

# Developing Country Debt and Default

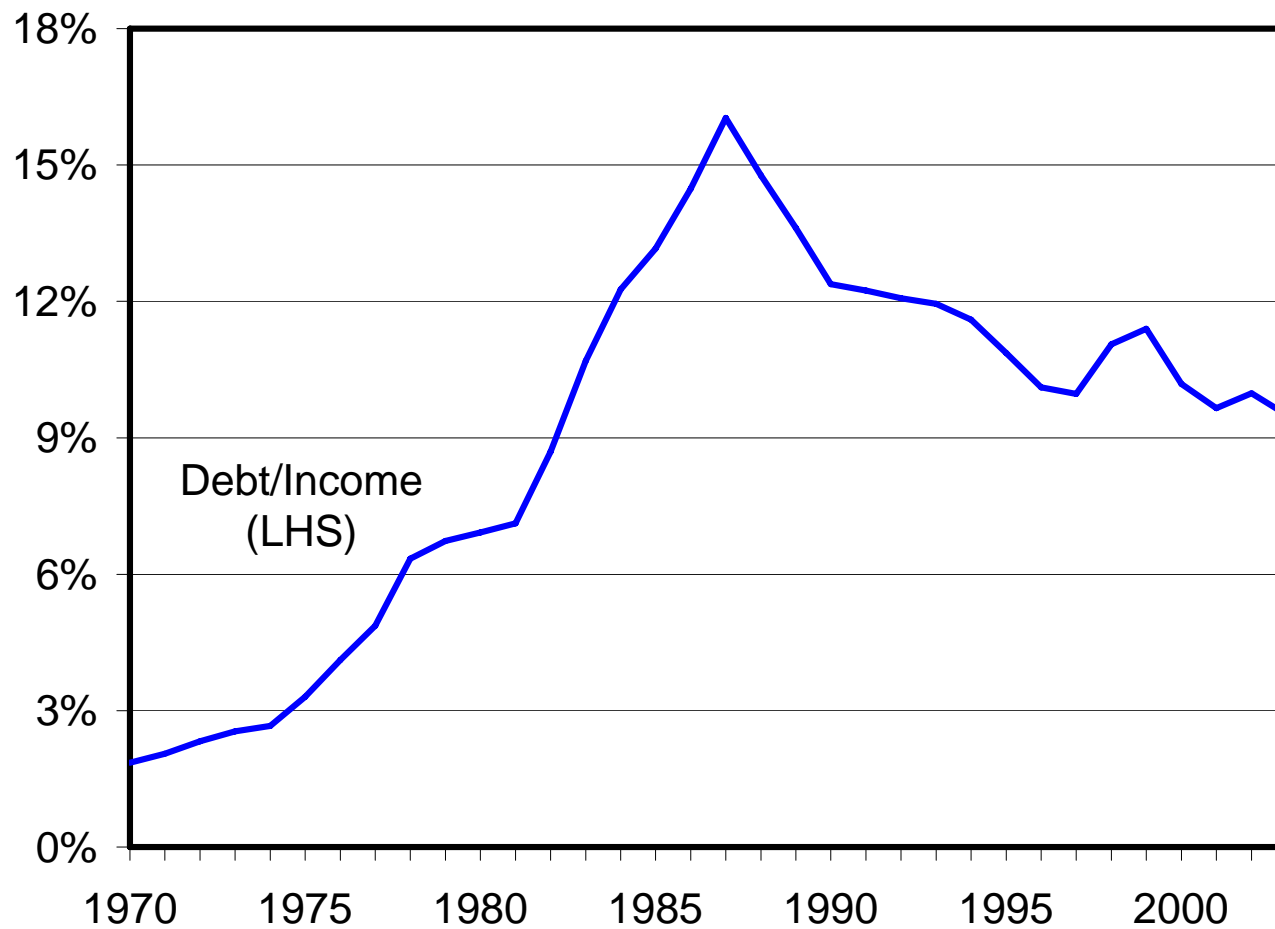
Mark L. J. Wright

Federal Reserve Bank of Minneapolis

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# Developing Country Government Debt

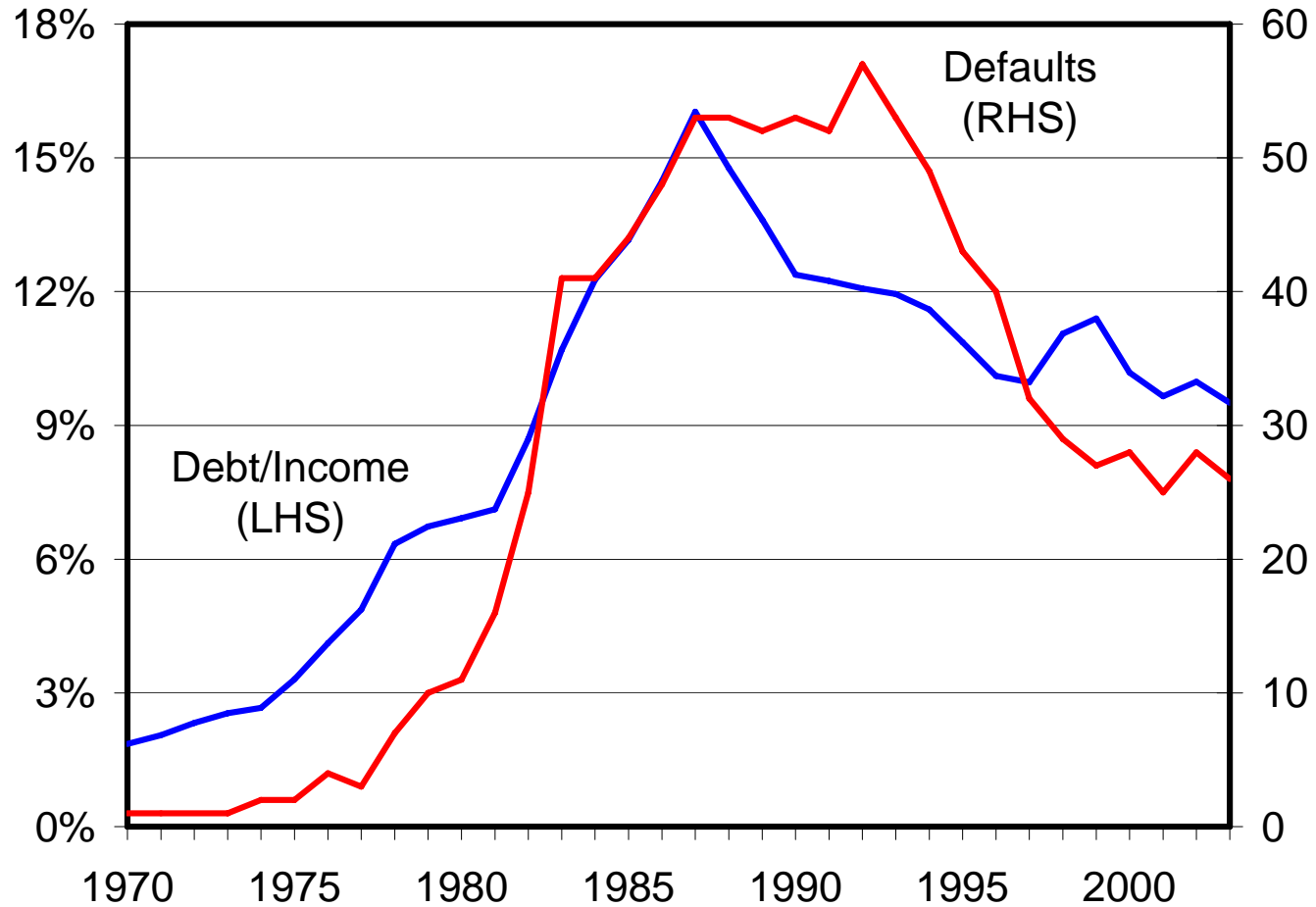
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# Debt and Default

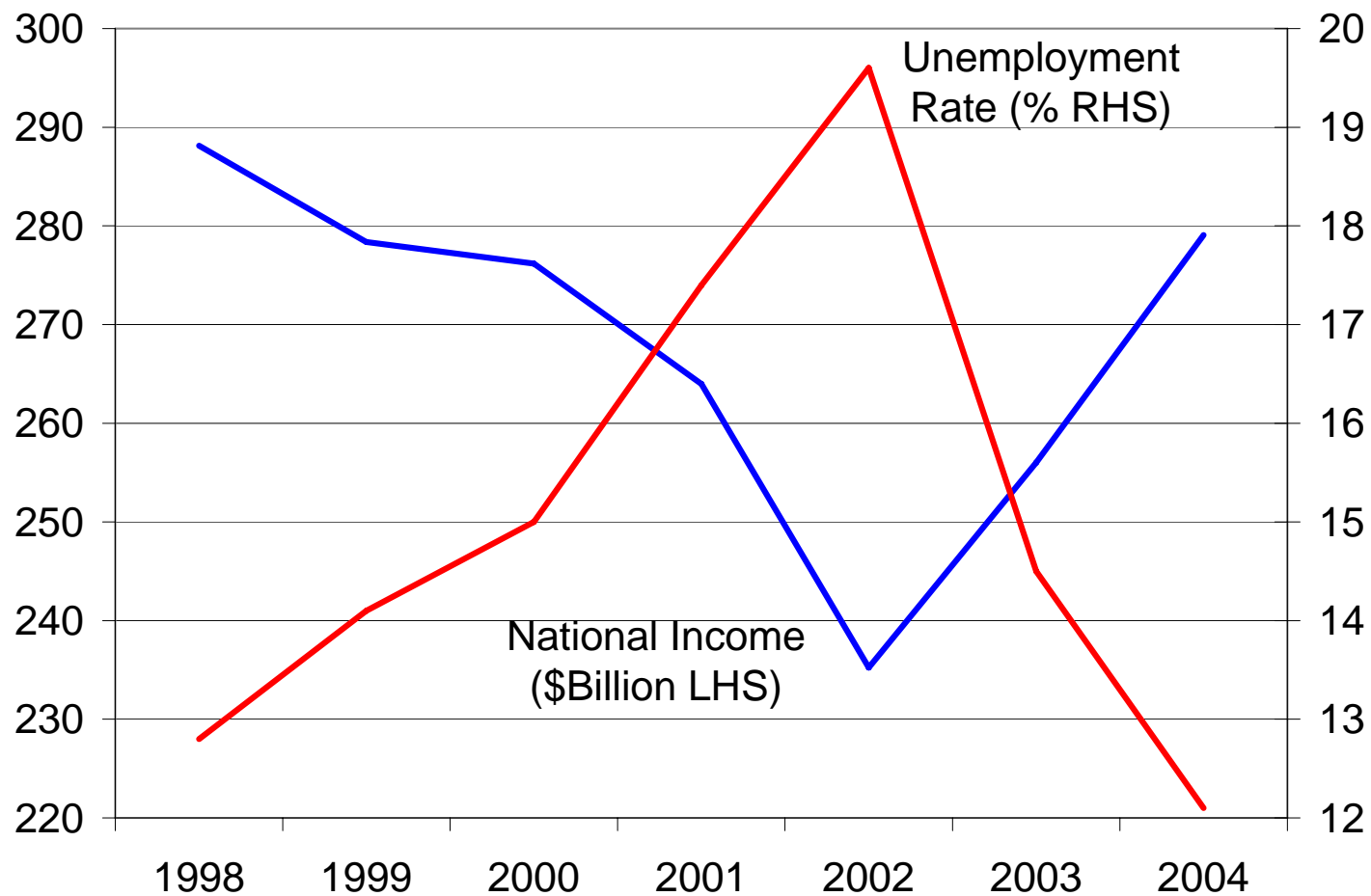
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## The Costs of Default: Argentina 2001

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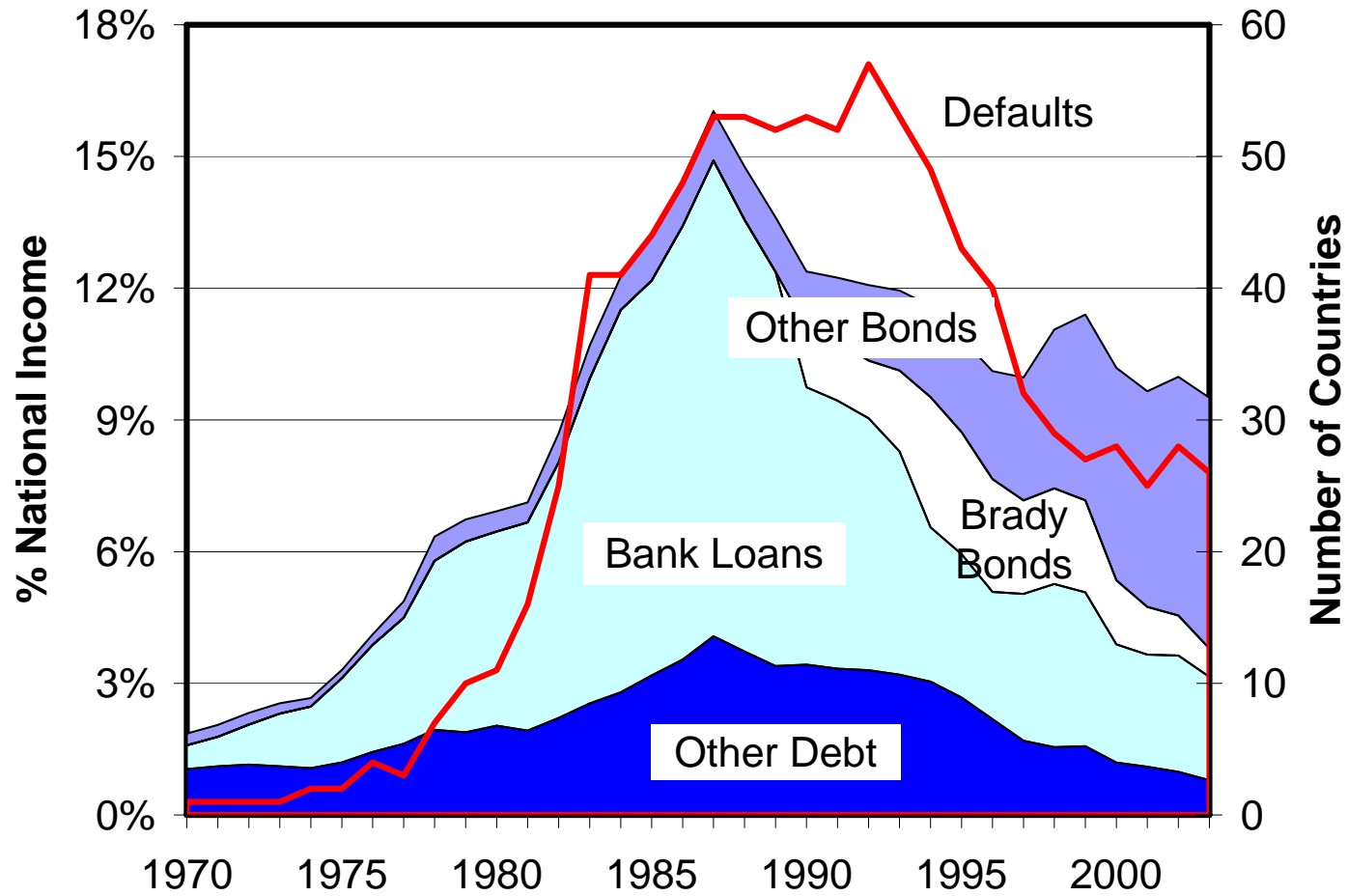
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# The Costs of Default: Creditors

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- A sample of recent bailouts by International Monetary Fund
  - 1995 Mexico (USD 18 billion)
  - 1998 Korea (USD 20.8 billion), Brazil (USD 18.4 billion), Russia (USD 15.1 billion)
  - 1999-2001: Turkey (USD 20.7 billion)
  - 2000-2001: Argentina (USD 22.1 billion)
  - 2001-2002: Brazil (USD 35.1 billion)
  - 2002: Turkey (USD 17.6 billion)
- Does not include World Bank or USA direct funding (eg Argentina 2001 approximately USD 20 billion)

# Composition of Debt



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## What Can Be Done?

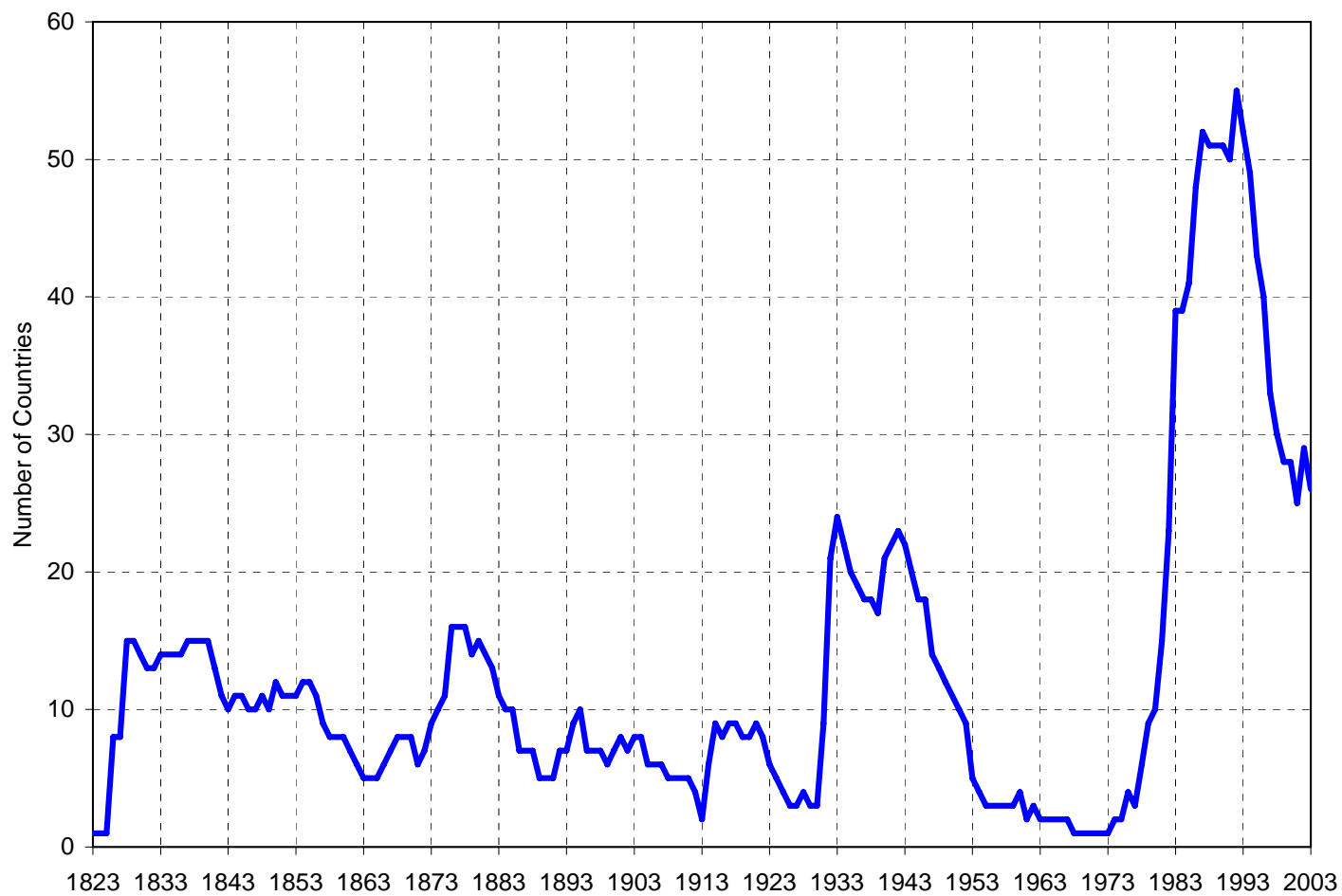
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- Question: Can we “reform” the international financial system to minimize the incidence and severity of debt crises, while still promoting efficient capital flows
- Research approaches this question from two directions:
  1. The history of sovereign defaults
    - why do defaults occur?
    - how did the private sector resolve defaults in history? (and how well did they do it?)
  2. Theories of sovereign defaults
    - use as laboratory for exploring the benefits of different policies by US government and International Monetary Fund

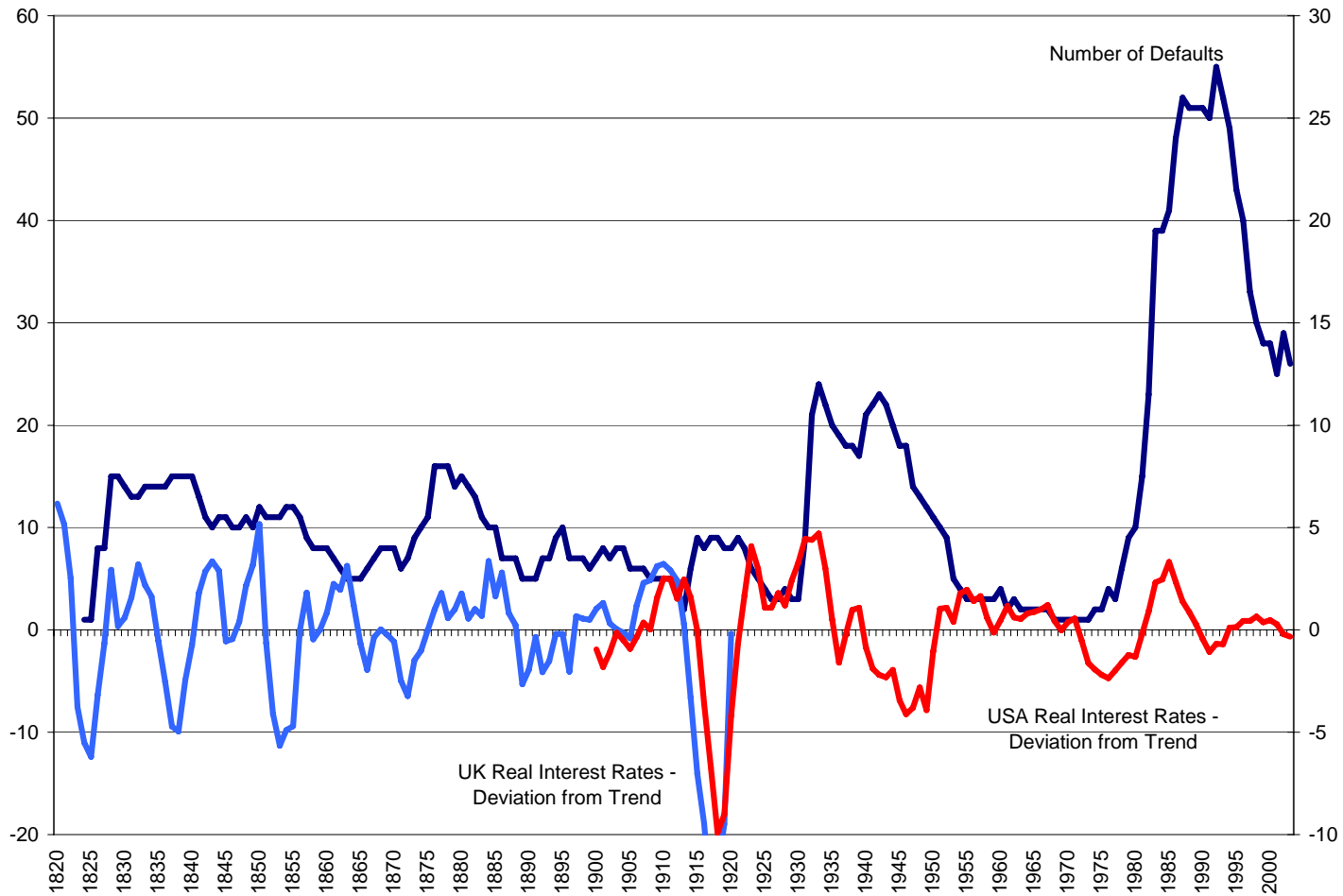
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# Two Centuries of Default

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# Default and World Interest Rates



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## Interest Rates and Output

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UK/Cty	>10%	>25%	<50%	<25%	<10%	<5%
>10%	0.02	0.02	0.10	0.16	0.22	0.36
>25%	0.02	0.06	0.12	0.18	0.24	0.26
<50%	0.06	0.06	0.19	0.15	0.14	0.28
<25%	0.01	0.07	0.03	0.04	0.06	0.07
<10%	0.02	0.01	0.06	0.03	0.05	0.05

# Dealing with Default in History

	1824 -1829	1830 -1839	1840 -1849	1850 -1859	1860 -1869	1870 -1879	1880 -1889	1890 -1899	1824 -1899
# defaults	15	3	2	3	5	13	2	17	60
# w. loan data	14	3	2	3	3	6	2	14	47
mean excl.	49	23	17	12	19	22	11	8	24
median excl.	38	31	17	12	23	17	11	7	19

	1900 -1909	1910 -1919	1920 -1929	1930 -1939	1940 -1949	1960 -1969	1900 -1969	1824 -1969
# defaults	6	14	4	30	6	3	66	126
# w. loan data	6	14	3	30	6	3	64	111
mean excl.	4	21	9	21	24	4	19	21
median excl.	2	7	2	11	18	4	12	14

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# Government Policy?

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- Private sector did well at resolving defaults in history ...
- ... government should foster the development of private sector creditor organizations
- Can the “bailout” dollars be better spent?
- Develop economic model of of developing country debt and default for use as a laboratory
  - current policy has “correct” form
  - but larger amounts of money needed
- Who will foot the bill?

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## Conclusion

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“there is a limit to the amount of money we are going to collect from within the U.S., from plumbers and carpenters, and send to some place and kiss it good-bye”

Paul H. O’Neill, Secretary of the Treasury, United States, April 30, 2002