMF, having started on 1 October, it remains to be seen how exactly she will approach this matter. But given her participation in the early February conference at the Vatican, which was covered in part two of this series, and the ongoing discussions she and the IMF staff have had with the Argentine government over the past several months, Georgieva should be very familiar indeed with the current situation in Argentina.

Ultimately, the balance of power between Argentina and the IMF in any negotiations may depend on the predilections of the IMF's board of directors, its largest shareholders and its senior staff – and whether they believe it makes sense to take a tougher or a more accommodating posture.