



The Argentines blame the 'Washington Consensus' for the real default in 2001 and the New York judiciary and vulture funds for the artificial default this year. The arbitrary court order and the unethical extreme greed of the vulture funds are challenges not just to Argentina; they endanger the global debt restructuring system and contradict the domestic laws of United States. The U.S. President and the Congress can save Argentina from the pain and put an end to the extortionary tactics of vulture funds as a redemption for the original sins of the 'Washington Consensus'

Washington, New York and the Argentine default

'Argentina has defaulted', screamed the headlines in financial newspapers on 31 July. But it was not an accurate report. Argentina did not default. It was forced into default by a New York southern district court judge Thomas Griesa. The Argentine government had deposited the payment of 539 million dollars on 26 June ahead of the due date, in a bank in New York to be transferred to the 92.4% bond holders. But Judge Griesa had blocked the transfer of the money. He would not allow this payment to the 92.4% of the bond holders until and unless Argentina paid the outrageous amount demanded by the vulture funds which hold just 1.6% of the bonds. So it is an artificial default situation created by Judge Griesa. Joseph Stiglitz, the Nobel Laureate and Martin Guzman from Columbia University call the artificial default "Griesafault". Standard and Poor labels it as 'selective default' while Fitch has categorized it as 'restricted default'.

The Argentines are outraged, and are blaming the "Washington Consensus" for having caused the socioeconomic problems of Argentina not just now but since the eighties and nineties which eventually lead to Argentina's first default in this century in December 2001. Many say that the support of Washington DC to the Argentine military dictatorship (whose crimes include incurring unnecessary and irresponsible external debt) was the root of the country's chronic problem of default. Now they accuse also the New York judge of the same.

Facts of the case

After the December 2001 default on its debt of 81.8 billion dollars, the Argentine government restructured the debt through agreements in 2005 and 2010 with 92.4% of the bond holders under which the latter received 'exchange bonds' giving them about 30 cents for a dollar of the old bond. These exchange bond holders have been receiving their interest payments punctually and seen the value of their bonds rise. The remaining 7% of the bond (value 4 bn dollars) holders did not agree to the debt swap. Among these holdouts, the vulture funds hold 1.6% of the bonds worth 1.3 billion dollars. NML Capital, the lead vulture fund sued the Argentine government demanding full payment. Judge Griesa ruled in their favor in November 2012. Argentine appeal in a higher court was rejected and later the U.S. Supreme Court refused even to hear the Argentine appeal. Judge Griesa then forced the Argentine government to negotiate with the vulture funds under Daniel Pollack, a New York lawyer appointed by him as mediator. The negotiations failed since the Argentine government could not agree to the outlandish demand of the vulture funds and the latter rejected the Argentine offer of payment on the same terms as paid to 92.4% of the bond holders. The deadline of 30 July passed without the payment, resulting in a default situation, although the Argentina has the money and willingness to pay. Judge Griesa has simply put a gun on the head of Argentina saying, 'pay the predators or go bust'

Argentina has now taken the matter to the International Court of Justice, [complaining](#) that the decision of the U.S. judiciary is arbitrary, abusive and beyond its jurisdiction besides ignoring the sovereign immunity of Argentina and hindering the sovereign debt restructuring process. But this would not help if the United States does not consent to the jurisdiction of ICJ on this matter.

Five fundamental questions

While the wise old, 83-year-old judge and the greedy vulture funds have some sound technical and legal arguments, the case defies logic, common sense and natural justice. It threatens the sovereignty of Argentina and the global system and practice of debt restructuring besides contradicting the basic principles of free markets. It needs to be seen in a larger context with all the facts behind the case. To start with, let us ask five fundamental questions.

1. Did the Argentine government actually borrow money from the vulture funds which have sued Argentina? No. Neither the vulture funds lent any money nor did the Argentine government borrow from them. The vulture funds bought the bonds cheaply in the secondary market after the default in 2001. They paid 49 million dollars for bonds worth 832 million dollars. NML did not ask the Argentine government nor did it go through American judiciary before it purchased the bonds, knowing fully well the risk. Why should any judiciary be involved now to arrange profit on the commercial purchase? The judiciary should simply let the market forces play freely. They should ask the vulture funds to sell their bonds in the market from where they bought. This would be perfect justice in the land of free market.

2. Did Argentina refuse to pay the vulture funds? No. The Argentine government offered to pay them on the same terms as they paid the 92.4% of the bond holders. This would give a

handsome profit to the vulture funds on their investment. But they want an unreasonable and different treatment. They want an outrageous 1.63 billion dollars which means a return of 1608%. Some might consider this demand as immoral and unethical but it is business as usual for Paul Singer, the chief of NML and his other fellow vulture friends. They specialize in buying distress debt at rock-bottom prices and then try to collect ransom by litigation and blackmailing. Argentina is not their first victim. They have already exploited some African and Latin American countries and their last victim was Greece. Jerome Roos of the ROAR magazine calls the vulture funds the ['Taliban of global finance'](#).

3. Have the 92.4 % of bond holders lost out terribly after having accepted 30 cents to a dollar swap? No not at all. They are happy with the value of their exchange bonds which is around 89 cents to a dollar. Since these are GDP-indexed bonds, they have received good returns with the high growth of Argentina since 2003. The interest which they get is high since Argentina is only one of the three countries in the world offering bond yields above ten percent. More importantly Argentina makes interest payments punctually.

4. Will the vulture funds suffer loss due to the Argentine default? No. In fact they might even gain since they own a large quantity of credit default swaps (CDS) against Argentine bonds, creating a further incentive to not only trigger a default against Argentina; but also to undermine the value of the bonds themselves, as the CDS would pay out at a higher rate if the defaulted bonds decline to extremely low values.

5. Can the Argentine government pay the vulture funds the amount demanded by them? No self-respecting government can give in to such blatant blackmail. Moreover such payment will open a Pandora's Box and the 92.4% bond holders would also want a similar full payment pushing Argentina into another real default causing avoidable suffering for the Argentine people. Martin Wolf of Financial Times (24 June 2014) says, "If Argentina is forced to pay the holdouts in full, the price will be borne by Argentines. This is extortion backed by the U.S. judiciary". Asking Argentina to make full payment to the 1.6% bondholders while 92.4% have been paid one third of the full value is mockery of justice and undemocratic. Blocking the payment to 92.4% unless and until payment is made to 1.6% is punishment of the majority for appeasing a small minority?

Vulture funds harass Argentina

The vulture funds have been harassing the Argentine government for the last several years by threatening to seize Argentine assets and Central Bank reserves abroad. In October 2012, the vulture funds got a historic Argentine naval sailing vessel seized in Ghana through a local court order. Argentina took the case to the international tribunal for the law of the sea which asked Ghana to release the ship on the ground that the impounding of the ship was "a source of conflict that may endanger friendly relations among states". The incident was a terrible embarrassment for Argentina.

The vulture funds tried to confiscate Argentine assets including those of diplomatic missions in U.S., UK, Belgium, Germany, France and Switzerland. Argentina was forced to fight in the courts of these countries to protect its assets.

Even now the Argentine President does not travel in the official plane to U.S. or some other countries where there are risks of seizure of the aircraft by the vulture funds. The President charts planes for such trips.

The vulture funds are now trying to unearth dirt against the Argentine leaders in order to use them to blackmail as they did in the case of Congo. They have warned, ' the worst is yet to come'.

Argentina has done well on its own after the 2001 default

It should be highlighted here that Argentina had done the successful restructuring of its debt in 2005 and 2010 on its own without the involvement of IMF or any other external rescuer, demonstrating to the world that restructuring could be done without the painful and humiliating austerity conditions of IMF.

It is even more commendable that Argentina recovered from the debt crisis very quickly, resumed economic growth and paid off a significant amount of debt. It repaid its 9.5 billion dollars debt in full to the IMF in January 2006 at one go and has also settled many other external debts. It has brought down its public debt from 166% of GDP in 2002 to 44% in 2013. In May 2014 it signed an agreement with the Paris Club to settle the debt of 9.7 billion dollars. It has been servicing the restructured debt scrupulously paying interest to the exchange bond holders punctually. This has generated a confidence in the market because of which the price of Argentine bonds is holding at 89 cents to a dollar even after the default on 31 July.

Argentina achieved an impressive growth rate of 8.8% in 2003, a year after the debt crisis and economic collapse. It grew over 8.5% annually from 2004 to 2007. Even after the global financial crisis, the economy grew by 9.2% in 2010. No doubt, Argentina's recovery and growth were helped by the high commodity prices. Despite being cut off from the global credit market for over a decade, Argentina has done not so badly. In contrast, Greece which was bailed out with 110 billion Euros by Eurozone countries and IMF in 2010 is still in negative economic growth with high unemployment and continued suffering by the population due to the severe austerity conditions.

Argentina verdict contradicts U.S. domestic law

The American court verdict against Argentina contradicts the domestic law of U.S. which allows individuals and companies as well as cities and counties to declare bankruptcy under Chapter 11 and 9 to ensure orderly survival when debts cannot be repaid in full. The reasoning behind this American law is that no credit system can function or has ever functioned with zero

default. This possibility of default is embedded into credit contracts through the interest rate, with spreads operating as the market estimate of the probability of a default. So those who are seen as less likely to be able to repay are forced to pay higher interest rates, in both formal and informal credit transactions. A creditor who has been demanding and receiving a higher interest rate based on this probability cannot then demand full repayment as a right, since the contract reflected that very likelihood. [So the ruling actually negates the basic principles upon which all credit markets function](#). According to [Stiglitz and Guzman](#) "Griesa's ruling encourages usurious behavior, threatens the functioning of international financial markets, and defies a basic tenet of modern capitalism: insolvent debtors need a fresh start".

Implications for the world

Judge Griesa's decision favoring the vulture funds has provided a potentially dangerous precedent for future debt restructuring of other countries. It is because of this reason that even IMF and the World Bank have expressed concerns that the NML case could endanger the debt restructuring they oversee around the world. Brazil, France and Mexico filed amicus briefs with the U.S. Supreme Court in March this year arguing that the ruling against Argentina would endanger the sovereign debt markets. Argentina's position in the case has also been supported by Latin American regional groups such as Mercosur, UNASUR, CELAC and OAS besides G-77 and China.

Some U.S. bankers and economists have also cautioned about the adverse implications of Judge Griesa's decision for the global financial system. In a [letter](#) addressed to the U.S. Congress on 31 July, over 100 economists have expressed concern that the court judgment against Argentina could cause unnecessary damage to the international financial system. The letter has called for a legislative solution pointing out the examples of UK and Belgium which have passed legislations preventing such litigations by holdouts.

Argentina needs alternative credit sources

Judge Griesa's decision has come at a wrong time for Argentina. The Argentine economy has deteriorated since 2007 with high inflation, currency devaluation and shortage of forex reserves among other problems. Judge Griesa and the vulture funds have compounded the economic problems of the country by creating more uncertainties and challenges. The artificial default situation means that Argentina will continue to be locked out of the global financial markets although the country badly needs external funds to finance its development projects.

Argentina has to look out for non-western financial sources. They have been offered thirteen billion dollars of credit as well as currency swap facility by the Chinese President during his visit in July this year. May be Argentina could become the first customer for the New Development Bank created by BRICS last month.

The larger issues

The vulture funds versus Argentina case is not just a legal issue about a few billion dollars. It is about the sovereignty of a country, the economic situation of 42 million people and the future of debt structuring for other countries. It is also about the credibility of United States financial and judiciary system. [Stiglitz and Guzman](#) have a warning, 'The U.S. financial system, already practiced at exploiting poor Americans, has extended its efforts globally. Sovereign borrowers will not – and should not – trust the fairness and competence of the U.S. judiciary'.

Let us not forget that the extreme and reckless greed of a few had caused the financial crisis for U.S. and the world in 2009. The people and the government of U.S. have paid a high price as a consequence. Such tragedy could be avoided for Argentina and other countries.

Back to Washington DC

The second default of Argentina in this century caused by the New York courts and vulture funds could still be rolled back in Washington DC with Presidential discretion. Washington has a chance to redeem itself - and protect its systems and global trust. [Greg Palast](#), who has done investigative reports for BBC, Guardian and Al Jazeera, says, "President Obama could intervene in the Argentine case in the same way as President Bush prevented the seizure of the US property of Democratic Republic of Congo by the same Paul Singer. But a long term solution lies with the U.S. Congress which can enact legislation, as the UK and Belgium have done, to prevent the predatory and unethical litigations by vulture funds in matters of foreign sovereign debt. This will go some way in alleviating the lengthening list of the sins of the 'Washington Consensus'.

[Ambassador Viswanathan](#) is Distinguished Fellow, Latin America Studies, Gateway House. He is the former Indian Ambassador to Argentina, Uruguay, Paraguay and Venezuela, and Consul General in Sao Paulo.

This article was written exclusively for Gateway House: Indian Council on Global Relations, and was written for a special compilation of essays titled Federalising India. You can read more exclusive features [here](#).

For interview requests with the author, or for permission to republish, please contact Reetika Joshi at joshi.reetika@gatewayhouse.in or 022 22023371.

© Copyright 2014 Gateway House: Indian Council on Global Relations. All rights reserved. Any unauthorized copying or reproduction is strictly prohibited.