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P R O C E E D I N G S

MR. PRASAD: (in progress) -- of the third report of the Committee on International Economic Policy and Reform.

My name is Eswar Prasad. I'm a senior fellow here in the Global Economy Program at Brookings, and I'm also a professor at Cornell University.

This committee, of which I'm a part, actually had its origins apparently in a discussion that Barry Eichengreen and Raghu Rajan had in Davos, where they said, "We academics complain about a lot of things, but we don't seem to be able to put our heads together as a group to come up with solutions to the problems we keep carping about."

So, they got me involved, as well, and we pulled together a committee of distinguished academics, former central bankers, former government officials. And the idea was to have a group with a fair amount of intellectual firepower, but, also, one less constrained by institution prerogatives or in terms of worrying too much about realism.

But, of course, in order for any policy proposals that a group makes to have any content, it not only has to worry about the analytical issues involved, but, also, about the feasibility.

Our very first report, launched a couple of years ago, was about rethinking central banking. Last year's report was on financial

regulation.

But this year, we thought we'd pick a topic that is one where we think academics have an important role to play in terms of the analytical elements -- but also may have something useful to say in policy.

And, of course, events have been fortunate to us, in the sense that what happened in Europe in the last couple of years -- especially the very messy debt restructurings in Europe, and, more recently, the interesting happenings related to Argentinian debt in the Appeals Court, in the Second Circuit, in New York City -- have brought these issues very much to the fore.

So, we have today this report that has been written by a team that is really the core of the committee, and we have three members of the core writing team here with us today.

Beatrice Weder di Mauro, who's sitting in the middle, is, in fact, the person who sort of conceptualized the report, and has been leading the writing team. She's a professor of the University of Mainz. She's also a member of the German Council of Economic Experts, so anything she says tends to get a lot of attention in Europe -- and that group really has been very influential in driving policy proposals and outcomes in Europe.

Beatrice has also worked at the IMF before, and has taught

at other institutions, as well, including Harvard.

Anna Gelpern is a professor of Law, Georgetown University. She's worked in private practice before, and, unlike in previous reports, we felt it was really important this time to have legal expertise, rather than just economic expertise.

Anna, in addition to being one of the leading international scholars on issues related to international finance and debt restructuring, also has the great distinction on this panel of being the only one who's actually not worked at the IMF -- which may not be a distinction.

Jeromin Zettelmyer is the third member of the writing team. He's the deputy chief economist at the European Bank for Reconstruction and Development. He's also the director of research there, and Jeromin has written extensively on this area, back from his graduate school days. In fact, he has a very good book on precisely this issue.

So, the amount of expertise we have in terms of the core writing team this year was really fantastic.

And we have two extremely distinguished panelists who will help us sort through some of these issues in the report, and perhaps give us some critical perspectives.

On my right is Siddharth Tiwari, who's the head of the strategic policy and review department of the IMF. And as you can infer

from those three words, that is really the most important department at the IMF, because it determines a lot of the policy and directions at the IMF. Siddharth is probably too modest to admit this, but it really is one of the core departments that determines the Fund's direction on many of these issues.

And we also have Charles Collyns. Charles used to work at the IMF. He used to head the team that produced the World Economic Outlook. He then moved over to Treasury, where he was the Assistant Secretary for International Finance, and just very recently, he switched sides, and is now the Chief Economist and Managing Director at the Institute for International Finance.

So, we are delighted to have such a distinguished panel here today, and we'll kick things off with remarks by three of the lead authors.

So, here with us today, one of the other members of the writing, Elizabeth Broomfield, another legal expert, is also with us, and she'll help us with technical questions and legal issues, if they should arise.

So, Jeromin will start off with a brief discussion about the lay of the land, the motivation of the report, and what led us to this report at this time.

Jeromin?

MR. ZETTELMEYER: Thank you very, very much for the very kind introduction, and I'm really pleased to be here, and very flattered and honored to see so many of you who really have, both practically and academically, delved into the issues that we're going to discuss in this report. So, thank you very much for coming.

So, what we're going to do is, we are going to give you a short overview of what's in the report, which we'll split into two halves. I'm going to be responsible for the part that did not motivate the Davos meeting; me just laying out the problems, and then the solutions will come from Beatrice.

So, I think one useful way of sort of presenting -- okay, that is pretty small. Can anyone see that? A little bit? Yeah.

So, one way of conceptualizing what we are going to do is, if you think back to, you know, the stereotypical discussion on sovereign bankruptcy regimes -- so typically, the way this starts is that a crisis happens somewhere, and the resolution of the crisis is very messy, it's very painful.

And so then, you regularly get the calls for a sovereign bankruptcy regime -- something that's more legally anchored, more institutionalized, more orderly, that would deal with these debt crises and

make them less messy.

And so this happened several times in history. The first time it really came up in cultural history was in the early 1980s, when Mexico defaulted, and it has continuously come up since then.

So, there's a strong intuitive case for a bankruptcy regime, but that case by itself is really not enough to make the argument that one should do such a thing -- and it's not, for two reasons.

So, one is, there needs to be some sort of professionality between the problem that you're trying to solve and the legal and institutional apparatus that you're creating to solve it.

So, clearly, debt restructurings are difficult situations, but there also are ad hoc means to dealing with them that have been essentially figured out by creditors and debtors over time. And these ad hoc methods actually work quite well, particularly since the second half of the 1990s -- and probably all the way into the mid and late 2000s -- at dealing with these types of problems.

There's a more fundamental argument not to do a sovereign debt restructuring regime, which argues that, you know, the people that really focus mainly on the objective to make debt crisis easier to resolve exposed a missing really important point, which is that maybe, just maybe, sovereign debt crises are supposed to be messy.

And in a bigger perspective that looks at the ability to borrow and the cause of debt, *ex-ante*, it's actually a good thing for a debt crisis to be messy, because it effectively is nature's -- or, if you like, the international finance system's -- response to the fact that sovereign debt is not enforceable in the same contractual way as domestic debt.

And so the worry here is that if you put into place a regime that makes sovereign debt crises easier to resolve, less costly for the debtor, you're just going to get more defaults, and that's going to drive up the cost of debt, and kill the sovereign debt market.

So, the last time we had this debate -- which was pretty much 10 years, when the IMF's SDRM proposal was extensively debated and ultimately rejected -- it was rejected for a combination of these two arguments.

The argument's a little bit inconsistent, but they were argued, if you like, by different sets of critics. Ultimately, I think it was the second argument that was more important and rejected.

So, the point is that, in order to now convince you that, you know, some of the solutions that do go into the direction of a sovereign bankruptcy regime are sensible ones, we will have to convince you that something has changed about these two counterarguments. And so what has changed in the last 10 years?

So, one immediate thing that has changed is a series of recent court rulings that imply that if you like the ad hoc machinery -- to use a term that was coined by Lex Rieffel, who's here in the audience -- for resolving sovereign debt crises, it's not going to work -- at least in its current form. And this is something that I will not go into detail on, but we have an expert on this here, Anna, who may talk about it.

Very roughly, what has happened is that these court decisions have given potential holdouts who do not agree to a debt exchange offer a much stronger tool to get their money back than they had in the past, and that means that they have greatly increased the attractiveness to be a holdout.

And symmetrically to that, they have reduced the attractiveness of being a creditor that accepts a debt exchange offer, because you can never be sure, if you do that, what holdouts might do to you in the future.

And so this means that probably the ad hoc approach will be much more difficult in the future -- which means that the exposed costs of debt crisis will go up.

The second, more fundamental, thing that has changed is, I think, a shift in attitudes -- and based on actual cases and experience over the last 10 years of what constitutes the fundamental problem in sovereign

debt.

And so what we have seen is a sort of shift from the direction of, you know, the most important problem is Brazil repudiating sovereign debt, the enforcement problem, and the fact that, you know, debtors may misbehave -- in the sense of repudiating their debts -- to a different type of misbehavior that happens long before crisis -- and that has to do with over-borrowing and essentially policy mistakes that could lead to debt crises.

And complementary to that, what we've also seen is a tendency of both creditors and debtors to essentially procrastinate on the resolution of sovereign debt problems when they arise. So, they typically restructure too little and too late, until the problem can no longer be dealt with, without a really fundamental default.

So, if you think that these are the real fundamental problems in sovereign debt, then this really means that there is no tradeoff between trying to reduce the cost of debt crisis exposed and trying to make, you know, *ex-ante* problems smaller -- because what you actually do want is penalize countries that over-borrow with higher interest costs. You want to limit the access to credit, and you want to really provide a legal framework that encourages debt restructurings before it becomes too late.

Now one of the reasons, of course, why these problems are

particularly in our mind today is because of what happened in the eurozone.

So, the eurozone is, if you like, a case which has these problems magnified, because there are fewer instruments to deal with debt crises -- so you do not have monetary policy, you do not have exchange rate policy.

There is also a fear of exceptionally high spillovers from disorderly defaults. And the reason why that is the case is because a sovereign default is always a potential threat to the actual integrity of the currency union. So, there is always the problem that a default might trigger an exit risk.

And so for this reason, the temptations to procrastinate on these problems and try to resolve them with inappropriate means -- which is just large-scale lending, combined with very heavy adjustment, even when adjustment might turn counterproductive -- is much bigger than in the standard international case.

Now one remarkable thing that the eurozone was able to pull off is the Greek debt restructuring. It came much too late, but it was very deep.

And so one thing that we discuss in the report is whether or not this, if you like, makes a new case that ad hoc machinery did work in

Europe, and whether that ad hoc machinery could be replicated in future cases.

And the conclusion we arrive at is that, you know, while it was a remarkable success in some ways, it, you know, achieved success through means that are inherently not replicable. They're not replicable because, in some cases, you know, the underlying factors were special -- but, also, because very, very large amounts of public money were involved that are very unlikely to be on the table in future cases, and because of the way that holdout creditors were treated -- namely, being paid off in full, which is essentially going to be a factor that makes it much more difficult to then get future holdouts to agree to debt restructurings of this type.

So, basically, that's the dilemma we're left with. We have a very significant exposed problem. We're not quite sure how to resolve debt crises in the aftermath of the Second Circuit rules. And, at the same time, we also think that we need a mechanism that, you know, sets the right incentives for borrowers well before the crisis -- and then for the management of crisis when they do occur.

MR. PRASAD: Thanks, Jeromin. That was a very eloquent statement of where we stand, and what we need to fix.

Beatrice?

MS. di MAURO: Thank you. Just let me also thank you for coming, and welcome you.

Now that we know where the problems are, so how do we find solutions?

What should reform achieve? Well, we have already outlines that we have essentially *ex-ante* and an *ex-post* problem. The new *ex-ante* problem seems to be that countries tend to over-borrow, rather than under-borrow. This would require a reform that basically has a disincentive to over-borrow; a second part, which is, you know, in the interim, when your problems have already started arising, a reform would have to also address the problem of the incentive to procrastinate, and to do too little too late.

That requires a restructuring regime which, in unsustainable cases, has the apparatus of legally, legitimately, and economically feasible restructuring, which also would involve -- especially in cases where there are very large interdependencies, like in the euro area, which also involves an apparatus to safeguard those countries that are innocent bystanders.

And finally, there is a final thing that reform should achieve, and it has to deal with the *ex-post* problem of holdouts -- which, you know, as Jeromin has argued, has just become much, much larger than it was

before, after the Argentina case.

Now we tried to come up with several solutions, rather than just one -- because, at the global level and at the European level, both the conditions are different, but, also, the possibilities to find solutions are different.

Certainly, at the European level, as we've just argued, a debt restructuring regime for the long run is probably a very essential part of the long run setup, of the long run architecture of the eurozone. And this is also why, in this context, our proposal is basically the most ambitious.

So, what you see here in this line is the top part of the table, which you'll find in the report on page 46, and that's a table that summarizes the different proposals, and compares them to the status quo.

International solutions -- we have three of them. They have become gradually more ambitious as you move from left to right. And the idea is also, as you're moving from left to right, you're solving more problems at once.

So, let me start from the right, and with the most ambitious proposal that is the European debt restructuring regime that we are suggesting.

Now we have emphasized that the euro area has many characteristics which make the problem more acute, and the good news,

however, is, it also has a setup and the framework which makes a solution more feasible -- and, in particular, there is already a very developed framework of both fiscal and crisis response.

There is, however, also a macro-potential and a macroeconomic framework -- which is generally agreed among the euro area countries, that they have committed to both at the level of the European institutions, as well as, for instance, in this case, of the fiscal compact, at the level of their own constitutions, where they've written rules into their constitutions that define, ultimately, what is solvency -- or what is fiscally good behavior.

Now how do we introduce this restructuring regime into the existing framework? The proposal that we have here is that we use the ESM -- the European stability mechanism -- crisis response mechanism -- as a vehicle by amending the ESM treaty in two ways.

One is addressing the holdout problem -- meaning that the ESM treaty would incorporate a clause that protects assets and revenue of ESM-endorsed restructurings from attachment.

So, basically, through this immunization, we defang the holdouts, and have a possibility of basically, you know, solving the problem that Jeromin addressed that has been made worse through the Greek restructuring.

The second part, however -- and since we've emphasized so much that the *ex-ante* problem is maybe the even more important one -- is to amend the lending policies of the ESM in such a way that restructuring not only becomes a possibility, but under certain conditions, a condition for further official lending.

And then, of course, the question is here, what are these conditions? How do you condition ESM lending?

And the proposal we have here is that basically they'd be subject to a debt threshold. And the system would work in such a way that the debt threshold, which is already totally enshrined in the European framework of 60 percent, is used as a base. Under 60 percent debt-to-GDP ratio, ESM access would be prequalified. This would be a bit like a prequalified program of the IMF.

Between 60 and an upper threshold, which is still to be defined, there would be access to ESM funding in a similar way as it is today. So, you know, restructuring can happen, but usually will not.

And above an upper threshold, further access to official lending is only possible if there is, at the same time, a restructuring.

Now this, of course, raises a lot of questions. One of them is, you know, why one threshold? Why debt? Why not multidimensional conditionance? Why not different ones for every country? Aren't there

different countries? And everybody should have their own threshold. Where to set the threshold -- these are all things that we discuss at length in the report, and I just want to mention them here -- that we do actually address these questions. I'm happy, also, to get back to them in the discussion.

But, you know, the bottom line that we come up with is that, in the European context, it would not be thinkable to have different thresholds for all countries in the eurozone, and that basically using the existing fiscal framework would lead us to suggest that we have one threshold, and that this be somewhere -- and that's then the question -- where to set it -- somewhere between 90 and 100 percent of GDP. So, that's the 1.5 times Maastricht level.

Now why around this -- I mean, obviously, if you have a threshold, that is very high. If you set it at 200, then, you know, it never binds. If you set it at 60, at the same level as the Maastricht threshold, then you may get into situations where you really are getting sort of too many restructuring.

So, why something between 90 and 100? It is somewhere in this range that we think, you know, in the long run, equilibrium of the eurozone, one could reasonably assume that you do not get too many shocks -- assuming that all the other reforms that are being put into place,

which deal with private debt, which deal with the banking union, et cetera, are also working -- that then the incentives -- or, basically, the cases where you sort of accidentally move above 90 percent or 100 percent will be very few.

And the disincentive from this regime, of course, is exactly the fact that the *ex-ante* problem of over-borrowing -- there are less incentives both to over-borrow as a government, but, also, to assume private sector debt, as there are costs to this, even *ex-ante*.

So, this is a -- well, at the same time, you may think a radical proposal, but it's also not very radical, given the fact that, you know, euro passed on much, much more radical things, such as in producing a common currency or a banking union.

But it's, of course, also a proposal that cannot be implemented tomorrow. We are not that radical, because, of course, it means that many countries that now have debt over 100 percent would be in trouble right away.

So, it's not -- let me be very clear about this -- this proposal I just made before is not something that we're suggesting should be implemented tomorrow. But it should be implemented as soon as possible.

When is it possible? Essentially, when countries' debt levels

are below the upper threshold, so they don't trigger, or they don't create the incentives for restructuring. So, there is a need for a transitional regime from getting there from where we are now, to the long-run regime.

And this could have different shapes and forms. We discussed it very briefly at the end, because that's not the main emphasis of this report. One is basically a version of a CAC regime, which only takes the part which defangs the holdouts, and basically makes the CAC restructuring into (inaudible) easier.

Another one which is -- that then it becomes a part of a grand pact -- would be to adopt a version of the debt redemption pact that the German Council of Economic Experts has suggested some years back, which essentially neutralizes for one time the debt that is over the 60 percent threshold for countries that are now not under Troika programs, and then redeems them over the course of many years.

And as countries' debt levels come down, once they fall below the upper threshold, they could enter the long-run regime. So, you would have a bridge from the short into the long-run regime.

Now to the global level -- here, of course, the conditions are more difficult, more varied -- many countries, there is no presumption that there is a convergence, and that we would have a one-criteria threshold for all countries.

Also, it maybe less important at the global level (inaudible) expect bailouts since the inter-linkage is present if you share a common currency. But other disincentives and other distortions are also there at a global level.

For instance, you know, over-borrowing could be the result of short-term horizons, and procrastination, and "too little, too late" is also a problem at the global level. And, of course, the holdout problem was already mentioned.

Now for the global level, our most ambitious reform would include -- or would, you know, be shaped in a similar way as the ESM proposal. It would involve a new lending facility by the IMF, a server debt adjustment program -- SDAP, as we call it -- which would set out the criteria -- and we are not defining them here ourselves -- that would probably be multidimensional. They may have to be adaptive over time, but would set out the criteria through which countries are then steered towards such a program, which is official lending come at the same time restructuring.

And to make this thing stick, in terms of, you know, taking away the power of the holdouts, this would -- any type of restructuring, any type of assets and revenue streams that were generated in the course of such a debt adjustment program -- from the IMF-endorsed debt

adjustment program would be immune to attachment.

The latter probably requires an amendment of the articles of agreement -- and in order to introduce this additional class of immunities. However -- and, you know, we had a long discussion in the group, also, whether any type of article of agreement change -- to suggest any type of a change in the articles of agreement should be something that we should not even discuss, because it will never happen.

But we felt that that is exactly our role; as an independent group of academics, we are actually able to -- and should actually be also willing to talk about things that may not happen tomorrow, but may still be the right things to do.

Then we have two solutions, which, you know, if you think that nothing can be done at the IMF level, then at least, you know, you would want to address the holdout problem. And we have two suggestions, which are more gradual. They do not address the *ex-ante* problem; only the *ex-post* problem. But they may still at least create the conditions that were in existence before the Argentina case.

Immunizing the payment systems -- that would require large financial centers to adopt some legislation which immunizes their payment systems and clearinghouses, et cetera, from attachment.

And finally, a coordinated introduction of a tax with strong

aggregation features based on super majority across all bonds. That is also a contractual, even softer approach, which, you know, over time, may have the effect of lowering the holdout problem.

Do not, however, both of them address the *ex-ante* problem, which, in many ways, we think has become the bigger problem than the *ex-post* problem.

So, let me conclude by saying sovereign debt restructuring regime, both for the euro area and beyond, now seems more essential than 10 years ago, and the good news is, at least for the eurozone, seven debt restructuring regime also is probably more feasible.

And thank you very much for your attention. I'm looking forward to the discussion.

MR. PRASAD: Thank you, Beatrice, for laying out the full panoply of recommendations in the report, from the modest to the radical, but not so radical. It does seem interesting and ironic to be talking about issues of political feasibility and rationality in Washington, D.C. today.

But again, our objective as a committee was really not just to think about things that are simple and relatively easy to implement, but, also, to lay out what the first best ought to be, even if it's very difficult to get there, because it's a good guidepost for where we ought to be.

Now Anna has decided to hold off and be available for

questions and answers on the difficult issues that come up in the report.

But, first, I want to turn to Siddharth. Now Siddharth is wearing his official hat as the head of the Key Department at the IMF. And, in fact, the IMF put out a report itself in May -- once again, trying to grapple with some of these issues that are clearly very important to the IMF, because even in our proposals, the IMF does play a very important institutional role, and that clearly is unavoidable.

So, Siddharth, I'd be very interested to hear your reactions to the recommendations in the report -- not just in terms of the feasibility, but, also, in terms of their analytical content.

MR. TIWARI: I see several people in this audience who have taught me, so if I make any mistakes, it's their fault; it's not mine.

But most seriously, I'd like thank the committee, and also like to thank Brookings for this panel. I'm really pleased to be here. I'll touch on two things -- the report of the committee and the work of the Fund.

So, the publication of the report is timely, and it makes important contribution. There have been important developments in the world of sovereign debt restructuring in the last few years. It's the Greece sovereign debt restructuring, which is the largest in history, sovereign litigation against Argentina, the implications for collective action clauses, and, finally, several ideas that have been proposed on the global stage for

some kind of mechanism, including the ideas that have been put forward today.

So, one conclusion of this report is that there's been a shift in the debate. Critics of the previous attempts to reform the sovereign restructuring mechanism feared *ex-ante* efficiency, and that was important at that point.

The argument was that opportunistic defaults from an overly accommodating restructuring framework and the resulting higher borrowing costs. So, that was clear at that point that the *ex-ante* fears were relevant.

The report points out that the resulting events have shown that it's probably more adequate to fear *ex-post* inefficiencies, rather than *ex-ante*, and that over-borrowing and delayed restructuring has been problematic.

In fact, the paper makes clear if there's a tendency to over-borrow, then the system that raises borrowing costs may not be inefficient.

The paper puts forward a mechanism facility for the Fund. I will not comment on the specifics of the facility at this stage, because I've had it for a few days, but we will review it and respond. But I will comment on the broad framework under which the facility or the program has been developed.

So, one broad point to start off is that the debate (inaudible) has been going on for about 50, 60 years now. This debate was at the heart of the exceptional access discussion that took place in the Fund. It's been at the heart of defining access policy in the Fund.

So, the access policy that finally emerged was that a rigorous and a systematic analysis should indicate, with a high probability, that a member's debt is sustainable in the medium term.

So, there were two compelling considerations for this. One was, it was recognized that sustainability was a judgmental criteria where judgments were brought to bear on a country's debt sustainability position. If that was so, hard access limits would preclude the flexibility that was needed in providing large-scale financing in circumstances where a member with significant debt could manage its problems without restructuring. So, that's one part.

What comes to mind here is Turkey, and what comes to mind here is Brazil, which happened under the first part.

And then, on the other hand, there were concerns that because these issues were judgmental, the Fund would lend too much into unsustainable positions -- that there would be pressure on the Fund to provide financing in the absence of restructuring.

This view would argue that there should be extra-thick limits

on access -- the flip side of it being that restructuring would be predefined, and that is the position that is akin to what is in this report.

I think for us, these two considerations were important. The way it was balanced was to provide for constrained discretion, in the sense that it required a high probability of debt sustainability. The debt crisis has brought this debate back squarely into the ring.

These are core operational implications for us. Our resources are often called upon when the countries run into problems and has lost market access.

In most cases, adjustments and provision of financing can resolve the problem without restoring to restructuring. But if sustainability cannot be achieved and financing is not available, sovereign debt restructuring may be the only option. We are a key partner in this, in assessing the envelope available for the country.

The work of the panel is timely in reviewing our role in this area, and at this stage -- and I'll touch upon our work a little bit -- we are quite open to inputs from this panel and other panels into how we take the work forward.

So, in May of this year, the Fund did its first paper in recent times on sovereign debt restructuring. The paper, although it was substantive, did not provide any strong policy conclusions. In the

discussion, two conclusions came out.

One, that the question was the extent to which our lending policies need to be modified to address the risk that restructurings, by and large, have been too little and too late. And these are not so much recent restructurings, but if you look at them from the Caribbean to some in Europe, some in Africa, they have been too little, too late.

And in that sense, our own work that we did earlier this year is in line with the premise of this report.

And the second issue that came out was how the contractual framework can be in hands to address the collective action problem.

On the "too little, too late" problem, there's several factors that affect this. Creditors are naturally opposed to NPV losses. Debtors fear economic and political fallouts, while official lenders may resist spillovers and moral hazards. Assessing whether debt is unsustainable, essential for Fund lending, is a judgment, and that judgment can delay coming to a conclusion.

I might add that the international community itself is not immune from these pressures. Collective action problems are also a constraint. The spread of (inaudible) have helped, but, as you know, holdout remains a concern.

At the same time, it's important to act promptly to address

the problem, and the committee's put forward a suggestion in that direction.

Delay is costly. If it is prolonged debt, overhangs depress growth, and official money is used to bail out the private sector.

So, how can we do better? There's one suggestion here. There are other suggestions, which we've been looking at, as how we can improve the debt sustainability analysis. Greater realism in the baseline scenarios, enhanced coverage of risks associated with the debt profile, analysis of macro-fiscal linkages, macro-financial banking sector linkages, contingent liabilities, related to the level of the public debt, greater coverage of fiscal and public debt aggregates.

The analysis is also taking a more risk-based approach than before. I think one of the things we're also looking at is stricter requirements for the use of our resources, for creditor bailouts, and we're exploring ways to keep creditors in.

Our work is also looking at ways to prevent or contain contagion, to reduce the cost of restructurings.

And finally, it's looking at how to address the collective action problems.

We are open for suggestions. There's committees. Work (inaudible) next six months, we will have several interactions with this

audience, audiences like this to seek inputs while we go forward.

Thank you.

MR. PRASAD: Thank you, Siddharth.

Charles, let me turn to you now for the private sector perspective. Now you, of course, have seen this from many different angles. You worked at the IMF on countries that were dealing with debt restructurings. Now you're advocating for private financial institutions. What do you see as the content and possible criticisms of the recommendations we have come up with?

MR. COLLYNS: Thanks, Eswar. Certainly, it's a pleasure to be here -- very distinguished panel -- and a very distinguished audience, too.

I'm reminded by sitting next to Siddharth that he and I used to sit next to each other in the deadbeat debtor division in SVR -- although it had a somewhat more bureaucratic name at the time.

Well, since then, I've been in Treasury, and now I'm at the IIF. But I'm not going to give an official IIF response to the report -- and certainly not going to give a Treasury point of view, either.

On the other hand, I'm definitely at the skeptical end of the panel, so you've placed me correctly.

I think I would challenge -- I mean, I take your points, but I

would challenge the strength of the argument towards saying that both the *ex-ante* problem and the *ex-post* problem have increased considerably, to such a degree that we need now consider very radical solutions, rather than tweaking the system.

And, certainly, the Argentina legal judgment raised a lot of uncertainty about the future fate of litigation by holdout creditors, but it's not absolutely clear how this is going to work out, in the sense that the court, in making its judgment, emphasized that this was an exceptional case.

Argentina had taken a confrontational approach over many years, had not been responsive to the courts, let alone to the creditors, and, therefore, it's not clear that this should immediately be seen as a precedent that can be applied across many other cases.

That's the first point.

I mean, as has been mentioned, there have been a number of other restructurings last couple of years that have proceeded quite smoothly. We have the Greece case, but we also have a number of Caribbean cases -- Jamaica, Saint Kitts, Belize -- maybe the haircuts are relatively small in the Caribbean cases, but in part, that reflected the judgment -- since most of the debt was actually domestic debt, rather than external debt -- you created bigger problems than you solved by having

large write-downs.

So, it's not clear that the relatively small size was because of the negotiation process, but, rather, the underlying fundamentals.

Nevertheless, there is an increase in uncertainty. There are questions raised about the holdout problem, and I think it is sensible to consider, are there ways to improve the approach that has been used? You know, the market-based, contractual, voluntary approach.

And I know that a number of groups are looking at the possibilities of rewriting collective action clauses, performing more uniform clauses, introducing super aggregation clauses that would make it easier to void the holdout problem.

The IMF is doing work in this area. The IIF is certainly considering these issues. The Treasury is considering these issues.

So, it's a very active research program in this area, and the trick is going to be finding the right balance between changes that would allow more efficient restructuring, but at the same time, recognizing the need to respect the rights of creditors, so you can give the majority great powers to enforce a general solution.

But at the same time, you need to make sure that you're providing fair treatment of the full range of creditors.

So, that, I think, is a feasible approach that could get broad

support across the community.

Now when you go to the more radical solutions that are, in some sense, top-down, rather than bottom-up approaches, I think you enter some really pretty fundamental problems.

For a start, you're shifting the balance between creditors and debtors in a fairly fundamental way, and you need to be very careful how you do that. It's not exactly clear what the recommendations in the report are, so it's hard to comment specifically on that.

But, I mean, going back to the SDRM days, there were concerns from many parts about the proposal to introduce a mechanism -- not least from emerging market potential debtor countries that were concerned that introducing such a mechanism would tilt the balance in such a way that it would be much harder for them to borrow in future, because creditors would be worried about the application of the mechanism in a punitive way.

So, in fact, the emerging markets resisted the SDRM, as well as the United States and other mature economies.

There is the question of potentially destabilizing effects, potential contagion effects. If you trigger a mechanism too easily, that could have impact not just on the particular country, but on a broader range of countries that need to be considered.

Also, I think, more fundamentally, there is this political issue, which I think you sort of alluded to in your initial remarks.

Quite frankly, it's very hard to see, in the United States, any support for an amendment to the IMF's articles or any other international mechanism that would, in a sense, supersede U.S. creditors' rights to use the legal system to protect their positions. I think that's just a complete nonstarter -- and it's not just a nonstarter now; it was a nonstarter 10 years, and I'm sure it'll be a nonstarter 10 years from now.

So, I just don't think that's -- I mean, economically, it's interesting, and I appreciate the analysis, but I think, politically, it's a nonstarter.

In terms of the IMF's role, and, also, you know, what happens in the eurozone, I think I share many of Siddharth's views -- that it's very difficult to set quantified thresholds that can be used in a fairly blunt to guide decisions. In the end, the IMF needs to use its judgment about when a country's in an unsustainable position, and when, in fact, it could work through its problem with some tough policy choices.

I worked on Brazil as it went through a very difficult period, when, you know, all the experts said that Brazil is not going to make it. But Brazil was able to muster the political will to take tough economic decisions that allowed them to make adjustments, so that they were very

quickly able to repay the Fund and to regain market access.

It's also very hard to make early decisions on how much the restructuring needs to be in crisis situations. I worked on Argentina in 2002, when, you know, it was clear that Argentina would need a restructuring. But there was no way we could provide a debt sustainability analysis that had any real concreteness or credibility, just given the huge amount of uncertainty in the situation.

So, the idea that the Fund has been supporting too little, too late -- I don't see that as a general tendency, but, certainly, there have been some circumstances. But I wouldn't see it as a general rule. You need to give countries the opportunity to work their way through problems. You need to find out, what is the true situation or problem? What is, indeed, a deep insolvency problem, as opposed to a liquidity problem? What are the political constraints on action?

I'm also somewhat skeptical about whether there is really a widespread sovereign over-borrowing problem in emerging markets. I mean, certainly, there are some advanced economies that have over-borrowed. And I think the European situation was quite a special one.

But if you look at emerging markets, broadly, these countries have adopted much more prudent, more disciplined fiscal policies over the past 10 years. They've been bringing down their debt-to-GDP ratios quite

consistently. There are exceptions, or some countries that have gone on borrowing binges when emerging markets turned very favorable. But as a broad systemic judgment, I'm a little bit skeptical on that.

I think that the bigger problem's not so much sovereign borrowing, but corporate and banking borrowing. And, certainly, there have been credit booms in recent years, including surges in external borrowing that were exposed over the summer, when we had this correction in emerging markets and in the wake of the increased market expectation that the Fed would start to taper soon.

So, overall, I mean, I tend to support what Siddharth was saying -- that constrained discretion is the way. You shouldn't impose rules. Yeah, sure, it strengthens the TSA; that's a sensible thing to do, but look at the bigger problems -- banking problems, corporate problems. I'm not sure that the sovereign is really the central problem for emerging markets.

And then, quickly, on the euro area -- I mean, a similar range of principles. I'm not sure that, again, it's sensible to set very hard and fast thresholds. And, also, I think you need to consider that when this new system comes into play, it's not going to be anytime soon; it's going to be maybe five, ten years from now.

The whole architecture of the eurozone is going to be very

different from what it is today. The Europeans are working hard to strengthen their overall framework to support currency union. They're working hard to build fiscal discipline through their new procedures. They're also working hard to put in place banking unions, stronger supervision, stronger resolution.

Of course, I'm somewhat skeptical about the rate of progress, but I think five to ten years from now, they will have made very substantial progress and strengthened the underpinnings. And it's less clear -- in those circumstances, you really need the sort of statutory mechanisms that are being proposed here.

So, I'll leave it there -- but, generally, I'm on the skeptical end.

MR. PRASAD: Thanks, Charles, for those blunt but very constructive comments.

Let's pick up on what Charles mentioned at the beginning of his remarks -- and perhaps we'll start with you, Anna. I'd like to get your reaction to his notion that the Second Circuit Court of Appeals's rulings related to Argentina don't really set a precedent. I'd like to get your reactions to that.

And second, Charles said perhaps even if you think there is a problem -- and he wasn't convinced there is -- that perhaps some small

tweaks to the system that gets us closer to a market-based contractual approach to these issues would be sufficient, rather than tacking on any additional rules or any additional framework.

What are your thoughts on those two issues?

MS. GELPERN: So, I think Charles and I are not that far apart, but I think it makes sense to flesh out where we differ.

So, the Second Circuit issued two opinions, and the second one -- perhaps responding to the concern about precedent -- said, "Well, just because we're deciding this in the case of Argentina" -- which did a number of bad things -- "doesn't mean that we will do it in other cases."

What the Second Circuit didn't say is, where do you draw the line, right? So, we know what a bad country looks like; we don't know what a good country looks like. So, it is entirely possible that there will be adaptation in the form of future decisions, in the form of future restructurings, future contracts -- but that's not where we are today.

In addition, the decision made some inaccurate statements about the state of the world. So, for example, Argentina's contracts -- which are not at all unique, and, in fact, have been much more common in recent years than before.

So, in that sense -- but the bottom line is, I think Charles and I are on the same page. Argentina has injected uncertainty. Whether this

uncertainty is fatal, I think, depends somewhat on your view of the current state of the sovereign debt restructuring equilibrium.

And I think if you view the world as basically okay, and resilient, and not terribly overindebted, and correctable, then I think we can stand more uncertainty.

I think if you view the world as a very fragile balance between, on the one hand, debt that cannot be enforced; on the other hand, debt that can never go away, then even a limited disruption can make a big difference. And I think that's where we differ.

Now the final point is, so why does this take us to statutory versus contractual? Now I think it's important to point out that we're not against contractual. In fact, we're for contractual.

But one of the things that's important to take away from the litigation is that contracts are both flexible and fragile, right? So, the other side of flexibility is fragility. You have a term that, for many years, was interpreted one way, that then is interpreted a different way by a court, which then, 10 years later, is picked up by another court, and, all of a sudden, debt that unenforceable becomes enforceable.

That's the world of contracts. It's inherently flexible, but it's also inherently unstable. A surgical statutory response addresses that.

MR. PRASAD: That's a very precise response, which is

exactly what one would expect from a lawyer.

Let me expand the discussion, and come back to another point that both Siddharth and Charles have raised. And Beatrice, maybe you can take on the issue of the thresholds.

Now both of them have pointed out that in the report, we do talk about specific thresholds. We do talk about thresholds in fairly limited dimensions -- so both Siddharth and Charles have made the point that perhaps one should be a little cautious about setting up thresholds -- perhaps even in Europe, as Charles had mentioned; later on, globally.

And over lunch, we had this discussion that there might not just be "too little, too late," but perhaps a "too much, too soon" problem if you set the threshold at the wrong level.

So, why the emphasis on thresholds, and do you think there is a way around them, or do you think they pose a risk?

MS. di MAURO: Well, the emphasis on thresholds ultimately is linked to the question -- if you think that, you know, the system has an inherent incentive to misdiagnose, to wait for too long, and then do too little, then you need some kind of binding the hands of those who are making the decisions. And those, ultimately in our view, can be -- you know, you can bind the hands of the official lenders.

So, it's not a system where you have, you know, an

international bankruptcy court. There is no top-down in that sense. I would really push back on that. There is no top-down here; it's just a restriction on what, you know, taxpayers' money can be used for -- and let me put it this way -- for bailing out, yes?

Now in the European case, you know, there used to be a system that was called "no bailout," and it turned out to be nonenforceable, non-credible, you know -- a huge problem of, ultimately, non-credibility. And we're not suggesting going back to that. We're using a crisis mechanism which has, implicitly, of course, a bailout feature.

But the question is, you know, can you go from a system in which you have, you know, no bailout to now, one in which you have predictable bail-in?

Because the type of bail-in that we are seeing in Europe is clearly not predictable, if you look at Cyprus -- and probably, also, not optimal, you know, if it comes out of the blue, and only when people cannot stand it anymore -- or when they think, "Now we can do it with this little country."

So, that's not a very good system -- and remember that the threshold -- if we look at the U.S., there is a clear no-bailout rule for states in the U.S. -- and there, the threshold is, in that sense, much, much lower, because there is no system for providing temporary crisis finance to a

state which run into trouble.

So, the U.S. fiscal system is much, much stricter than what we are proposing here for the eurozone -- just, you know, to put some context to this pushing back against the threshold.

And, also, remember that we're not suggesting having a threshold which is set very, very low. It, in fact, is taking some buffer idea into account, because the whole fiscal system, as you correctly said -- you know, if everything works that the Europeans are putting into place right now -- take a loan -- the six-pack and the two-pack -- if all of that works, then we are down to 60 within 15 years almost everything. And then you can say, "Okay, we've done it. This problem is solved."

Then if you have an upper threshold of somewhere between 90 and 100, that's going to be costly. That's because you never use it here. Okay, fine; then you can, as well, have it. You could say, "We may as well not have it," but, you know, the incentives are set better if you do have it. If you say from a certain point on, you know, "Careful, private lenders; careful, governments." You don't want to get there anymore. You've been there; don't want to get back there.

And let me just say one more thing. You know, Charles has said this is about shifting the balance between debtors and creditors; I think a lot is about shifting the balance between different types of

creditors. We are restraining official lending here, so it's about the balance between official lending and private lending -- or, you know, at what stage private lending or private also taking part in the burden-sharing has to set in.

And it's not the case in my view that -- the immunization part is not about, you know, super national authority constraining creditors in the U.S.; it is about restricting the ability of some creditors in the U.S., in this case, abusing -- I'm using a non, you know, technical word here -- the legal system to attach revenues of other creditors who have agree to a restructuring.

These are also creditors in the U.S., so it is about the distribution between different types of creditors. And there, I don't see why, in the political sense, if we're honestly speaking, why this could not be something that is totally acceptable, also, in the U.S. -- because this kind of redistribution, I don't know if you think that's good; I don't.

MR. PRASAD: Charles, let me get back to you for your reaction to what Beatrice said, before I go back to Jeromin for the bigger point.

MR. COLLYNS: Yeah, and perhaps I don't quite understand what is being proposed, but what I had understood was that the IMF or some other international body would have the capacity to reach a

judgment that a debt restructuring would be needed, and then to provide immunity to the debtor country to attachment by creditors who are concerned about the country's failure to pay the full amount.

It wouldn't just be targeted specifically at creditors who did not participate in a voluntary discussion, but, rather, would provide a blanket protection of the country against all attachments.

What are you proposing?

MS. di MAURO: Not quite.

MR. COLLYNS: But subject to the agreement of the super majority of creditors.

MS. di MAURO: Right; that's key.

MR. COLLYNS: So, this is not -- I mean, this is really important -- this is not about shifting the balance between creditors and debtors. It is about limiting the use of public money in situations where, you know, there are serious doubts about debt restructuring.

And the only thing, I think, that makes what we're proposing controversial is that we are proposing that the judgment of what is unsustainable be specified exactly, okay? And then you can always make mistakes, I suppose.

But this, I think, is the tradeoff that one cannot avoid. So, if one thinks that there is an inherent bias in the system towards overuse of

lending, essentially, in situations where debt restructuring is needed -- and on that, I think we do have abundant evidence.

Unfortunately, you do have to come up with commitment devices, and when you come up with commitment devices, there are always errors that you make exposed. But on average, I think that the system will be improved.

MR. PRASAD: Siddharth, do you have thoughts on this issue?

MR. TIWARI: So, my sense was, it's not shifting the balance; it's getting the right balance. The right balance is adequate adjustment, prompt restructuring, and sustainability over the medium term.

And what is sustainable over the medium term, this issue of thresholds? I see thresholds as being dynamic; they're not static, one. Two, they differ across countries.

So, ability of a country to generate a primary balance, and build the ability to productivity changes over time, the debt management system -- all of these determine the threshold. And these factors change, and they differ across countries.

So, to some extent -- and I think we talked about it before -- to some extent, the thresholds here are akin to the (inaudible) system. I see them as backward-looking -- backwards for the official sector, not for

private market borrowing.

So, I have an issue with a threshold, and I also have an issue with shifting balance, because one thing we should be able to agree is, what is the right balance?

MR. ZETTELMEYER: Can I make one just clarification?

So, there are two proposals here that differ quite a bit. One is for the international level, involving IMF; the other one is within the European system, within the European fiscal framework, through a chance in the ESM treaty.

As far as the international level is concerned, we do not take a position on what exactly the exacting criteria should be that limit the IMF's lending, or that it should be uniform, or that it should be one-dimensional.

So, these are things that, indeed, you know, given the fact that the IMF is likely to be a much smaller source of moral hazard, given its size, than the ESM, and given the much greater diversity among its clients, and given the lack of an underlying consensus on a fiscal framework within the membership of IMF, this is stuff that will have to be resolved, not through imposing a uniform rule on the IMF through a change in the articles, but through the procedures of the IMF itself.

Now the hope is that the IMF will figure out a way to do that,

so this is actually worth the paper that it's written on, and is not simply shoved aside once the rubber hits the road, as was done in the case of Greece, right?

So, we have wonderful people at the IMF right now who have learned their lessons from Greece. We are very optimistic that this will happen.

Where we do take a tougher approach is on the eurozone, right? And the reason that we take a tougher approach on the eurozone is because the potential source of official lending is much, much bigger, because there is really no serious governance that is in any way rules-based or practice-based, even as far as internal rules are concerned, of this source, which is ESM. It is an entirely politically-driven decision-making body, and it's huge. And it arguably, you know, hasn't gotten off to a terribly good start with Greece.

And so here, I think we need to have externally-imposed constraints -- to write into the ESM treaty, "Thou shalt not bail out countries if their debt exceeds a certain threshold," right? Because the temptation to do so otherwise, politically, is just overwhelming.

The nice thing is, though, that the bluntness and, if you like, the primitive nature of the rules that we think are necessary to constrain the ESM are fully in line with what the Europeans themselves have agreed

to in the Maastricht framework, in which what they think are the right thing to do.

So, they really deserve these rules. I mean, they have, in some sense, laid the foundation for them. We just forced them to a little bit of consistency, right? You cannot, on the one hand, impose these rules, pretend that everyone's countries should stick to them; on the other hand, you create a big -- a pile of 500 billion euros that, you know, governed politically, and is not governed by tough criteria.

So, I think we have to put those in place.

MR. PRASAD: The room has certainly gotten a lot more passionate since we went to the EBRD from the IMF.

Let's give the audience, which has been waiting patiently, a chance to get in on the action. If you have questions, please raise your hand -- and limit it to questions rather than commentary, please -- and please identify yourself at the beginning.

Randall? A mic is coming around to you.

MR. HENNING: Thank you very much. I'm Randall Henning, at American University.

My question had to do with the relationship between the two proposals -- the one at the IMF level, and the one at the European level. Of course, European countries will be members in both, right? So, two

parts to this question.

What are the ways in which we need to worry about the consistency between the two proposals, and how do you anticipate that?

And the second has to do with the design of the proposal at the European level. The early versions of the ESM treaty specifically provided for a role of the International Monetary Fund in the decision as to whether debt of a European state was sustainable. Is that sort of involvement of the Fund in the European regime, in one way or another, desirable or undesirable?

And I'd put that question to both the authors of the report and to Siddharth Tiwari.

MR. PRASAD: Actually, I think many of these questions are going to be directed to many people. So, why don't we gather up questions, and then each person can speak for a couple of minutes at the end -- and summarize comments.

Yes, please?

SPEAKER: Thank you. It's supposed to be a question, so I guess I'll have to start by saying I hope Charles will respond to the comments that I make.

MR. PRASAD: Keep it short, please.

SPEAKER: Two things, if I may. Charles, you said as you

look around the world, you don't see sovereign debt problems proliferating in the emerging market countries -- and that's true.

Then you said it's mostly private -- Ireland. Ireland was a private debt problem. It became a sovereign debt problem. So, I don't think you can -- and I think, in the future, when that kind of situation arises, you may well have the same kind of device looked to, to deal with it. So, I don't think that puts me at rest and calm about the situation in those countries. Banking problems are going to continue, and they fall with a heavy burden on the governments.

The other one is Greece. In my view -- and I think this is correct -- and maybe Anna will comment on this -- Greece was a statutory solution. It was not fundamentally a CAC solution. The only reason it worked is because most of Greece's debt was under domestic law, and it was able to change that law in a statutory law.

Thanks.

MR. PRASAD: Okay, thanks.

Nancy?

SPEAKER: Yeah, this is to follow up a little bit, actually, on the last point -- sort of the big elephant in the room that hasn't been discussed in terms of trying to deal with the problems *ex-ante* is, a lot of the sovereign debt issues really originated with badly managed financial

sectors.

And that certainly is a big part of the problem in Europe. We saw Spain, for example, that did not have unsustainable debt levels until the banking system collapsed.

So, in addressing *ex-ante* issues, isn't a lot of the problem -- and, increasingly, we've seen a lot of the problem is how to deal better with financial sector management.

And I don't know whether your group addressed tht at all.

SPEAKER: Hi. Actually, this is a related question, because there's a lot of work on bank restructuring -- also making the debt issue by banks and so on. So, I was just curious whether you've tried to link the two.

MR. PRASAD: Jim?

MR. BOUGHTON: Thanks. Jim Boughton, with the Centre for International Governance Innovation.

I have two questions of sort of a philosophical nature.

First question is with regard to the CACs. There's a lot of talk about preserving the rights of minority creditors, but, to me, that's kind of a nonsense idea. And when we discuss political democracy, there's clearly winners and losers, and you have to protect the rights of the minority.

In the case of creditors, every creditor has exactly the same interest, which is to squeeze as much money out of the debtor as they can. And the problem, it seems to me, instead, is that there's no objective criterion for determining what a sovereign debtor can afford to pay. It's not like a corporation, where you just add up assets and liabilities.

Any debtor can afford to repay all of its debts if it can tax its citizens highly enough. And so that strikes me as a real problem, in that the CACs sort of ignore that. It's kind of a diversion.

And then the second question comes out of remarks that Jeromin just made -- that it's true that the European Union had this criteria, and then they just started being ignored, and the temptation to ignore them becomes greater the longer it goes on.

But isn't the fundamental problem with those criteria that the criteria themselves are completely arbitrary? I mean, you set up 60 percent of GDP as a criterion, or you set up 90 percent as a threshold. They're completely arbitrary, so I'm wondering how you can set up a proposal that's based on completely arbitrary rules.

MR. PRASAD: Okay, that's a nice set of questions for discussion, ranging from elephants in the room to philosophical issues.

But let's start with you, Charles, and maybe go in reverse order. And don't feel obliged to answer all the questions, but maybe just

take a minute or two to summarize your key thoughts.

MR. COLLYNS: Sure. Well, Nancy very kindly gave the reply to Jack's question about, isn't the Irish over-borrowing in the banking sector ultimately a sovereign problem?

Well, it depends what your resolution regime is for banks. At the time that Ireland got into its mess, you didn't have a proper resolution regime for banks, and all the debt was transferred -- well, not all the debt, but a substantial amount of debt was effectively acquired by the sovereign.

But once we have an effective resolution regime, that will not be the case -- A, because the private creditors or the banks will start taking a hit, and, also, because you'll have a European-wide sharing of the risk, not just (inaudible) on the Irish sovereigns. You break the link between the banking balance sheets and the sovereign balance sheets.

On Greece, I would not say that it was a statutory solution, but rather as an accelerated contractual solution. Certainly, they've changed the rules *ex-post*, but the rules that they created were the sort of rules that one might now consider as useful rules for sovereign debt contracts for the future.

So, what they did, essentially, was introduce an aggregation clause into the domestic debt that allowed a qualified majority of creditors

-- I think the threshold was, what, 75 percent -- and in the end, it was far exceeded.

So, introducing the aggregation clause allowed the market-based approach to be successful, and to achieve a pretty dramatic write-down of the debt.

In the case of the Greek debt issued under English law, they didn't have the aggregation clause; they only had the collective action clauses, and in 50 percent of the cases, the creditors did not have a sufficient majority to actually agree. And those lines of debt did not get restructured.

So, I think, back to the Greece case, perhaps can give an example of how a different legal framework could actually be quite effective for restructuring.

And finally, on this issue of the rights of creditors -- I think it is more complicated than you were saying, Jim, because, you know, different creditors hold different sorts of debt, and are in different situations.

So, I guess it's, you know, particularly clear in the Greek situation; you had a number of creditors who had short-term claims, and you had creditors who've had longer term claims. And by applying a similar haircut across all these creditors -- in fact, you're applying much

greater losses on one group than another.

So, that raises questions of inter-creditor equity, which I think are complicated. Belize needs to think them through pretty carefully.

MR. PRASAD: Thanks, Charles.

Siddharth?

MR. TIWARI: So, I would say one thing that we've learned in the last three or four years is that the feedback loops between financial sector, fiscal, real economy operate in both directions. And so when I look at things -- what is a banking sector problem if it becomes a financial sector problem -- it's not very far from a fiscal problem. So, I'm closer to Jack in that situation.

And this has actually made us look at our DSA again -- the debt sustainability analysis. It's been revamped fundamentally, in looking at enhanced coverage of risk -- whether there are contingent liabilities, quasar fiscal liabilities, they need to be looked at, and they need to be added.

So, I don't see this as being a sectoral issue, as much as risk-based coverage of liabilities.

MR. PRASAD: Thanks, Siddharth.

Anna?

MS. GELPERN: Right. So, just chiming in on banks -- we

actually do address this point directly. And if you'd look at the emerging doom loop literature -- I mean, the message, I think, is that banks are viewed very much through the sovereign lens, whether looking at the credibility of the sovereign as a backstop to the banks, but, also, looking at the sovereign and sovereign debt as an asset in the banking system.

So, truly, our position is, we're not going to solve the banking problem, but to the extent we help fix -- in the sense of making more certain -- the sovereign piece of it, we're certainly not hurting the banks -- and we may be helping it.

On Greece -- I think talking about statutory and contractual is not entirely helpful; it's like talking about Democrats and Republicans. You're immediately polarizing and, you know, kind of foreclosing analysis -- and just purely because of the history of these terms in this debate.

So, as a matter of fact, the Greek aggregation mechanism was a unilateral, retroactive, nonconsensual statutory change of private contracts -- which used voting thresholds, such as they were, that were far below anything that is either seen in the market or has been viably proposed. You can call it Tinkerbell, but that's what it was.

So, if, in fact, everyone is in agreement that sovereign debt structures should change to conform to the retroactive Greek collective action clauses, I think we can save a lot of time.

But I don't think there's agreement on that. I think that's precisely kind of where the debate is. And the debate is to be continued.

And finally, on collective action clauses -- collective action clauses are a very limited procedural device that tell you nothing about the substance of the debt restructuring outcome, and, as has become very clear in their current form, don't even tell you a whole lot about the process and the outcome, right?

Bond by bond, they might help on the margins; they certainly didn't fix Greece in any way, right? So, this is the foreign law traditional CACs.

So, we're all for CACs, but it's a baby step on a very long road.

And with that, I hand it over to my colleague.

MR. PRASAD: That's probably the first time I've heard a reference to Tinkerbell preceded by seven qualifiers.

Now Beatrice.

MS. di MAURO: Well, let me take the one about the interaction between the ESM and the IMF. Yes, we did think about that, and there are two ways in which you can address this. The one that you are mentioning is (inaudible) to IMF still be in the Troika, in this long-run regime. The answer is probably no.

You know, in this long-run regime, the ESM would be a much more fully-fledged institution, but there is another way that, you know, the IMF and ESM interaction -- which you also mentioned -- is, you know, how are they compatible, since countries will continue to be members of the IMF?

Well, you know, that could open a back door way off, undermining the proposal -- you know, the ESM is constrained in its official lending abilities, and countries could then turn to the IMF if that door was still open.

And one elegant way of closing that door is by, you know, having one seat of the euro area countries at the IMF, and then, of course, access to IMF resources would, at the euro area level, you know, be governed by the same kind of criteria as any other country.

And I think that is, actually -- you know, somebody mentioned that, you know, in the future, if everything works -- I think it was you, Charles -- if everything works in the euro area as now envisaged, then, of course, you know, questions like, you know, how do you deal with unsustainable buildups of private debt, and how you deal with booms and busts, and the implication of the banking system?

They are all independent instruments that are also being set in place to deal with these things individually, but we think that the

restructuring regime would serve, still, as something like -- not say concert, but maybe force line of defense against the incentive to actually socialize private debt -- because, you know, the countries will think about twice, whether they want to put themselves in a position where they have a jump in their debt ratios, which, you know, in very short time, takes them way above the upper threshold.

So, in that sense, it also reinforces disciplining effects of other mechanisms.

Now the criteria question -- you know, of course, the question is extremely valid. You can ask that of any number. You know, any number is always wrong. It can only be maybe -- or hopefully -- right on average.

You know, that's the probability of insolvency in Greece with debt -- probably, yes. Does the the vulnerability of countries to debt runs increase with debt levels? Well, probably, yes. Does the probability of disruptive events that (inaudible) especially if you are sitting in one currency union increase with debt levels? Yes.

So, you know, from this follows that, you know, there has to be some range in which you do want to be -- and that's probably not above 100 percent; it's probably lower than we thought in the past, you know, where debt sustainability was seen as something that, you know,

can be sustained at much higher levels in advanced countries.

Is 60 right? Well, probably not, but if you have the right number, that's great, and, you know, I would be happy to write it into a report; it's just that the Europeans have basically agreed on the number, and they're all working towards it.

So, you know, why use a number that is maybe a little bit more right -- maybe it's 72, rather than 60 -- but I wouldn't want to, you know, try to change all the fiscal framework in order to get 72, rather than 60.

MR. PRASAD: Last shot Jeromin.

MR. ZETTELMEYER: Okay, so I think at this point, probably everything that was asked has been addressed in form or the other, which means I probably shut up, but, of course, I still want to answer at least two points in my own words.

So, first, Nancy's point, which was also sort of implicit in what (inaudible) said, and then what Jack said about private versus public -- the difficulty to distinguish. So, let me rephrase it.

So, the question is, are you guys really not addressing the wrong problem in this report? Because you are obsessed with sovereign debt -- when, in fact, the main debt is corporate banking system.

Okay, so our answer to that is twofold. First, there are other

important problems in the world. There's also global warming, okay? There are different tools to address different problems, and, clearly, we have picked a problem that we do address -- and it doesn't mean we address everything, okay?

Having said that, there is a very critical sense in which our proposal contributes, also, to addressing the private debt problem, which is that when we put in these rules saying once your public debt exceeds a certain threshold, you can't get bailed out anymore unless you restructure.

We are not telling any country how you are getting to that high public debt; could be anywhere. Could be fiscally, could be because they didn't pay attention to the corporate system, could be because they didn't supervise their banks properly.

What we are telling countries is, once you are at those debt levels, no matter how you got there, you're on your own, unless you accept the restructuring.

And so this is why these proposals will produce good incentives more broadly, not just for sovereign debt management. So, in that sense, it contributes -- but, of course, you will need extra policy instruments, right? You will need macro-prudential instruments, right? You will need good regulation supervision of banking systems. So, all these things, we need, too.

And then the second point is, you know -- so yes, I think Greece was essentially statutory. And the way to think about our proposal for the eurozone is that it has two halves.

One half is this notion that, conditional on a super majority of creditors agreeing, in the context of an ESM-supported adjustment program to a debt restructuring, we are not allowing the holdouts to go after the sovereigns or after other creditors, right? That's one part of the proposal.

And that part is essentially simply the generalization of what was done in Greece for the domestic debt, to the entire eurozone debt. It is, in fact, a little more conservative, I should say, than what was done in Greece, because, as someone pointed out, you pointed out, the thresholds that we would apply to get super majority agreement are the euro CAC thresholds, which are 75 percent, not 2/3.

So, in that sense, we are actually a little more creditor-friendly in this proposal than what was done in Greece.

The other part of what we are proposing is that we are essentially telling the ESM, you know, when a country's in sufficiently bad shape, you have to require restructuring as part of the conditionality of your lending -- and that's the more controversial.

Thanks.

MR. PRASAD: Okay, thanks, gentlemen.

So, we should thank our distinguished panel for guiding through debates that I think we haven't heard the last of, ranging from "too little, too late," to "too much, too soon," from contractual to statutory, from rules to discretion.

And I think they've been very helpful in shedding light on these issues, and I think these are important things that the global economy's going to contain, and it's great that we have people on the frontlines, dealing with this in a very thoughtful manner.

So, thank you very much to the very distinguished panel, and thank you very much for coming.

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I, Carleton J. Anderson, III do hereby certify that the forgoing electronic file when originally transmitted was reduced to text at my direction; that said transcript is a true record of the proceedings therein referenced; that I am neither counsel for, related to, nor employed by any of the parties to the action in which these proceedings were taken; and, furthermore, that I am neither a relative or employee of any attorney or counsel employed by the parties hereto, nor financially or otherwise interested in the outcome of this action.

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