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TOWARDS BUILDING A FAIR AND ORDERLY INTERNATIONAL FRAMEWORK FOR SOVEREIGN DEBT RESTRUCTURING

AN AFRICAN PERSPECTIVE

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1.0 INTRODUCTION

The recent history of Sovereign Debt Restructuring (SDR) undoubtedly demonstrates the need for a reform of the international financial architecture. Not only have financial crisis and sovereign default become problems affecting developed and developing countries alike, these phenomena have also recast the focus on the question of whether SDR should be guided by a more formal process.

In the past decade, the world has witnessed a series of SDRs that have led to devastating results for citizens in and outside of the countries involved. In particular, the Greek SDR (the largest restructuring to date) and the messy Argentinean bond debt renegotiation arising from the 2001 financial crisis, present a strong case for the need to reform the SDR legal landscape. These problem-ridden restructurings highlight three key issues:

- There is a major of legal gap (non-system) in the international governance of sovereign default. Despite the unique nature of the debtor, a sovereign, and the complex issues involved, including sovereignty and human rights, the SDR landscape still experiences major gaps.
- At an international level, the absence of a uniform mechanism for SDR, has led in many cases of unfair results for debtors and well meaning creditors, through procedural inefficiencies and normative frameworks that do not prioritize fairness.
- Recent restructurings have also highlighted the new complexities that arise with SDR of bond debt, in particular with regard to the more disperse creditor structure, that were not present in the restructuring renegotiations held at the Paris Club or with multilateral development banks such as the International Monetary Fund (IMF).

In the African context, despite multilateral initiatives to provide debt relief, including the Paris Club, Heavily Indebted Poor Country program (HIPIC) in 1999 and the Multilateral Debt Relief Initiative (MDRI) in 2005, countries are again coming dangerously close to unsustainable levels of debt they had prior to these initiatives and some are already facing distress.[1] For Sub-Saharan Africa (SSA), not only is sovereign debt on the increase, but its nature of the debt is changing as countries turn to capital markets for funding and new bilateral partners such as China.

1 Various factors are contributing to debt distress on the continent including falling global commodity prices, local currency devaluations and foreign currency risk, debt mismanagement and the revelations of previously unknown debts. According to Fanwell Bokosi, the CEO of AFRODAD, aalready by early 2017 debt vulnerabilities are increasing in Burundi, Cameroon, Carpe Verde, Central African Republic, Chad, Djibouti, Ghana, Mauritania, Sao Tome and Principe, whilst Sudan and Zimbabwe are in debt distress.
See F. Bokosi, Halting the spawn of foreign debt' Freidrich Ebert Stiftung (31 July 2017) http://www.fes-connect.org/popular-posts/detail/halting-the-spawn-of-foreign-debt/

On the African front, restructuring of debt has always been a contentious issue especially in the context of official debt; however several African countries are now experiencing difficulties with the repayment of other types of debt, including bond debt and commercial debt. The most recent case is the infamous Mozambique secret debt saga that involved government guaranties that added approximately 20% to the country's foreign debt and the failure to make repayments on the country's Eurobonds in early 2017. Additionally, in 2011 Seychelles defaulted on a $230 million Eurobond following election disputes; Côte d'Ivoire missed a $29 million interest payment on a 2010 bond issue; Ghana has been facing debt difficulties, just to name a few.[2]

As such, with the changing landscape on the continent, the risks associated with the lack of a uniform international approach, reforming SDR is very much a priority issue for African countries, as it is for other developing countries like Argentina and developed counties. Further, not only is SDRs one of the most contentious issues in economic policy-making circles as well as within the civil society, but the United Nations General Assembly (UNGA) has placed SDR reform on its agenda in 2014.[3] Among the complex questions that international policy makers, governments and Civil Society Organizations (CSO) like AFRODAD now seek to answer is: how should future SDRs be conducted in a way that balances the interests of both debtors and creditors and that alleviates present flaws in the system?

In light of the above question, the objective of this paper is to explore the current challenges; current innovations that affect SDR and global reform proposals to create a new framework for SDR. The paper will also focus on the special circumstances of African countries and will subsequently provide food for thought from an African civil society perspective regarding these issues as a way to move the debate forward.

2 S Brooks, D Lombardi & E Suruma *African Perspective on Sovereign Debt Restructuring* (September 2014) CIGI Issues Paper No.47 2 https://www.cigionline.org/sites/default/files/no43_web.pdf .

3 See United Nations General Assembly, Resolution 68/304, *Towards the Establishment of a Multilateral Legal Framework for Sovereign Debt Restructuring Processes* http://www.un.org/en/ga/search/view_doc. asp?symbol=A/RES/68/304.

2.0 THE CURRENT "NON-SYSTEM" OF SDR: EVIDENCE OF GROWING PROBLEMS

Sovereign Debt Restructuring (SDR) is a process used to alter the key terms of sovereign debt contracts through negotiations between debtors and creditors. In effect, this process may either alter the maturity of the servicing of debt (debt rescheduling) or the nominal value of the debt and/or interest rate (debt reduction). At present, unlike corporate restructuring, SDR is not guided by any statutory framework. Instead, the restructuring process is conducted through a market based/contractual approach which comprises negotiations that are initiated by sovereign debtors. The duty of creditors to participate in such negotiations is however voluntary. In practice, these negotiations are complex and may sometimes be protracted depending on the number of creditors in the restructuring, on the complexities of each case and the presence or absence of a predetermined super majority threshold of creditors (collective action clause) for voting on the restructuring package.

Where the negotiations result in no agreement on the restructuring package or even prior to the conclusion of the restructuring process, disgruntled creditors may unilaterally institute legal proceedings at national courts or international arbitration bodies. Dispute resolution, especially during the restructuring process, is proving problematic as sovereign debtors become at the mercy of judges at foreign national courts and this process may have a disruptive effect on the entire restructuring and the debtor's ability to return to financial health. In effect, these national courts play a very ill-suited gap filling role (or what may be seen as a form of unintended rule-making), to compensate for the lack of a coherent international framework.[4] It is therefore unsurprising that over the past few decades, the debt restructuring process has been seen to be uncertain, excessively prolonged and resulting in adverse results for both creditors and debtor states.[5] Among these legal complexities are creditor co-ordination (in particular with respect to holdouts), and imbalances between the rights of creditors and debtors, the almost instant tradability of bond instruments and litigation that disrupts renegotiation.

The United Nations Conference on Trade and Development (UNCTAD) has grouped the challenges emanating from the present state of SDR into three broad categories.[6] Firstly, there is the issue of fragmentation or lack of coordination. In this respect, the lack of a structured and coherent approach to SDR is manifesting itself through (1) the

4 M. Goldmann & S Steininger, *A Discourse Theoretical Approach to Sovereign Debt Restructuring: Towards a Democratic Financial Order,* (November 2015) 15. On this issue, Gelpern correctly points out that "the rise of sovereign debt contract lawsuits in national courts exacerbated the problem: by mandate, courts pursue piecemeal resolution of contract disputes, not comprehensive resolution of financial crises". A Gelpern, Sovereign Debt: Now What? (2016) The Yale Journal of International Law Vol. 41: 2 89.

5 A. Krueger, *A New Approach to Sovereign Debt Restructuring,* International Monetary Fund (April 2002) IMF 1.

6 See UNCTAD, *Sovereign Debt Workouts: Going Forward – Roadmap and Guide* (April 2015) 3 - 4 http://unctad.org/en/PublicationsLibrary/gdsddf2015misc1_en.pdf.

multiplicity of forums officially tasked with solving SDR disputes, (2) incoherent legal interpretations emanating from the different legal forums and (3) the presence of multiple legal procedures.[7] These symptoms of incoherence are resulting in confusion, encouraging forum shopping and leading to great efficiency deficits. Resultantly, the line between much desired flexibility in the restructuring process and much needed global incoherence has to be more clearly demarcated, the absence of which is often resulting in harmful results, especially for citizens of debtor states.

Secondly, there is the too little too late problem, which occurs when a debtor state delays to initiate the restructuring process. Among the reasons behind the intentional or sometimes unintentional decision to procrastinate on SDR are the fear of stigmatization, the fear that a country will not be given a 'fresh start' to access finance on the international financial markets, insufficient information to determine that a restructuring is needed, uncertainty about the results of SDR and the debtor's electoral cycle.[8] Irrespective of the justification, the current system of SDR does not prompt sovereigns to restructure in a timely manner, especially when it is apparent that this would be the best action.[9] Therefore, it is truly important to create incentives that promote early restructuring without encouraging general misuse of such a system.[10]

The last broad challenge highlighted by UNCTAD is the lack of fairness in the current SDR landscape, that is leading to undue outcomes for both well meaning creditors and their over indebted sovereign debtors. Unfairness is a natural result of the procedural inefficiencies discussed above and a system that seems heavily reliant on goodwill. Historically, both creditors and debtors have contributed to unfair outcomes of the SDR process by perpetrating bad faith conducts; the former have done so through disregard for transparency and due process, while the later through unilateral decision making.[11] This notwithstanding, the biggest hindrance to a fair restructuring process has been the conduct of vulture funds, whose role and influence is increasing, as countries are moving away from syndicated bank loans and turning to capital markets as an alternative source of finance. This recent trend of using sovereign bonds has raised the number of creditors in SDR processes (sometimes in the thousands), thereby amplifying the divergence of their interests and making more space for vulture fund activities.

7 UNCTAD, ibid 3.
8 UNCTAD, ibid 4.
9 See M Guzman, J Antonio Ocampo, J E. Stiglitz (Eds), Too Little, *Too Late: The Quest to Resolve Sovereign Debt Crises,* Columbia University Press (2016) xiv.
10 See Kruger (note 6 above) 5.
11 See UNCTAD (note 7 above) 4.

The role of vulture funds in SDR has received criticism for their 'immoral' business model that is usually based on the exploitation of the carcasses of sovereign debtors for excessive profit making.[12] Vulture funds are generally private hedge funds that:

- Pursue distressed debt held by sovereigns debtors with limited legal capacities to raise legal defences;[13]
- Take advantage of the absence of regulations on the secondary capital markets;
- Systematically exercise their right to refuse to participate in a restructuring and instead litigate for the full value of bonds and penalties, thereby making exorbitant profits;
- Once favourable judgements have been obtained, they aggressively pursue the enforcement of the judgments; and
- Usually elect to operate in tax havens where banks apply strong secrecy rules.[14]

Various African countries have been targeted by vulture funds. The African Development Bank Legal Support Facility notes that the out of 25 judgements granted in favour of vulture funds (yielding approximately 1 billion United States Dollars), a majority are against countries that are regional members of the bank.[15] Among the cases against African countries include cases in national courts of the United Kingdom concerning the pursuit of Zambian distresses debt,.[16] litigation in the national courts of the United States and United Kingdome to recover distressed Liberian debt,[17] and litigation in the national courts of the United States and Hong Kong to recover DRC distressed debt.[18] Other countries that have been targeted by vulture funds include Angola, Burkina Faso, Cameroon, the Republic of Congo, Ethiopia, Ivory Coast, Madagascar, Mozambique, Niger, Sierra Leone, Tanzania, and Uganda.[19] These claims by vulture funds generally represent large portions of the Gross Domestic Product of debtor countries.

The effect of the activities of vulture funds globally and in Africa, is to undermine development efforts of debtor states, discourage well meaning creditors from

12 See EURODAD, *Tackling the Vultures* (September 2014) EURODAD Briefing http://eurodad.org/files/pdf/550a92e698c26.pdf . Also see AfDB, *African Legal Support Facility, Vulture Funds in the Sovereign Debt Context,* http://www.afdb.org/en/topics-and-sectors/initiatives-partnerships/african-legal-support-facility/vulture-funds-in-the-sovereign-debt-context/ and EC Stoica, *Sovereign Debt Restructuring and "Vulture Funds"* (2016) http://cks.univnt.ro/uploads/cks_2016_articles/index.php?dir=05_economics%2F&download=CKS+2016_economics_art.101.pdf.
The activities of vulture funds and their impact on human rights have been central to the work being conducted by the UN independent expert on debt and development and the UN Human Rights Council. In the *'Remarks by the Independent Expert on vulture funds and human rights at the 14th session of the Human Rights Council Advisory Committee',* (5 February 2015), in which he reiterated the legitimate concern that the legal ruling in the case between NML Capital Ltd. And Argentina may in effect erode the commercial incentive for creditors to participate in a restructuring and thereby encourage vulture fund activities. http://www.ohchr.org/Documents/Issues/IEDebt/IE_foreign_debt_side_event4March2015.pdf

13 In Africa this challenge of limited capacity in litigation necessitated the creation of the African Legal Support Facility (ALSF), an institution hosted by the African Development Bank. For a description of ALSF's mandate, see https://www.afdb.org/en/topics-and-sectors/initiatives-partnerships/african-legal-support-facility/

14 For an analysis of these issues please see pages 4 – 5 of the Report on *Report of the Human Rights Council Advisory Committee on the activities of vulture funds and the impact on human right* - A/HRC/33/54 , Human Rights Council Thirty-third session, (20 July 2016), https://documents-dds-ny.un.org/doc/UNDOC/GEN/G16/160/65/PDF/G1616065.pdf?OpenElement

15 AfDB African Legal Support Facility, *Vulture Funds in the Sovereign Debt Context* http://www.afdb.org/en/topics-and-sectors/initiatives-partnerships/african-legal-support-facility/vulture-funds-in-the-sovereign-debt-context/.

16 Camdex International Ltd. v. Bank of Zambia[1996] 3 All ER 431 (CA); [1997] CLC 714 (CA), Lordsvale Finance v. Bank of Zambia [1996] QB 752 and Donegal International v. Zambia[2007] EWHC 197 (Comm); [2007] 1 Lloyd's Rep. 397

17 Unreported case of Hamsah Investments Ltd. & Anor v. The Republic of Liberia Judgment of November 26, 2009 (unreported), Case No. 2008/587 High Court of Justice, London.

18 Democratic Republic of the Congo v. FG Hemisphere Associates LLC (No. 1) [2011] HKEC 747; [2011] 14 HKCFAR 95.

19 African Development Bank (n16 above).

participating in SDR and additionally to divert funds from the servicing of poverty reduction plans, healthcare, education and other social benefits to the servicing judicial awards. Thus the infamous question posed by Julius Nyerere in the mid-1980s as president of Tanzania – "Should we really let our people starve so that we can pay our debts? If African governments are really representing their people, they cannot accept conditions that would lead to more hunger, to social chaos, to civil war".[20] Although this question presents a very extreme context, the underlying message is clear – what is the balance between debt repayment (especially to vulture funds which purchase such debt at highly discounted rates on secondary markets) and the human rights and social obligations of states?

In answering this question, and as a result of pressure from the public and CSOs, Belgium has enacted groundbreaking legislation to counter predatory litigation of vulture funds by curbing disproportional/excessive legal claims by creditors who purchase debt at a fraction of the value of the debt.[21] What makes this law exceptional is that it incorporates human rights concerns and interests of citizens from debtor states, by requiring judges to consider the socioeconomic impact of payment in the debtor, amongst other factors.[22] This is just one of numerous anti-vulture fund national legislations that has been passes in the main financial centres in which the SDR litigation is instituted.

As a result of the challenges discussed above and despite the development of sophisticated tools to identify debt vulnerability, the risk of default at times may not be fully avoided. The question of how to resolve the complex task of SDR and what legal mechanism should perform the task remains generally unanswered and almost un-dealt with from an African perspective.

20 M. Black, A Cause for Our Times: Oxfam - The First Fifty Years, Oxfam and Oxford University Press (1992) 269.
21 On 12 July 2015 Belgium enacted a comprehensive law to curb activities of vulture funds- *'Loi relative à la lutte contre les activités des fonds vautours'.* This new law is more elaborate than the previous law enacted by Belgium *'Loi visant à empêcher la saisie ou la cession des fonds publics destinés à la coopération internationale, notamment par la technique des fonds vautours'* (6 April 2008).
22 UNGA, *Report of the Human Rights Council Advisory Committee on the activities of vulture funds and the impact on human rights* A/HRC/33/54 (20 July 2016) 12 https://documents-dds-ny.un.org/doc/UNDOC/GEN/G16/160/65/PDF/G1616065.pdf?OpenElement

3.0 TOWARDS A FAIR AND ORDERLY FRAMEWORK FOR SDR

There is a spectrum of approaches by academics and legal policy makers in the debate on the reform of the international finical architecture; however this study addresses two main approaches: the public law approach (international statutory approach) and contractual / free-market approach.[23]

3.1 Contractual innovations to SDR

The contractual approach, the present status quo in SDR, has experienced quite some popularity despite evident problems. This approach requires the strategic inclusion or modification of clauses in debt contracts. As discussed in the previous section, the SDR process experiences many challenges; however creditor coordination has received the most attention. The key innovations to debt contracts that have been proposed by proponents of the contractual approach such as the International Capital Markets Association's (ICMA), have revolved around creditor coordination.

A classical creditor coordination problem that arises during the SDR process is the holdout problem or the collective action problem. Holdouts transpire when a smaller group of creditors decline to accept a sound restructuring plan for larger pay-outs later.[24] A primary example of this is the infamous Argentine holdout. In 2005 and 2010 the Argentine government negotiated a restructuring package with over 92% of bond holders, who accepted what would be 70 % loss on the original value of their bonds, while the remaining minority creditors refused this deal. At the time of refusal their claim that was reportedly worth approximately US$6 billion, in 2016 was now worth US$20 billion.[25] In this instance, the holdout creditors (who happened to be vulture funds) are the winners, especially after successful litigation in New York District Court and Federal Court of Appeals has guaranteed them rateable payments when Argentina pays other bondholders.

Among the most important innovations to debt contracts to tackle this problem, is the enhanced collective action clause (CACs). CACs are clauses in debt contracts that set out the predetermined super majority of creditors for accepting the amendment of key terms in debt contracts. More advanced versions of these clauses may provide

23 Bohoslavsk provides a list of the different previous approaches proposed by international institutions, policy makers, academics:

- Statutory approach (IMFs 2001 Sovereign Debt Restructuring Mechanism (SDRM))
- *Ad hoc* approach (Sovereign Debt Adjustment Facility suggested by the Committee on International Economic Policy and Reform (Brookings Institute 2013); Sovereign Debt Forum (SDF), (Richard Gitlin and Bret House, Centre for International Governance Innovation 2014))
- Institutional approach (including Raffer's 2005 proposal for a Fair and Transparent Debt Arbitration Process; Paulus and Kragman's 2008
- Sovereign Debt Tribunal (UN expert group's International Debt Restructuring (A/63/838))
- Non-binding principles (non-binding Principles for Stable Capital Flows and Fair Debt Restructuring (Institute of International Finance 2004)

P Bohoslavsk, *Regional instruments a Fair and Transparent Debt-workout Mechanism* (2009) EURODAD 2 - 3 http://www.ohchr.org/Documents/Issues/Development/IEDebt/DebtRestructuring.pdf

24 SL Schwartcz, *Sovereign Debt restructuring: A model Law approach* 3

25 Financial Times, *Argentina to pay Italian 'holdout' creditors* (2 February 2016), https://www.ft.com/content/ee587988-c9e2-11e5-be0b-b7ece4e953a0

for aggregation of votes across various bond issues.[26]. The strategic inclusion of contractual provisions, such as CACs, does not fully resolve the abovementioned challenges, although they provide some level of relief for future restructurings. Despite this very welcome innovation various challenges still remain:

- Although CACs are being increasingly included in new debt instruments, there are still a substantial number of debt instruments that do not contain CACs.[27]

- Further, where the CACs are included in some debt instruments, do not always provide for aggregation across different issues of bonds.

In addition to modifications to CACs, the ICMA has also developed a model *pari passu* clause as a reaction to the broad interpretation of this clause in a judgement concerning NML Capital Ltd. versus Argentina decided at the U.S. New York Federal Court of Appeals in October 2012.[28] *Pari passu* is a latin phrase that means "equal footing". The pari passu clause is a standard clause found in many international bond contracts. The wording of these clauses may differ from contract to contract; however they have been commonly give a narrow interpretation and have been viewed as being aimed at preventing change of legal ranking of debt, for instance through enacting national laws to subordinate debt. However, despite how these clauses have been understood on the market, national judgements have recast the pari passu into the focus, due to a broader interpretation. In particular, the NML Capital case interpreted the pari passu clause to extend beyond the notion that debt will rank pari passu, to require that equal or rateable payments be made to holdout creditors. The effect of this is that vulture fund will receive full payment from the original value of their bonds even where a restructuring agreement has been reached with the majority of creditor whom accept loss on the original value of their bonds.

The NML Capital case is among the most contentious judgements arising from the Argentinean restructuring of 2005 and 2010. This case in particular has recast the spotlight on the potential tensions between judicial interpretation of debt instrument clauses and how these clauses have been commonly understood by debtors and creditors. Further, this decision shows how national courts can be used as a weapon in the hands of holdout creditors, to the detriment of both "erstwhile fellow bondholders" and sovereign debtors.[29] Although the full impact of this case on the bond instruments governed by New York Law is yet to be determined, it may prove to be potential legal impediments to future SDR.

26 See ICMA model CAC (August 2014), https://www.icmagroup.org/resources/Sovereign-Debt-Information/
27 In a 2014 study, the IMF noted that out of the foreign law bonds issued, from a total of about US$1.2 trillion foreign law bonds outstanding, approximately 25% do not contain CACs. Notably the IMF found that out of approximately US$500 billion (about 40 percent of all issuances) of a total outstanding stock of New York law bonds, 20% (US$100 billion) do not contain CACs. See IMF, The Fund's Lending Framework and Sovereign Debt, (22 May 2014) 30 https://ftalphaville-cdn.ft.com/wp-content/uploads/2014/06/SDR0614.pdf?mhq5j=e5
28 For the ICMA model *pari pasu* clause (August 2014) see: https://www.icmagroup.org/resources/Sovereign-Debt-Information/
29 L C. Buchheit and G. M Gulati 'Restructuring Sovereign Debt After NML v. Argentina' Capital Markets Law Journal Draft 8/7/16 (2016) 1.

3.2 In search for an international framework for SDR

Alongside with the contractual approach, another approach is the international public law approach, which calls for the creation of an international framework for SDR (whether in the form of soft or hard law instruments).

Two major milestones have been reached in the search for an international mechanism for SDR. The first of these milestones is the adoption of the United Nations General Assembly (UNGA) resolution "*Towards the Establishment of a Multilateral Legal Framework for Sovereign Debt Restructuring Processes*" on 9 September 2014.[30] This proposal comes over a decade after the IMF's failed proposal for the establishment of a Sovereign Debt Restructuring Mechanism under its auspices. Notwithstanding this failed attempt, the idea of an international rule of law for SDR, is again on the international agenda, although this time at the UN. Notably, of the countries that had the opportunity to vote for the resolution, 124 countries voted in favour (mostly developing countries), 11 voted against the resolution and 41 abstained from voting.[31] The debate between countries on this resolution revealed a rift between the developing and developing countries. Amongst the points of departure between developed and developing countries was whether the UNGA is in fact the relevant and qualified authority to determine matters of contemporary SoDR.

The second milestone in the establishment of an international framework for SDR occurred on 10 September 2015 when the UNGA passed resolution on "*Basic Principles on Sovereign Debt Restructuring Processes*".[32] This resolution requires that the following nine basic principles guide a SDR process:

- Sovereignty,
- Good faith,
- Transparency,
- Impartiality,
- Equitable treatment,
- Sovereign immunity,
- Legitimacy,
- Sustainability, and
- Majority restructuring.

30 Sixty-eighth General Assembly Plenary (107th Meeting), Resolution on Sovereign Debt Restructuring Adopted by General Assembly Establishes Multilateral Framework for Countries to Emerge from Financial Commitments (9 September 2014) https://www.un.org/press/en/2014/ga11542.doc.htm.
See Third World Network 'UN Adopts Landmark Debt Resolution on Principles for Sovereign Debt Restructuring (15 September 2015) http://www.cadtm.org/spip.php?page=imprimer&id_article=12201

31 UN, Resolution on Sovereign Debt Restructuring Adopted by General Assembly Establishes Multilateral Framework for Countries to Emerge from Financial Commitments, 9 September 2014, https://www.un.org/press/en/2014/ga11542.doc.htm

32 Resolution A/69/L.84 was adopted on, with 136 member States voting for, six against and 41 abstentions. http://unctad.org/meetings/en/SessionalDocuments/a69L84_en.pdf .

Similarly to the UNGA resolution on a multialreral legal framework mentioned above, the political debate on the adoption of the nine baisc principles also demonstrates that the divide between developing and developed countries is still a matter of fact. Notably, 136 states voted in favour of tthe adoption of the nine basic principls, while 6 voted against and 41 abstained from voting.[33] Of the countries that voted in favour, most were from Africa, Latin America, Asia and the Caribbean, while the countries that voted against include Canada, Germany, Israel, Japan, the United Kingdom and the United States.[34] Again, countries such as the United States, pointed out that the UN is not the correct forum for SDR and that, rather, the debate should be directed to the IMF, G20 or the Paris Club. Moreover, fears that these principles would undermine the principle of the sactity of contracts and the enforcement of contracts resulted in votes against the resolution.

Together with the lack of agreement between developing and developed countries, another issue affecting these principles is that both their interpretation and understanding of how they should be applied in practice still remain unclear. The resoluton provides some very basic guide on the interpretation of these principles however these principles in practice will be interpretation on a case by case basis by debtors and creditors of a spesicfic restructurings, potentially resulting in much more confusion. The true implicatons of these principles will however be felt when they are implemented and once debtors and creditors begin to measure their impact on restructurings. In the end, while this resolution is a step in the right direction as it creates the basic normative framework upon which the restructuring process will be founded on, they still require further development and the principles are not a susbsitituion for a formal mechanism for SDR.

33 UNCTD, United Nations General Assembly adopts basic principles on sovereign debt restructuring, 11 September 2015, http://unctad.org/en/pages/newsdetails.aspx?OriginalVersionID=1074
34 UNCTAD, *ibid*.

4.0 AFRICA'S SOVEREIGN BONDS: A DEVELOPMENT OPPORTUNITY OR A NEW TRAP

4.1 The flow of African sovereign bonds

The new millennium has brought African countries into a new era of their political and economic development, especially with respect to its sovereign debt. The unsustainable debt levels, possible default and renegotiation of sovereign debt is among the leading legal and economic issues threatening African countries despite previous initiatives to reduce the continent's debt levels. In 1999, the international community responded to Africa's unsustainable debt burden by initiating the HIPC Initiative, a debt relief program aimed at the reduction of unsustainable debt levels, encouraging policy and legal reform and the achievement of the then UN Millennium Development Goals. Surprisingly, the continent's debt levels are again rising.

In the last decade, several developing Sub-Saharan African (SSA) countries have started financing their public spending through the issuance of mostly US dollar-denominated sovereign Eurobonds. The new trend has been motivated by the 2007-08 global financial and economic crisis, which on one hand, had resulted in the conspicuous reduction of official aid flows to African recipients. On the other hand, the financial crisis had made western sovereign bonds less profitable, despite being considered less risky investment options. As such international private investors sought new and promising, yet more risky, investment frontiers.

When in 2006 Seychelles issued a $200 million Eurobond,[35] it was the first issuance of a sovereign bond in the history of SSA. Since then, between 2007 and 2015, another 12 SSA countries have issued Eurobonds (see Table 1 below).

35 M. Olabisi, H. Stein, Sovereign bond issue: *Do African countries pay more to borrow?,* Journal of African Trade 2 (2015) 87-109.

Table1. List of African sovereign bond issues: 2006-2014

List of African sovereign bond issues: 2006-2014					
Country	**Year**	**Coupon type**	**Coupon at Issue**	**Issue date**	**Tenor**
Cote d'Ivoire	2009	Step-up	5.75	31-Dec-09	23
Cote d'Ivoire	2014	Fixed	5.375	23-Jul-14	10
Congo	2007	Step-up	3.5	30-Jun-07	22
Ethiopia	2014	Fixed	6.25	11-Dec-14	10
Gabon	2007	Fixed	8.2	12-Dec-07	10
Gabon	2013	Fixed	6.375	12-Dec-13	11
Ghana	2007	Fixed	8.5	4-Oct-07	10
Ghana	2013	Fixed	7.875	7-Aug-13	10
Ghana	2014	Fixed	8.125	11-Sep-14	12
Kenya	2014	Fixed	6.875	24-Jun-14	10
Kenya	2014	Fixed	5.875	24-Jun-14	5
Namibia	2011	Fixed	5.5	3-Nov-11	10
Nigeria	2011	Fixed	6.75	28-Jan-11	10
Nigeria	2013	Fixed	5.125	12-Jul-13	5
Nigeria	2013	Fixed	6.375	12-Jul-13	10
Rwanda	2013	Fixed	6.625	2-May-13	10
Senegal	2009	Fixed	8.75	22-Dec-09	5
Senegal	2011	Fixed	8.75	13-May-11	10
Senegal	2014	Fixed	6.25	30-Jul-14	10
Seychelles	2006	Fixed	9.125	3-Oct-06	5
Seychelles	2010	Step-up	5	1-Jan-10	16
Tanzania	2013	Floater	6.332	8-Mar-13	7
Zambia	2012	Fixed	5.375	20-Sep-12	10
Zambia	2014	Fixed	8.5	14-Apr-14	10

Table extrapolated from Olabisi and Stein (2015)

In addition to the increased number of SSA countries issuing Eurobonds, some of these issuances are oversubscribed. By way of illustration, when Ghana issued its first $750 million Eurobond in 2007, it was four-fold oversubscribed, receiving $3.2 billion in bids.[36] Ghana was amongst the countries that had benefited from very recent public debt relief through the HIPC initiative, but, notwithstanding its previous difficulties in servicing debt, its profile was seen as favourable within the international investment landscape, as the oversubscription demonstrates. The same was the case in 2014 in Kenya (the $2 billion offer was oversubscribed four-fold), Senegal (the $0.5 billion offer was oversubscribed eight-fold) and Cote d'Ivoire (the $750 million offer was oversubscribed

36 See J. E. Tyson, *Sub-Saharan Africa International Sovereign Bonds,* Part I. Investor and Issuer Perspectives, Overseas Development Institute, (January 2015) 6 https://www.odi.org/sites/odi.org.uk/files/odi-assets/publications-opinion-files/9435.pdf

six-fold).[37] Between 2006 and 2015, SSA countries have issued $24 billion of Eurobonds in the international capital market, a figure that is $35 billion when interest rate payments are included (see Table 2 below).[38]

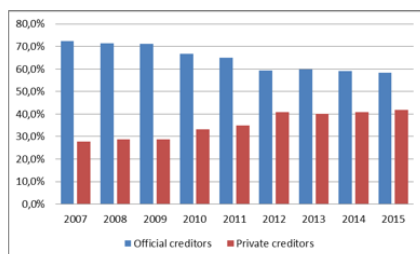
Table 2. African Countries and their Eurobond issuances since 2007 (in US millions).

COUNTRY	2007	2010	2011	2012	2013	2014	2015	TOTA
Ghana	750				750	1,000	1,000	3,500
Gabon	1,000				1,500			2,500
DRC	454							454
Cote d'Ivoire		2,300				750		3,050
Senegal			500			500		1,000
Tanzania					600			600
Nigeria			500		1,000			1,500
Namibia			500					500
Angola				1,000				1,000
Zambia				750		1,000	1,250	3,000
Mozambique					850			850
Rwanda					400			400
Kenya						2,000		2,000
Ethiopia			1,500	1,000		1,500		4,000
Seychelles	30	168						198
	2,234	**2,468**	**3,000**	**2,750**	**5,100**	**6,750**	**2,250**	**24,552**

Table extrapolated from The Conversation (2016)

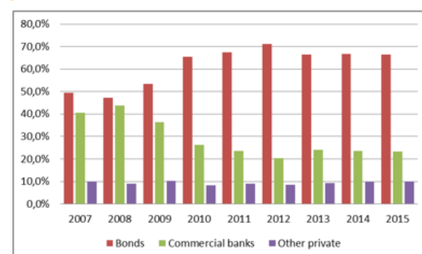
Although Africa as a region constitutes a smaller share of global sovereign bond market, the flow of sovereign bond issuances by countries in the region is so conspicuous that the composition of African public debts is slowly tilting towards a predominance of bonds, or more generally private creditors, as opposed to official creditors. The two figures below can best demonstrate this phenomenon. As shown in Figure 1, from 2007 to 2015, the weight of private creditors within the SSA countries public debt has grown from 28% in 2007 to 42% in 2015. If this growth is maintained, it is very likely that in the next decade private creditors will form a larger share of Africa's debt, as opposed to official creditors. Yet, within the private creditors' basket, in the same span of time, the weight of bonds has remained relatively high. This trend is shown in Figure 2 below. From 2007 to 2015, the composition of debt owed by SSA countries to private creditors predominantly consists of bonds compared to commercial banks: from 49% in 2007 to 67% in 2014.

Figure 1. Evolution of SSA Countries' public debt (2007-2015)



Source of data: The World Bank, International Debt Statistics (Created by Francesco De Bonis)

Figure 2. Evolution of SSA Countries' private creditors (2007-2015)



Source of data: The World Bank, International Debt Statistics (Created by Francesco De Bonis)

37 See J. E. Tyson ibid. Also see: Par. E. Tyson, *Part II. Risks for Issuers,* Overseas Development Fund, (January 2015) https://www.odi.org/sites/odi.org.uk/files/odi-assets/publications-opinion-files/9434.pdf

38 The Conversation, *Africa's ticking time bomb: $35 billion worth of Eurobond debt,* May 2016 https://theconversation.com/africas-ticking-time-bomb-35-billion-worth-of-eurobond-debt-59404

4.2 The complexity of bond debt

As the flow of African bond issues has become more widespread,[39] it is worthwhile to assess the drivers of these increased issuances of sovereign bonds. African countries have a past of excessive indebtedness that has resulted in the divergence of important and limited resources from social and economic development to debt and interest repayment. This is also deemed to be among the factors slowing the continent's development efforts. In the opinion of many analysts, there is a real risk that Africa's sovereign debts will return to pre-HIPC levels.[40]

Among the pull factors for the move towards bond debt are the terms of the conditions of lending – maturity, interest rate and the lack of conditionality. Despite the lack of conditionality in sovereign bond lending – the terms of lending are more expensive and more risky than concessional lending which may come with conditionality. Official loans carry an interest rate of approximately 1.6% on average and have an average maturity of 29 years.[41] Private loans to sovereigns instead carry an average interest rate of 6% and maturity of 11 years.

Bonds present various risks for African countries. Firstly, their terms usually translate into larger repayment over shorter periods. In addition, sovereign bonds are issued in foreign currency – mostly US dollars – which comes with foreign currency risks when local currencies depreciate.[42] Private debt especially bond debt is generally guided by the need for higher returns more quickly. Therefore, such investments are more likely to be guided by a more reckless attitudes (no due diligence on the part of creditors), with little consideration for the social and political implication of the borrowing or potential default. As such, terms of SDR when and if it does occur, may be made at a very high cost, especially to citizens of the debtor state.

Additionally, African economies are still very vulnerable to international shocks, such as international fluctuations of commodity prices, as their economies heavily rely on unprocessed raw material such as oil, coal etc and are generally still at early stages of diversification. Their capacity to generate the financial and currency resources in the short term to repay foreign currency denominated debt, may prove difficult. Finally, many countries may face challenges with this new form of borrowing due to weak fiscal, budgetary and debt management, as well as the absence of good governance.

39 See also: M. Macagni et al., *Issuing International Sovereign Bonds. Opportunities and Challenges for Sub-Saharan Africa,* African Department, International Monetary Fund (2014). and
A. Sy, *Trends and Development in African frontier bond markets,* The Brookings Institution (March 2015) https://www.brookings.edu/research/trends-and-developments-in-african-frontier-bond-markets/.

40 JE. Tyson , *ibid* (note37 above). Also see P. Collier , *Attracting international private finance for African infrastructure,* Journal of African Trade I (2014) 37-44. See also: The Conversation, *Ibid (note 31 above)*, A. Paul, *Africa Debt Rising*, African Research Institute (January 2015) https://www.africaresearchinstitute.org/newsite/publications/africa-debt-rising-2/, and W. Anzetse, *What's with all these international sovereign bonds being issued by African governments?,* The East African (July 2014) https://asokoinsight.com/news/whats-international-sovereign-bonds-issued-african-governments.

41 The Conversation, ibid (note 41 above).

42 *Foreign Exchange Risk* refers to risk of repaying interests at a much higher cost, because, as the bonds are issued in foreign currency and the possibilities of the devaluation of domestic currencies are very high, the money issuers will have to pay to dispose of that amount of foreign currency will be enormous. However, literature is pretty much divided on this aspect, mostly with respect of the real amount of domestic resources' loss needed to repay foreign currency-denominated obligations. This phenomenon is also referred as *dollarization* of the external debt.
See J E. Tyson, Ibid (note 37 above), A. Sy, Ibid (note 40 above) and M. Macagni et al (note 40 above).

The risk of African sovereign bonds is becoming more apparent as investors and debtors begin to sober from the very high expectations that come with the 'Africa rising narrative', as opposed to sound market strategy.[43]

4.3 Issuer motivations and first implications

The market of African sovereign bonds is however still small as compared to the overall world market. In 2011, 25% of the bonds issued by developing countries came from SSA countries. Yet, if South Africa is excluded, this drops to 2%.[44] Not all SSA countries are participating in the bond market. Countries that are issuing bonds are those that can meet the requirements of international investors. In this regard, beyond the credit rating – that usually ranges around 'Bs', investors are attracted by what they perceive as larger, faster growing economies, with positive future growth projections and have a more dominant position in the worldwide export market (such as the SSA countries listed in Table 1 above). In addition, investors are also attracted by countries that they perceive to have political stability, sound macroeconomic features like a contained Debt-GDP ratio and stricter fiscal policies.

For African countries issuing bonds, the primary driver is the growing need for financial resources meant to boost economic, social and infrastructural development. In attracting finance to the continent, it should be noted that in addition to the drop of official aid flows to Africa, domestic borrowing does not present an alternative source of finance due to the still-very-high costs.[45] The second key driver relates to the debt relief strategy. Many African countries have issued bonds within the framework of debt restructurings. As data shows (Figure 3 and 4 below), the immediate macroeconomic results after African sovereign bonds issues is not straightforward and definitely needs to be viewed on a case by case basis. As shown in Figure 3 below, Ghana, Namibia, Nigeria and Senegal - that had issued bonds explicitly to finance infrastructure projects – have all in recent years experienced an increase of their primary deficit - a reduction of the primary expenditures and an increase of the public debt.[46] Only Zambia has experienced slightly different results after the issue of bonds with a slight increase in its expenditure.[47] These are four examples that feed the fear for over indebtedness that can further harm and undermine social development of the continent.

43 This might explain the higher interest rates charged to African governments with respect of the world average. Even on this topic, literature is very much divided. Some state that African countries are actually paying an *African Premium* that is an interest rate on bonds that is higher than for other developing countries with same macroeconomic conditions. Some instead believe this *premium* is the right reflection of the current macroeconomic conditions. See
See also: A. Presbitero et al., *International Sovereign Bonds by Emerging Markets and Developing Economies: Drivers of Issuance and Spreads,* International Monetary Fund, WP/15/75.

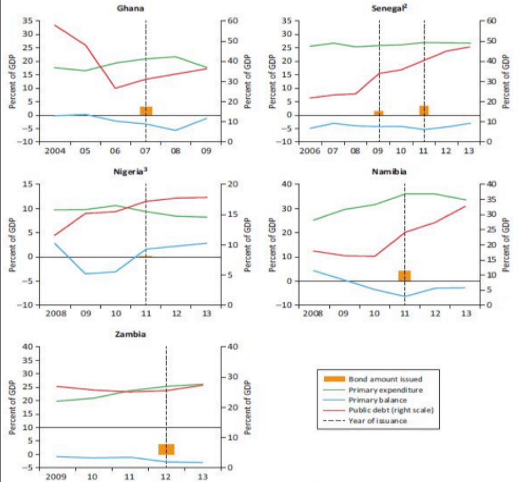
44 Macagni et al., *ibid (note 32 above).*

45 External borrowing in foreign currency is currently much more cheaper than domestic borrowing in local currency: in 2013, in Ghana local currency bonds could be issued at 23%, while the foreign currency interest rate was 4,3%. See A. Sy, *ibid (note 40 above).*

46 All these macroeconomic topics are expressed as percentage of GDP.

47 For a case by case analysis of each African issuance, See Olabisi and Stein, *ibid* (2015). And: Macagni et al., *ibid* (2014)

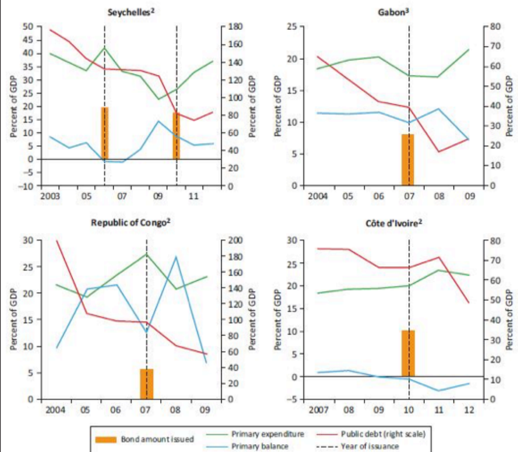
Figure 3. Sub-Saharan Africa: Primary Fiscal Balance, Expenditure, and Public Debt-Cases other than Debt Restructuring[1]



Sources: IMF, African Department Database; and IMF staff estimates and projections.
[1] South Africa is not included.
[2] Part of the proceeds from the bond issued in 2011 was used to exchange and repurchase the bond issued in 2009.
[3] Nigeria's bond amount issued in 2011 is 0.2 percent of GDP.

Figures extrapolated from Macagni et al. (2014)

Figure 4. Sub-Saharan Africa: Primary Fiscal Balance, Expenditure, and Public Debt-Cases Involving Debt Restructuring[1]



Sources: IMF, African Department Database; and IMF staff estimates and projections.
[1] Seychelles and Côte d'Ivoire issued small amounts of bonds in 2007 and 2012, respectively, which are not presented in the figure. South Africa is not included.
[2] In the case of Seychelles in 2006, the proceeds were used to clear external arrears to some multilateral and commercial creditors and to repay a collateralized loan. In the other cases, bonds were issued as exchange offers on their defaulted debts.
[3] The proceeds were used to repay outstanding debt to the Paris Club.

Figure extrapolated from Macagni et al. (2014)

5.0 THE AFRICAN PERSPECTIVE ON SOVEREIGN DEBT RESTRUCTURING: FINAL CONSIDERATIONS

Based on the study above, this paper makes the following final considerations:

- *Africa's debt new debt burdens are of great concern, especially in the absence of a fair, transparent and efficient way to conduct SDR*

Africa is at a critical shift in sovereign debt governance - on the one hand, the nature of the bilateral creditors is increasingly shifting from the traditional Paris Club countries, to new bilateral players including China as well as the capital markets. On the other hand, sovereign debt throughout the continent is increasing. This necessitates a fair and efficient mechanism for SDR. Taking into account the short time span within which African countries are accumulating bond debt, it is worrying what the future of the continent holds in this new era.

Indeed African countries are becoming more integrated in international markets; however the future hope is that African countries will be able to finance their development, reduce their debt burden, increase their role as world exporters and further develop their own domestic bond markets. The present reality however is that, as Christine Lagarde, managing director of IMF, has pointed out, African governments should not excessively expose their public debts to international private creditors by issuing sovereign bonds.[48] Not only is there a potential for more SDRs in SSA, but the process is increasingly becoming complex depending on the nature of the debt instruments and the creditors involved. In the absence of a policy co-ordination on SDR or a global sovereign bankruptcy regime, bond and other sources of commercial finance to SSA countries may lead to more harm than good in cases of financial strain or default.

- *The continent is not sufficiently featuring in the international debate on SDR*

Brooks, Lombardi and Suruma, whom are among the few authors that consider the African perspective on SDR, express the view that despite the large number of debt restructuring on the continent, the African perspective have not featured prominently to the international debate.[49] One reason for this is that the continents traditional source of finance has been official debt. Notably this is slowly changing. Africa may not be the leading player on the sovereign bond market, but it does require some level of special consideration.

48 See The Conversation, *ibid* (note 41 above).

49 S Brooks, D Lombardi & E Suruma, African Perspective on Sovereign Debt Restructuring' (September 2014) CIGI Issues Paper No.47 2 https://www.cigionline.org/sites/default/files/no43_web.pdf.

Although debt crises impacting developed and developing alike in very adverse ways, but the developing countries find themselves more vulnerable and African countries even more so. For many countries, SDR results in poor outcomes, however this is especially so for low income SSA countries.[50] Not only would African countries suffer most from the great human costs of a problematic SoDRs, problematic SDR may lead to more negative outcomes for the continent. As such the reform of SDR requires solutions that takes into account the unique developmental needs of developing countries in general and Africa in particular.

- *There is room for, and it is almost imperative that civil society organizations (CSOs) play a bigger role*

The UN Monetary Consensus on Financing for Development has found that the search for sustainable debt workout mechanism should include all relevant stakeholders.[51] Already CSOs have played a leading role in advancing previous debt relief initiatives such as the HIPIC and MDRI.[52] Recent events however present a unique opportunity for African CSOs in particular to play a greater role in determining the policy direction that the continent should take when it comes to sovereign debt and bond debt in particular.

African CSOs should play a greater role in the debate that will formulate one of the most important policies and laws in international finance, and that will affect the future of the continent. Their role may include engaging with their governments, directly engaging at the relevant international forums and very importantly, disseminating the complex issues of sovereign debt, debt management and SDR to the grass root levels. Finally, the adoption of the UN Basic Principles also presents an opportunity for SCOs to act as watchdogs during a restructuring process, especially where there are large restructurings.

- *The role of domestic legislation should not be underestimated, while international solutions are sought*

Though there have been significant advancements made to resolve the various problems in SDR, the contractual approach does not copiously resolve these issues. As such, from an African perspective an international mechanism would be preferred, but political realities cannot be underestimated.

50 MLJ. Wright, *Sovereign Debt Restructuring: Problems and Prospects* (2012) Review 2 Harvard Business Law 153 156.
51 UN Monetary Consensus on Financing for Development (The final text of agreements and commitments adopted at the International Conference on Financing for Development Monterrey, Mexico, 18-22 March 2002) 19 http://www.un.org/esa/ffd/monterrey/MonterreyConsensus.pdf
52 UNCTAD, *Think Tanks /Civil Society,* http://unctad.org/en/Pages/GDS/Sovereign-Debt-Portal/Sovereign-Debt-Links-4.aspx

Indeed a lot of focus has been placed on this well desired international reform. Notwithstanding, the present reality is that a workable legal framework will be more difficult to achieve at the level of international organizations due to state sovereignty. One cannot ignore the international political economy, the rift between developing and developed states and what this rift means when it comes to the formulation of an international mechanism for SDR. In particular, what will be the political violability of the UN's SDR resolutions and what will be the effect be if countries that hold the world's international financial centres are not on board? Will the UN's efforts follow the same stillborn fate as the IMF's proposed SDR Mechanism?

Resultantly, the role of voluntary international standards and national legislations should not be underestimated. Although, standards such as the UN Basic Principles fall short of a fully formed mechanism, they present a normative base for future SDR law. In addition to this normative base, a stronger focus should be given to shared responsibilities of debtors and creditors and direct integration of human rights obligations in the restructuring process.

With respect to national legislations, they have the potential to play a role in alleviating particular individual issues faced in the SDR architecture, for instance the vulture fund problem. Already as a result of the activities of CSOs and public outcry, some countries have recently enacted anti-vulture fund laws, including Belgium. These kinds of legislation will only be effective if they are passed in jurisdictions that are preferred for SDR dispute resolution. These do not fully solve the problem of vulture funds but provide more short term options. As such African countries should take these national legislations into account when determining the governing law and the jurisdiction of dispute resolution of sovereign debt matters.

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