PRINCIPLES

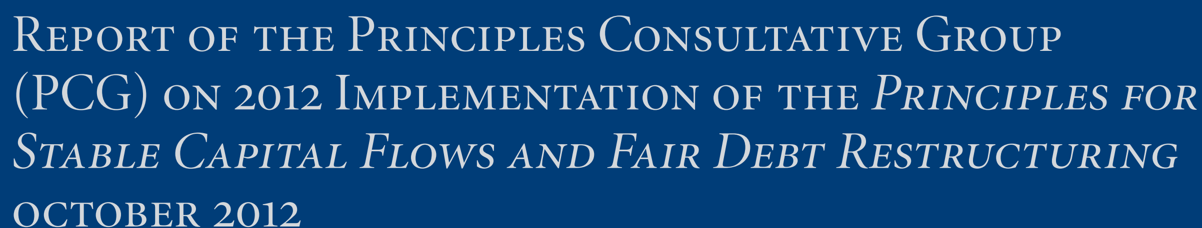
FOR STABLE CAPITAL FLOWS AND FAIR DEBT RESTRUCTURING

Report on Implementation
by the
Principles Consultative Group

With Comprehensive Update on
Investor Relations Programs
and Data Transparency

OCTOBER 2012

TRANSPARENCY   COOPERATION   GOOD FAITH   FAIR TREATMENT



Report of the Principles Consultative Group (PCG) on 2012 Implementation of the *Principles for Stable Capital Flows and Fair Debt Restructuring*

October 2012

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I. Overview

The global economy has slowed over the past year, with the sovereign debt and banking crisis in several Euro Area countries continuing to be a significant source of market turmoil and downside risks. The Euro Area is currently struggling to recover from a mild recession, while growth in the United States has been weak. Emerging markets, particularly in Asia, continued to be the only robust part of the global economy.

Overall, real GDP in the Euro Area as a whole is projected by the Institute of International Finance (IIF) to decline by 0.4% in 2012 and to increase marginally (by 0.5%) in 2013, with major declines in the problem countries and modest gains in the core countries such as Germany. The intensifying bank-deleveraging process in the Euro Area and the associated fragmentation of sovereign debt and bank-funding markets along national lines have contributed to a sharp slowdown in bank credit expansion to the private sector to 0.5% in the year to July 2012. The weakening demand in the Euro Area has contributed in turn to a steep decline in the growth of exports by emerging markets, particularly those in Asia. Growth in mature economies and emerging markets is also projected to slow during 2012, to 1.1% and 4.8%, respectively, with a modest pickup in 2013, to 1.3% and 5.4%, respectively. World growth would thus ease to 2.4% in 2012 and 2.8% in 2013.

However, these prospects are subject to sizable downside risks, emanating mainly from potential delays in putting in place the expected policy corrections in the Euro Area and in addressing the looming "fiscal cliff" and debt ceiling risks projected on current policies in early 2013 in the United States. In addition, several key emerging market countries are still in the process of engineering a soft landing.

Slow growth and risk factors emanating from the evolving situation in the Euro Area and other mature economies, in particular continuing deleveraging and financial fragmentation mainly in Europe, have contributed to volatile net private capital flows to emerging markets, in particular trade financing. According to the October 2012 estimates by the IIF, net private capital flows to emerging markets fell from $1,110 million in 2010 to $1,063 million in 2011 and will likely decline further to $1,026 million in 2012, with a modest recovery to $1,100 million in 2013.

The ongoing sovereign debt crises in the Euro Area over the past two and a half years are the first sovereign debt crises in mature market countries in recent decades. Several crisis management and resolution measures have been implemented, including the establishment of the European Financial Stability Facility (EFSF) and its successor, the European Stability Mechanism (ESM), which has helped fund adjustment and support programs for Greece, Ireland, and Portugal, with additional assistance envisaged for Cyprus and Spain (for bank recapitalization), and the negotiation of private sector involvement (PSI) in Greece, culminating in an unprecedented voluntary sovereign debt exchange in March 2012. In addition, major new policy initiatives have been introduced by the Euro Area authorities, including the agreements reached at the Euro Area Summit on June 29, 2012, to launch a single bank supervision mechanism led by the European Central Bank (ECB) as a first step toward the establishment of a banking union and possible direct ESM recapitalization of Euro Area banks, and also the ECB decision in early September on the launching of a new initiative for secondary-market purchases of the bonds of Euro Area member countries that agree to appropriate conditionality (Outright Monetary Transactions) on *pari passu* terms with similar bond holders. These measures have raised expectations that the Euro Area authorities are making significant progress in banking and fiscal integration to stabilize market conditions.

Although such crisis resolution efforts have contributed importantly to containing the sovereign debt crisis, they have also revealed serious problems that need to be considered by the international financial community for drawing useful lessons

in the future, especially because the key to resolving crises is to restore a sovereign borrower to international capital markets. These problems included

- Shortcomings by both public and private sectors in crisis prevention practices in the years leading to the eruption of the Greek sovereign debt crisis;
- The appropriate design of official adjustment programs that would balance fiscal consolidation and reforms with financing and growth support measures over a suitable time frame;
- The historic voluntary sovereign debt exchange for Greece, while having been negotiated largely, but not totally, in accordance with the guidelines set forth by the *Principles*, has presented a series of important issues that need to be resolved. These include the role of international laws and jurisdictions (i.e., English and New York laws) in the issuance of traditionally "domestic" sovereign securities, in the context of a sovereign debtor changing domestic law to modify terms and conditions of bond contracts; the problem of subordination of private investors by official bodies as exhibited in the Greek debt exchange or claimed by the ESM Treaty; and the use of collective action clauses (CACs), in particular the retroactive insertion of collective action mechanism (similar to CACs), aggregation, and exit consent.

Despite these unique features, the crisis prevention and resolution problems raised by the Euro Area sovereign debt crisis are reminiscent in several respects of the experience with debt crises in Latin America and other emerging markets over the previous three decades.

The *Principles for Stable Capital Flows and Fair Debt Restructuring* were in fact conceived in the aftermath of the sovereign debt crises in Latin America, Asia, and Russia. They constitute essentially a voluntary code of conduct between sovereign debt issuers and their private sector creditors that was agreed to in 2004 and endorsed by the G20 Ministerial Meeting in Berlin in November 2004 (see Annex I). Until October 2010, the *Principles* applied only to sovereign issuers in emerging markets, but their applicability has since been broadened to encompass all sovereign issuers (on a voluntary basis), as well as cases of debt restructurings by nonsovereign entities in which the state plays a major role in influencing the legal and other key parameters of debt restructurings.

The *Principles* incorporate voluntary, market-based, flexible guidelines for the behavior of sovereign debtors and private creditors with a view to promoting and maintaining stable capital flows and supporting financial stability and sustainable growth. The *Principles* promote crisis prevention through the pursuit of strong policies, data and policy transparency, and open communication and dialogue with creditors and investors (particularly under investor relations programs [IRPs]), and effective crisis resolution through *inter alia* good-faith negotiations with representative groups of creditors and fair treatment of all creditors.

The *Principles*, as a voluntary code of conduct, depend for their implementation on the good will of the debtors and creditors concerned, as well as the peer pressure exercised by two informal governing or overseeing bodies—the **Group of Trustees** and the **Principles Consultative Group (PCG)**.

The support by the Euro Area authorities and institutions and by the International Monetary Fund (IMF) of a voluntary debt exchange agreement for Greece reached through good-faith negotiations with private creditors consistent with the *Principles* has demonstrated and underscored the validity and usefulness of resolving even the most difficult sovereign debt problems in a manner consistent with the cooperative, market-based guidelines established by the *Principles*, with major benefits not only for the parties directly involved but also for the Euro Area as a whole and global financial stability in general.

More broadly, the experience since the launching of the *Principles* in 2004 has demonstrated the benefits that result from an effective implementation of the *Principles* in helping safeguard access to private external financing at a time of exceptional

stress in the global financial system (see Box 1). Countries with strong policy performance and active IRPs have clearly done well relative to others during the recent period of market turbulence.

Against the challenging global policy setting outlined above, the discussions over the past year among the members of the PCG—which includes senior officials from developed and emerging market countries, as well as senior bankers and investors—have continued to focus on the evolving policy and institutional setting in the Euro Area and the intensified efforts to conclude a voluntary debt exchange for Greece. In addition, the PCG monitored closely the changing economic situation, reform efforts, and relations with private sector creditors and investors in Iceland, Ireland, and other peripheral Euro Area countries. The PCG also reviewed the debt restructuring experience of St. Kitts and Nevis, a small island economy in the Caribbean, that concluded a comprehensive voluntary debt exchange deal with its private creditors at the same time as Greece did, that was also consistent with the *Principles*. In addition, the PCG was kept informed of further developments in the ongoing debt restructuring efforts of Iceland and Côte d'Ivoire. Since March 2012, however, the PCG has reviewed frequently the unfolding debt restructuring situation in Belize, which has raised

Box 1. Benefits of Implementing the *Principles*

The *Principles'* overriding strength is that they incorporate voluntary, market-based, flexible guidelines for the behaviors and actions of debtors and creditors, which have been developed by all concerned parties. The main benefit for the system as a whole is their proactive and growth-oriented focus, given that the *Principles* are operative not only after a crisis has occurred, but also during times of diminished market access and early stages of crisis containment.

The *Principles* also yield substantial shared benefits for emerging market and other sovereign issuers and their creditors. They can reduce debtor country vulnerabilities to economic or financial crises, as well as the frequency and severity of crises, by promoting:

- Information sharing and close consultations between debtors and their creditors to provide incentives for sound policy action in order to build market confidence, thus ensuring stable capital flows to these countries and preserving financial stability.
- Enhanced creditor–debtor communication by encouraging debtors to strengthen investor relations (IR) activity on the basis of market best practices and encouraging investors to provide feedback. IR practices help enable policymakers to make market-informed policy decisions.
- Early corrective action through sound policy-making, stimulated in some cases by intensified IR or based on direct consultations between the debtor and its creditors.

In cases where debt restructuring is deemed unavoidable, the *Principles* encourage cooperation between debtors and creditors toward an orderly restructuring based on engagement and good-faith negotiations toward a fair resolution of debt-servicing difficulties. Such actions could accelerate a country's restoration of market access and economic growth.

Through these cooperative actions, the *Principles* have underpinned a sustainable and healthy flow of private capital to emerging market economies, facilitating needed investment for long-term growth. In addition, cooperative action and enhanced creditor–debtor communication are consistent with the implementation of debt relief programs supported by multilateral organizations and public sector creditors, in particular, the Highly Indebted Poor Country (HIPC) Initiative and the Multilateral Debt Relief Initiative. New sovereign issuers in particular stand to benefit from the proactive implementation of enhanced data transparency and IR practices as recommended by the *Principles*. New issuers can attract investment through strengthened communication with creditors.

New sovereign issuers in particular stand to benefit from the proactive implementation of enhanced data transparency and IR practices as recommended by the Principles. New issuers can attract investment through strengthened communication with creditors.

some concerns about deviations from the cooperative guidelines of the *Principles.* Finally, the PCG has been kept informed of the progress made by the Joint Public–Private Committee in assessing and drawing lessons from the recent sovereign debt crises in the Euro Area (see below).

The four Co-Chairs of the Group of Trustees of the *Principles* agreed in mid-March 2012 with the two Co-Chairs of the IIF Special Committee on Financial Crisis Prevention and Resolution on the formation of a Joint Public–Private Sector Committee to assess the recent experience with sovereign debt crisis prevention, management, and resolution in the Euro Area and elsewhere; to draw appropriate lessons; and to make recommendations for strengthening of the existing framework for sovereign debt crisis prevention and resolution as embodied in the guidelines of the *Principles.* The formation of the Joint Committee was prompted by the unprecedented nature and historic significance of the Greek debt exchange and the systemic importance of the issues that have been raised by the process and specific terms of the deal both for Greece itself and the broader financial community.

The Joint Committee's overall assessment is that the guidelines underlying the *Principles* remain an appropriate, relevant, and effective framework for sovereign debt crisis prevention and resolution. Their fundamental emphasis on voluntary, cooperative, market-based procedures for debtor-creditor dialogue and good-faith debt restructuring negotiations remain an essential cornerstone of sovereign debt crisis management and should continue to guide the interaction between sovereign issuers and their creditors. However, while the voluntary overall framework of the Greek PSI negotiations was consistent with the *Principles*, aspects of the process through which the actual debt exchange deal was reached and certain specific features of the coverage and terms of the deal raise some concerns going forward. The special or unique institutional features of the Euro Area and the recent experience in sovereign debt crisis management made it highly desirable for the Joint Committee to offer some elaboration or updating of the guidance provided by the *Principles* to make it more practically relevant to the circumstances faced by mature economies, in particular, those that are members of currency unions. The Joint Committee's Report (Annex II) includes an addendum to the *Principles* summarizing the Committee's recommendations. The Group of Trustees and the PCG reviewed and endorsed these recommendations at their annual meeting on October 14, 2012, in Tokyo.

II. Framework for Implementation of the *Principles*

The *Principles* set forth a voluntary approach to debtor-creditor relations, designed to promote stable capital flows to emerging market and other debtor countries through enhanced transparency, dialogue, good-faith negotiations, and equal treatment of creditors. The implementation of the *Principles* is based on the cooperation and partnership between issuers and investors that was evident during the discussion that led to their creation. The implementation process has six broad objectives:

1. Monitoring and evaluating how the *Principles* are being adhered to by issuers and investors;
2. Facilitating the development of a continuous effort by issuers and investors to keep each other abreast of developments in emerging markets and other debtor countries and encouraging sound policies and investor support;
3. Providing guidance in cases in which early course correction can promote better conditions for stable capital flows;
4. Providing recommendations to authorities with respect to better IR practices and enhanced transparency, including the format and frequency of data being disseminated to the market;
5. Offering guidance for the debt restructuring process in appropriate cases; and
6. Helping ensure the continued relevance of the *Principles* in light of changing characteristics of international capital and sovereign credit markets.

The Group of Trustees is the guardian of the *Principles*. The Group consists of 45 current and former leaders in global finance with exceptional experience and credibility. The Group has four Co-Chairs. The current Co-Chairs of the Group are **Agustín Guillermo Carstens,** Governor of Banco de México; **Christian Noyer,** Governor of Banque de France; **Zhou Xiaochuan,** Governor of the People's Bank of China; and **Toshihiko Fukui,** former Governor of the Bank of Japan (see Annex III for the list of all members of the Group of Trustees).

The Trustees meet once a year to review the progress being made on the implementation of the *Principles* within the framework of the international financial architecture.

The Group's mandate includes

- Reviewing the evolution of the international financial system as it relates to emerging markets and other major debtor countries;
- Reviewing the development of the *Principles*, including their implementation; and
- Making proposals for modification of the *Principles*, if needed.

The Group oversees the work of the **Principles Consultative Group (PCG),** a select group of finance and central bank officials with senior representatives of the private financial community tasked with monitoring and encouraging the practical application of the *Principles.*

The PCG has 29 members, including finance and central bank officials from a diverse group of emerging markets and senior representatives of the private financial community, many of whom were instrumental in the formulation of the *Principles* (see Annex IV for a list of the PCG members). The membership of the Group has increased since its first meeting in 2005 to represent more adequately the evolution of global finance in emerging markets and other debtor countries. The PCG maintains an appropriate balance between private and public sector members, as well as membership balanced in geographical scope.

The purposes of the PCG are to

- Consider specific country circumstances with a view toward providing suggestions to authorities and creditors as to how to better

align their policies and actions with the *Principles*;
- Evaluate a wide range of country cases, including those in which significant progress has been made, as well as others that are facing market difficulties;
- Consider the implications of developments in global capital markets for emerging markets and other sovereign debtors and possible measures to address any systemic difficulties that may arise; and
- Review market trends and the changing characteristics of capital and credit markets in order to ascertain if the *Principles* remain relevant or require amendment. Such reviews will be generally completed ahead of the annual meetings of the Group of Trustees.

PCG meetings are held regularly to discuss implementation issues, country cases, and implications of developments in global capital markets. Members enrich PCG discussions with diverse experiences and perspectives.

IMF staff (from the Strategy, Policy, and Review Department and from the Monetary and Capital Markets Department) and a representative from the Federal Reserve Bank of New York have, for some time, joined PCG discussions as observers. Additional observers from the World Bank, the International Finance Corporation (IFC), the Inter-American Development Bank (IADB), the European Bank for Reconstruction and Development (EBRD), the Bank of International Settlements (BIS), and the ECB also participate. The positive involvement of the representatives from international financial institutions provides further evidence of broad support for the *Principles*' implementation process.

The IIF supports both the PCG and the Group of Trustees as their secretariat. The IIF secretariat consults with members of the PCG as well as other market participants as to which country cases or regions to include in PCG discussions. It also prepares background material on international capital market developments, country issues, and other topics on the agenda.

III. PCG Discussions on Regional and Country Circumstances

At their last meeting on September 25, 2011, in Washington, DC, in the context of the joint Annual Meetings of the IMF and the World Bank and the parallel Annual Membership Meeting of the IIF, the Trustees took note of the comprehensive report provided to them by the PCG and welcomed the PCG's effectiveness in providing feedback to a range of authorities over the past 12 months on the implementation of the *Principles*, policy options, and adjustment needs.

The Trustees at their meeting noted the continuing strong net flows of private capital to emerging markets, driven by positive growth prospects in these economies and interest rate differentials versus those in mature economies. However, they noted that there remained the need for heightened vigilance among certain emerging market countries to cope with inflationary pressures in order to underpin stable capital flows and continued growth in emerging markets.

The Trustees reaffirmed their confidence in the value of the *Principles*, which incorporate voluntary, market-based, flexible guidelines for the behavior of sovereign debtors and private creditors with a view to promoting and maintaining stable private capital flows and supporting financial stability and sustainable growth. The Trustees underscored the usefulness of increased reliance on the underlying core guidelines of the *Principles* in promoting crisis prevention through the adoption of strong policies and a more open, systematic dialogue with investors and data disclosure.

The Trustees noted that the *Principles* have served as a reference framework for the formulation of operating modalities in dealing with private sector investors in the new institutional arrangements set up by the Euro Area to handle debt management difficulties. The Trustees were appreciative of the IIF's role in promoting the implementation of the *Principles* in addressing sovereign debt problems. They noted that key elements of the *Principles* have been applied in the process of negotiating the July 21, 2011, support package for Greece. They emphasized that this experience also affirmed the validity of the *Principles* in the context of today's sovereign debt challenges.

As Trustees reviewed the application of the *Principles*, they emphasized that countries with strong policy performance and active IRPs have clearly done well relative to others during this period of market turbulence. They stressed the importance of convincing actions where needed to address fiscal deficits and to put public debt firmly on a sustainable path.

The Trustees noted that since the promulgation of the *Principles* in 2004, a growing number of sovereign borrowers have recognized the importance of active IRPs and strong data dissemination practices as tools to strengthen their relationship with the investor community. The PCG reported to the Group of Trustees that the number of countries with formal IRPs in place increased from 5 in 2004 to 15 as of September 2011.

Over the past year, the PCG held five conference calls, reviewing country cases and developments in international capital and sovereign debt markets. As in 2011, these calls focused primarily on the debt exchange agreement for Greece and the rapidly evolving sovereign debt crisis management policy framework in the Euro Area. The PCG monitored closely the changing economic situation and reform efforts in Ireland and Portugal and other peripheral Euro Area countries. In addition, the PCG also reviewed the debt restructuring experience of St. Kitts and Nevis and the unfolding debt restructuring situation in Belize. Finally, the PCG was kept informed of further developments in the ongoing debt restructuring efforts of Iceland and Côte d'Ivoire and of the work, findings, and recommendations of the Joint Committee. In most instances of debt servicing difficulties, a representative creditor group was formed as a vehicle for engagements with country authorities in line with market practices (Annex VI provides Best Practices for Formation and Operation of Creditor Committees).

Evolving Debt Crisis Management Framework in the Euro Area and the Greek Debt Exchange

The PCG reviewed closely the changing sovereign debt crisis management policy framework in the Euro Area during the last quarter of 2011 and so far in 2012. It took note of the new policy initiatives undertaken by the Euro Area leaders to strengthen sovereign debt crisis prevention and resolution. These included the reinforcement of the arrangements for the monitoring of economic and financial developments, the implementation of fiscal consolidation plans and structural reforms, and in particular more firm rules for the strengthening of fiscal discipline under the Fiscal Compact.

The ongoing sovereign debt crises in the Euro Area over the past two and a half years are the first sovereign debt crises in mature market countries in recent decades. Several crisis management and resolution measures have been implemented, including the establishment of the EFSF and its successor, the ESM, which has funded (together with the IMF) economic reform programs for Greece, Ireland, and Portugal, with additional assistance envisaged for Cyprus and Spain (by the EFSF/ESM for bank recapitalization), and the negotiation of PSI in Greece, culminating in an unprecedented voluntary sovereign debt exchange in March 2012. In addition, major new policy initiatives have been introduced by the Euro Area authorities, including the reinforcement of regional economic surveillance and of fiscal discipline at the country level (under the Fiscal Compact); the Euro Area leaders' decision on June 29, 2012, to set up an ECB-led single bank supervision mechanism as a first step toward the establishment of a banking union and possible direct ESM recapitalization of Euro Area banks; and the ECB decision in early September on the launching of a new initiative for secondary-market purchases of the bonds of Euro Area member countries that agree to appropriate conditionality (outright monetary transactions) on *pari passu* terms with similar bond holders.

The ESM is expected to commence its operations in October 2012, following the positive decision of the German Constitutional Court in early September. Euro Area leaders have also reaffirmed the existing EFSF/ESM mechanisms allowing purchases of sovereign bonds of Euro Area member countries from primary and secondary markets, under appropriate conditionality.

The PCG welcomed these reforms and noted that they constitute an essential complement to the reform efforts being implemented by several Euro Area countries to restore sustainable fiscal and public debt positions over time. The PCG noted that while such crisis resolution efforts have contributed importantly to containing the sovereign debt crisis, they have also revealed serious problems that need to be considered by the international financial community for drawing useful lessons for the future, especially because the key to resolving crises is to restore a sovereign borrower to international capital markets. These problems included shortcomings by both public and private sectors in crisis prevention practices in the years leading to the eruption of the Greek sovereign debt crisis. They also pointed to the need for appropriate design of official adjustment programs that would balance fiscal consolidation and reforms with financing and growth support measures over a suitable time frame.

As regards Greece, the PCG maintained a strong focus on the progress toward the completion of a voluntary debt exchange under a framework consistent with the *Principles*. It pointed to the benefits of adherence to such a framework and to the costs of any deviations. The PCG noted that there have been instances during this protracted negotiation process that started in June 2011 and ended in February 2012 of strong pressures to deviate from these underlying cooperative guidelines of the *Principles* and resort to unilateral, top-down decisions on debt crisis resolution, but eventually a voluntary, consultative approach was followed. The support by the Euro Area authorities and institutions of a voluntary debt exchange agreement for Greece reached through negotiations with private creditors was critical for the successful completion of the PSI deal. The PCG underscored that this process has demonstrated the validity and usefulness of resolving even the most difficult sovereign debt problems in a manner consistent with the cooperative, market-based guidelines

established by the *Principles*, with major benefits not only for the parties directly involved but also for the Euro Area as a whole and global financial stability in general.

In assessing the protracted negotiating process and the terms of the historic voluntary sovereign debt exchange for Greece, the PCG emphasized that while it was negotiated largely, but not totally, in accordance with the guidelines set forth by the *Principles*, it has presented a series of important issues that need to be resolved. These include the role of international laws and jurisdictions (i.e., English and New York laws) in the issuance of traditionally "domestic" sovereign securities, in the context of a sovereign debtor changing domestic law to modify terms and conditions of bond contracts; the problem of subordination of private investors by official bodies as exhibited in the Greek debt exchange or claimed by the ESM Treaty; and the use of CACs, in particular the retroactive insertion of CACs, aggregation clauses, and exit consent.

The PCG recognized that the successful conclusion of the voluntary debt exchange for Greece has provided Greece with a major upfront nominal debt reduction and cash flow benefits. It has also given Greece the necessary breathing space to enable it, together with large official financial support, to be in a position to effectively implement the needed economic reforms in order to correct existing imbalances and attain over time debt sustainability. The extensive involvement of the IIF in the Greek PSI negotiations (reviewed in Box 2) reflected in part the IIF's special role in the development and ongoing efforts for broadening the acceptance of the *Principles* and its service as a Secretariat to the PCG and the Group of Trustees. The details of the unprecedented and historic Greek PSI deal are reviewed in Box 3.

PCG DISCUSSIONS ON OTHER COUNTRY CASES

1. St. Kitts and Nevis

The PCG reviewed very closely the outcome of the voluntary debt exchange concluded by St. Kitts and Nevis, a small Caribbean island economy, in February–March 2012, at the same time that the Greek PSI deal was finalized, as part of a comprehensive debt restructuring and in the context of an IMF-supported adjustment program (see Box 4). The debt exchange agreement covered $150 million of the $750 million subject to the debt restructuring exercise, which includes domestic bank debt, bilateral debt, and intragovernment debt. The balance of St. Kitts and Nevis's total $1 billion debt is in Treasury bills and multilateral loans and was excluded from restructuring. Local banks holding secured government debt will assume government assets under a debt-land swap through a special-purpose vehicle. The details of this swap and the terms of the restructuring of the debt held by Paris Club creditors were settled later in the year.

The debt restructuring was consistent both with the IMF's policy of lending into arrears and the *Principles*. It benefited from a cooperative, transparent, and market-based approach. In assessing the debt exchange, the PCG pointed to several welcomed key features. The government adopted a market-friendly approach from the start and maintained constant dialogue with its creditors, based on the macroeconomic projections prepared under the IMF first review of the Stand-by Arrangement. The macroeconomic assessment and debt sustainability analysis prepared by the IMF was perceived by all parties as objective and realistic and facilitated the acceptance by private creditors of the debt restructuring proposals. Although much of the debt was governed by domestic law, it was modeled after English law and incorporated CACs, which allowed creditors to be engaged on a fair and equitable basis. The activation of CACs raised the creditor participation rate to 100%. Although the exchange was voluntary, there is some concern that the exchange terms were not comparable between the creditors that chose the new discount bonds and those that chose the new par bonds. The net present value losses of the former bonds are significantly lower than those for the latter.

2. Belize

Following the March 2012 parliamentary elections, the new government of Belize has initiated a debt

restructuring process centered on the 2029 bond of $544 million that consolidated Belize's external commercial obligations under the voluntary debt restructuring concluded in 2007. This process is still unfolding, with limited progress so far in reaching understandings with private creditors (see Box 5 for a detailed review of the progress made so far). In view of the delicate nature of the ongoing contacts among the authorities, its legal and financial advisors, and the private creditor committee that has been formed and its advisors, the PCG in its periodic review of developments has strived to seek the views of both parties and provide guidance on the way forward that is consistent with the cooperative approach of the *Principles*.

Overall, the PCG noted that there were at times worrisome tendencies to deviate from the cooperative guidelines of the *Principles*, with increased risks of unilateral actions. The key issue remained the need for data and policy transparency

Box 2. The IIF's Role in the Voluntary Debt Restructuring for Greece

The role played by the IIF in the negotiations on the voluntary debt exchange for Greece demonstrated the Institute's special position in the international financial marketplace—not just as an association of the world's largest financial institutions but more broadly as an "honest broker" in advancing the shared interests of the private sector and the official community. More specifically, the IIF was seen as an effective representative of the broad interests of the private creditor community, not only in the debt restructuring negotiations but also in fostering understanding of their implications for regional and global financial stability. IIF involvement in the Greek debt restructuring also reflected in part recognition of the Institute's pivotal role in developing and encouraging the acceptance and effective implementation of the *Principles for Stable Capital Flows and Fair Debt Restructuring*.

The IIF was invited during the course of 2011 by the Eurogroup Working Group (EWG)—comprised of senior officials from the Euro Area countries, with representatives from the European Commission, the EFSF, the ECB, and the IMF as observers—to engage in discussions with a view to arranging a private sector involvement in support of Greece.

During the first phase of this engagement, which started in mid-June and ended in mid-October 2011, the IIF formed—with the approval of its Board of Directors and other key members—a ***Task Force for Greece*** encompassing IIF member firms and other creditors to Greece (including insurance companies and asset management companies) to reflect on these issues and formulate proposals. The first stage of negotiations with the Euro Area official sector—led by Josef Ackermann, Chairman of the IIF's Board of Directors, and Charles Dallara, IIF Managing Director—culminated in a ***July 21 voluntary private sector involvement agreement.*** This agreement formed an integral part of the comprehensive package of EFSF reforms and expanded financial assistance and other measures adopted by the Euro Area leaders in support of Greece and other Euro Area countries facing debt management challenges. However, by the time the process of securing legislative approval for the EFSF reforms by all 17 Euro Area countries was completed in mid-October, the economic and financial situation in Greece had deteriorated and the July 21 agreement was not implemented, as it was no longer seen as a viable framework for Greece to regain access to capital markets.

Against this background, in mid-October the EWG invited the IIF for a new round of discussions—led by Charles Dallara, IIF Managing Director, and Jean Lemierre, Senior Advisor to the Chairman of BNP Paribas and Co-Chair of the IIF's Special Committee on Financial Crisis Prevention and Resolution—which resulted in the ***October 26/27 private sector agreement*** on Greece. This agreement, reached with the Euro Area leaders including German Chancellor Angela Merkel and French President Nicholas Sarkozy, envisaged a nominal haircut of 50% on all outstanding privately held Greek sovereign debt; a contribution by Euro Area countries of €30 billion; and the securing of a decline in the debt:GDP ratio with the broad objective of reaching 120% by 2020. At the invitation of the Euro Area leaders, discussions among private investors and the Greek and Euro Area authorities and other concerned parties (the European Commission, the IMF, the ECB, and the EFSF) on the detailed structure of a voluntary debt exchange were also planned.

In preparation for the initiation of negotiations on the details of the new agreement with the Greek authorities, the IIF Task Force on Greece transformed itself on November 17, 2011, into a formal ***Private Creditor–Investor Committee*** (PCIC), which comprised 32 members, accounting for a large share of privately held Greek sovereign bonds. The PCIC selected a Steering Committee of 13 major creditors, co-chaired by Charles Dallara and Jean Lemierre. Senior IIF staff served as Secretariat to the Steering Committee.

about the authorities' adjustment plans and adequacy of its reform efforts and the associated need for appropriate burden sharing with all its creditors. The PCG emphasized that all parties would be best served by engaging in an open and constructive dialogue and good-faith negotiations on the financial constraints and policy challenges facing Belize, the authorities' efforts to address these challenges, and the role all creditors could play in providing assistance through debt restructuring. Such contributions should be based on fair treatment of all creditors and a burden sharing that is proportionate to the needs of the country under a coherent and realistic macroeconomic framework that incorporates the authorities' reform commitments and addresses adequately debt sustainability concerns.

Box 3. Greece—Main Provisions of the Voluntary Debt Exchange Agreement

The final agreement and Greek debt exchange results represent a historic event:

- It was the first debt restructuring by a mature country in decades and the first debt restructuring ever by a Euro Area country, and this had a significant impact on global and regional economic and financial developments and market sentiment. Covering €206 billion of Greek government debt, it was the ***largest debt restructuring in history.***
- It demonstrated that the Euro Area did eventually recognize the value and importance of reaching a debt restructuring agreement in a voluntary, cooperative approach consistent with the *Principles*.
- The agreement entailed ***a very high voluntary overall private creditor participation rate*** of 83.5%—almost 97% with the activation of CACs.
- The cost of the debt exchange for private creditors was itself unprecedented, estimated to exceed 74% in net present value terms at an assumed discount rate of 12%.

The key terms of the voluntary debt exchange agreement included the following:

- An ***upfront nominal debt reduction of 53.5%,*** going beyond the 50% haircut initially agreed in October 2011; 15% of existing claims paid in the form of EFSF notes of 1–2 years' maturity, and the remaining 31.5% exchanged with new Greek government bonds (GGBs) of maturities of up to 30 years.
- Cash-equivalent payments to private creditors financed by a ***special contribution of €30 billion by the official sector*** through the EFSF as a loan to Greece.
- ***Annual coupons on the new GGBs kept at very low levels*** (2% during the three-year period to 2014, 3% during the five-year period to February 2020, 3.65% during the year to February 2021, and 4.3% thereafter), well below the prevailing market levels and the coupons on the old bonds.
- Other special features **designed to help enhance the credit quality of the new GGBs,** included a co-financing (A/B loan) scheme with the EFSF €30 billion loan and the use of English law as the governing legal framework.
- ***GDP-linked securities based on the face value of the new GGBs,*** offering supplementary coupon payments after 2014 in the event that Greece's actual nominal and real GDP growth exceed baseline levels.

The **benefits to Greece** are unprecedented and substantial, and they entail

- ***An up-front nominal debt reduction of about €106 billion, or almost 50% of GDP***—lowering the debt:GDP ratio from 165.3% at end-2011 to 132.4% in March 2012 (a reduction of almost 33 percentage points)—contributing to a projected reduction in the debt:GDP ratio to around 116.5% of GDP by 2020, according to the IMF program estimates.
- Significant cash flow benefits during the period to 2020 resulting from the agreed restructuring as well as ***substantial interest savings*** of about €30 billion relative to what would have been due, and potential interest payment savings of €90 billion relative to the estimated cost of new market borrowing.
- More importantly, the ***voluntary debt exchange will help provide Greece some breathing space to effectively implement the broad range of reforms needed*** to achieve fiscal consolidation, lower public debt, enhance competitiveness, regain market confidence and market access, restore economic growth, and thus pave the way for debt sustainability.

The PCG pointed out that debt sustainability could not be attained without the restoration of market confidence in Belize and the regaining of market access down the line. The thrust of this assessment was conveyed to the authorities and the private creditor committee through letters by the IIF Managing Director.

3. Other Country Cases

The PCG continued to follow developments in **Ireland,** where fiscal, financial, and structural reforms are advancing as envisaged under Ireland's three-year economic reform program supported by the IMF and Euro Area countries. At times during 2012, renewed tensions in the Euro Area contributed to increases in Irish sovereign bond spreads. While reforms in Ireland's financial sector are advancing, it continues to face challenges in securing market access. However, in late July 2012 Ireland sold new long-term government bonds for the first time since losing market access in September 2010, ahead of the time schedule (2013) anticipated under its program.

The PCG monitored closely the continuing efforts of **Côte d'Ivoire** to alleviate its external debt burden vis-à-vis official bilateral creditors, while also regularizing the servicing of its debt to external private creditors, following the restoration of political stability in the country (see Box 6 for an overview). Côte d'Ivoire reached a new HIPC completion point in June 2012 under which a total $6.5 billion, or about 99.5% of Côte d'Ivoire's bilateral debt, was forgiven. In early July 2012, Côte d'Ivoire resumed full contractual payments to the holders of the Eurobonds, beginning with the interest coupon due June 30, 2012, and made a good-faith payment to creditors of 2.4% of outstanding

Box 4. St. Kitts and Nevis—Debt Restructuring

At the same time Greece embarked on a voluntary debt exchange of its privately held public debt, St. Kitts and Nevis, a small Caribbean island economy, announced and successfully concluded a restructuring of part of its outstanding public debt, covering certain bonds and commercial bank loans. This was part of a broader debt restructuring initiative envisaged under the IMF-supported (under a stand-by arrangement) three-year reform program initiated in July 2011. The IMF deemed total public debt, at 160% of GDP, unsustainable. The debt exchange encompasses $150 million of $750 million subject to the debt restructuring exercise, including domestic bank debt, bilateral debt, and intragovernment debt, but excluding short-term debt (Treasury bills) and debt to multilateral institutions.

The government announced in June 2011 its intention to seek the cooperation of its creditors in the restructuring of its public debt stock, releasing indicative restructuring scenarios in August 2011. After broad creditor consultations, an offer was launched in February 2012. Creditors had the option of exchanging their instruments for new discount bonds denominated in U.S. dollars or par bonds denominated in East Caribbean dollars. The discount bonds (amortizing bonds with a maturity of 20 years and a coupon of 6% for the first 4 years, falling to 3% a year thereafter) entailed a 50% upfront reduction in face value, backed by a $12 million partial guarantee of cash flows by the Caribbean Development Bank. Par bonds had a maturity of 45 years with a 15-year grace period, carrying a fixed 1.5% coupon.

As part of the debt exchange deal, 96.8% of principal of debts eligible under the exchange were tendered. Two-thirds of the creditors opted for the discount bond, and one-third opted for the par bond. Much of the debt was governed by domestic law, modeled after English law, and CACs have been used for decades. The high participation exceeded the 85% threshold, allowed the activation of CACs embedded in four of the eligible claims for the holders of the 3.2% of eligible claims not tendered in the exchange (who received discount bonds), thus ensuring 100% participation.

On April 18, 2012, discount bonds with a face value of US$43.3 million and par bonds with a face value of EC$134.4 million were issued. In May 2012, holders of the discount bonds received a one-off goodwill payment of 13% of face value of bonds held; holders of par bonds received 11.25% of face value of the bonds. Local banks holding secured government debt will assume government assets under a debt-land swap through a special-purpose vehicle.

The debt restructuring was consistent both with the IMF's policy of lending into arrears and the *Principles*. The government adopted a market-friendly approach from the start and maintained constant dialogue with its creditors. Macroeconomic projections prepared under the IMF first review of the stand-by arrangement formed the basis for facilitating understanding of the government's adjustment efforts and the need for debt relief.

Box 5. Belize—Initiation of a Debt Restructuring Process

Following the victory of the UPD party in the parliamentary elections of March 2012, the new Prime Minister Dean Barrow announced the formation of a special Debt Review Team, with legal and financial advisors, to assess the country's public debt dynamics, with a resolute view to placing the nation's medium- and long-term finances on a sustainable footing and identify "debt management alternatives." In reaction to this, a private creditor committee was established in June 2012, representing by August 2012 holders of over $300 million (or about 60%) of Belize's 2029 bond.

Belize concluded in 2007 one of the early successful voluntary debt restructurings that resulted in the consolidation of the then existing external commercial government obligations into a single new instrument ("Superbond"), with a face value of $543.8 million—with a 12-years' grace and equal semi-annual principal payments starting in 2019 and final maturity in 2029. At the time, the favorable terms of the Superbond eased significantly Belize's debt service burden. The new bond entailed a step-up coupon structure, lowering the annual average interest rate from 11.25% prior to 2007 to 4.25% for years 1–3, 6.0% for years 4–5, and 8.5% for year 6 (starting in August 2012) to maturity. The bond also included CACs with a 75% majority required for reserved matters.

According to the latest IMF staff report (October 2011), Belize's economy has weathered the global economic crisis relatively well compared with its Caribbean Community peers. After leveling off in 2009, Belize's real GDP grew by about 2.5% a year during 2010–2011 and is projected by the authorities to expand by 2% in 2012 against the background of a weakening investment climate and an unanticipated declining trend in domestic oil production capacity. In the decade prior to 2007, Belize enjoyed much higher average output growth rates (7% a year). The current account deficit was reduced from 10.6% of GDP in 2008 to around 3% by 2011. Public finances remained under pressure, but actual performance was fairly strong by international standards. The overall budget deficit was contained at about 1.5% of GDP during 2009–2011, while the primary balance remained in surplus, averaging 2.2% of GDP. Total domestic and external public debt declined from a peak of 92.5% of GDP in 2006 to 80.4% by end-2011.

The IMF staff report noted that Belize's medium-term prospects were uncertain, with risks tilted to the downside. These prospects were based on the authorities' medium-term plans for real GDP growth of 2.5% and a primary budget surplus target of 2% of GDP, which the IMF staff report noted would keep the public debt and the gross financing needs high over the medium term. The latter were projected to increase from 3.6% of GDP in 2012 to 7.5% by 2019 when the principal bond repayments would commence. The IMF recommended instead that the authorities raise the target output growth rate to 3.5% through appropriate reforms and aim for larger primary budget surpluses of 4% of GDP a year during the rest of the decade so as to keep public debt firmly on a downward trend. The authorities noted that the attainment of such fiscal consolidation plans was constrained by the global economic slowdown and Belize's rising fiscal needs to combat poverty.

Against this background, Prime Minister Barrow announced in late June 2012 during his budget speech that Belize would adopt a new public debt and liability strategy calling for a major restructuring of the Superbond. He stated that such debt relief was necessitated by the following interrelated factors: (1) the global economic slowdown; (2) the fact that the loans underlying the Superbond had "provided little or no tangible benefit to Belizeans"; (3) the 2.5 percentage points' increase in the Superbond coupon to 8.5%, which would raise the budget interest payments burden by over 1% of GDP and which Belize could not afford to pay; (4) the prospective halving of the government's oil-related revenue (from 3.1% of GDP in 2011 to less than 1.4% by 2013); and (5) the large cost of the government compensation of the renationalization of the telephone and electricity utilities (with estimates ranging from $85 million claimed by the government to $450 million claimed by the former owners).

Belize's total public debt amounted to $1.2 billion, or 81% of GDP, at end-April 2012, excluding contingent liabilities. The Superbond accounted for 47% of total debt, while multilateral creditors accounted for 22%, bilateral creditors for 15%, and Treasury bills and other domestic debt holders for 16%. Inclusive of an assumed mid-point estimate of the compensation for the nationalization cost of the two utilities, the total debt would rise to $1.5 billion (103% of GDP). The budget for the fiscal year ending March 2013 envisages an overall deficit of 2.5% of GDP and a primary surplus of 2.0% of GDP, with a gross financing requirement of 4.6% of GDP and 5.8% of GDP in the fiscal year ending March 2014.

To cover in part this requirement, the authorities envisage continued drawdown under existing project loans from Taiwan Province of China, multilateral creditors (the IADB, the Caribbean Development Bank, and the Central

(continued)

Box 5. Belize—Initiation of a Debt Restructuring Process *(continued)*

American Bank for Economic Integration) and special funds (OPEC Fund and Kuwait Fund), as well as domestic bank financing. Belize has not accessed capital markets since the 2007 debt restructuring. But, on current policies, Belize considers that debt relief is needed to help cover its budget and other funding shortfalls and lower its public debt burden.

The interaction between Belize and its private creditors since June 2012 has taken the form of frequent contacts between financial advisors and public announcements with limited direct contact. On August 8, the government of Belize issued three "indicative restructuring scenarios" that provide for the following options for holders of the Superbond: (1) a 50-year par amortizing bond, with a 15-year grace period and a fixed 2% coupon; (2) a 40-year discount bond, with a 45% haircut, no grace period, equal semi-annual principal repayments, and an escalating low coupon (1% for years 1–7, 2% for years 8–14, and 4% for year 15 to maturity); and (3) a 40-year discount amortizing bond, with a 45% haircut, a five-year grace period, and a fixed 3.5% coupon. These terms imply fairly large financial losses for private creditors (estimated at 79%–83% in net present value terms at assumed discount rates of 12%–15%), which go significantly beyond the terms of recent sovereign debt restructurings by Argentina and Greece. In addition, Belize announced on August 14 that it was unable to make the August 20 coupon payment of $23 million (based on the stepped-up coupon of 8.5%) during the normal 30-day grace period.

In response, the private creditor committee issued a statement on August 13 in which it expressed disappointment with the indicative restructuring scenarios, which it did not consider as the start of negotiations. The announcement added that private creditors "are prepared to work with the authorities in a consensual and collaborative manner" and that they "will respond to proposals that are based on ability to pay using reasonable, mutually agreed assumptions as well as demonstrated burden sharing among commercial, bilateral, and multilateral creditors, and, importantly, the Government itself." The authorities counteracted these reactions with a communiqué issued on August 21 in a question-and-answer format that denied concerns that the nonpayment of the coupon reflected unwillingness rather than inability to pay and called for the private creditors to express their views on the scenarios put forward. The authorities expressed willingness to complete the negotiations by end-2012.

The market reaction to these developments has been swift. The secondary-market price of the 2029 Superbond declined sharply from the stable level of around 50% until early August to 35% by late August, while ratings agencies have lowered Belize's ranking several steps since March 2012. On August 21, Standard & Poor's lowered Belize's foreign currency rating to "selective default" and the rating on the 2029 bond to "default."

coupon arrears. Côte d'Ivoire also announced that, given the debt reduction effort already made by the London Club creditors under the 2010 debt exchange, no additional effort was required from holders of the Eurobonds to comply with the Paris Club comparability of treatment principle. The PCG praised the authorities for their open and transparent communications with its bond holders and the creditors' understanding for the delays experienced in receiving coupon payments.

Finally, the PCG was kept informed of developments in **Iceland** and the ongoing efforts to regularize the payments due to foreign depositors with Icelandic banks and to reach restructuring agreements with the winding-up boards of the three main banks (Box 7).

International Capital Markets and Emerging Markets Roundtable

On April 22, 2012, the Leadership of the Group of Trustees hosted the annual Roundtable on International Capital Markets and Emerging Markets in Washington, DC. The Roundtable serves as a leading forum for dialogue between policymakers and senior leaders in global finance, bringing together public officials from both mature and emerging market economies, representatives of international financial institutions, and leaders from the private financial sector.

The 2012 Roundtable was organized in coordination with the Mexican G-20 Presidency and included two panel discussions on the "Challenges in Resolving Sovereign Debt Crises in Mature

Economies in the Context of a Fragile Global Recovery" and the "Challenges Ahead in the G20 Agenda: Macroeconomic and Structural Policies for Balanced and Sustainable Growth." The discussions focused on the challenges in resolving sovereign debt crises in Euro Area countries and other mature economies, including lessons learned and implications for further strengthening of the debt crisis prevention and resolution framework. In a special luncheon keynote address, José Antonio Meade, Secretary of Finance and Public Credit of Mexico, summarized the progress on the G20 Agenda and the global efforts toward deleveraging in mature economies. Interest in the 2012 Roundtable was particularly high, with nearly 300 participants in attendance.

Joint Committee Report and *Addendum to the Principles*

The setting up of the Joint Committee and the reaching of broad understandings among private and public sector financial officials and experts on an *Addendum to the Principles* have been major undertakings of the Group of Trustees during 2012. As explained in detail in the Joint Committee Report (Annex II), the formation of the Joint Committee and its terms of reference have been prompted by several critical factors and considerations.

First, the emergence of sovereign debt crises in mature countries, and in the Euro Area currency union more specifically, has opened a new chapter in the international experience with sovereign debt

Box 6. Côte d'Ivoire—Normalization of Relations With Creditors

Côte d'Ivoire cleared its arrears with the World Bank in 2008 and with the African Development Bank in March 2009, facilitating the approval in March 2009 by the IMF of a three-year, $566 million arrangement under the Extended Financing Facility (EFF) and the Poverty Reduction and Growth Facility (PRGF). In May 2009, Côte d'Ivoire concluded an agreement with the Paris Club; bilateral debt restructuring agreements, signed with nearly all Paris Club creditors, reduced debt service payable to these creditors by 93%. Côte d'Ivoire qualified for further debt relief assistance after reaching a completion point under the enhanced HIPC Initiative.

In parallel, Côte d'Ivoire reached a preliminary agreement with the informal London Club group of private external creditors in September 2009 and completed a voluntary debt exchange in mid-April 2010. Over 99% of the $2.8 billion Brady bonds in default since 2000 were restructured with $2.38 billion in new bonds. Civil war in 2002–2003 and the ensuing political instability delayed negotiations until 2009.

However, run-off presidential elections in November 2010 triggered political turmoil and violence, paralyzing economic activity. Following the resolution of the crisis, a new government was installed on May 21, 2011. The new Minister of Finance, Charles Koffi Diby, issued a communiqué on June 1, 2011, to the external private sector holders of $2.3 billion of Eurobonds, expressing full recognition of the missed interest payment at end-2010 and its commitment to communicate with its creditors.

On July 8, 2011, Minister Diby announced to bond holders that, due to the severe damage to the economy resulting from the post electoral crisis, the country would not be able to make scheduled payments on external debt due in 2011 to the Paris Club or private holders of the $2.3 billion Eurobonds. Nevertheless the government undertook to resume contractual payments to its bond holders beginning in 2012 and continued to fully recognize its obligations. The IMF approved on July 8, 2011, a new $129.3 million arrangement under the Rapid Credit Facility to support the country's economic recovery program. The IMF also approved a new $616 million three-year program under the Extended Credit Facility in November 2011, which provided the basis for an interim agreement with the Paris Club, facilitating the normalization of relations with private creditors.

Côte d'Ivoire reached a new HIPC completion point in June 2012, under which debt relief of $1.77 billion was secured from the Paris Club, with members agreeing to grant a further $4.73 billion on a bilateral basis, for a total equivalent to 99.5% of Côte d'Ivoire's debt. In early July 2012, Côte d'Ivoire resumed full contractual payments to the holders of the Eurobonds, beginning with the interest coupon due June 30, 2012, and made a good-faith payment to creditors of 2.4% of outstanding coupon arrears. Côte d'Ivoire also announced that, given the debt reduction effort already made by the London Club creditors under the 2010 debt exchange, no additional effort was required from holders of the Eurobonds to comply with the Paris Club comparability of treatment principle.

crisis management. It underscored the urgency of strengthening the framework for crisis prevention and the reinforcement of the architecture of the Euro Area currency union arrangements to facilitate economic adjustment among member states and regional financial stability.

Second, it raised important analytical and operational questions on how best to address sovereign debt crisis resolution while managing at the same time the actual and potential contagion and spillover effects to other countries in the region and containing the adverse feedback effects between sovereign debt markets and the regional banking system.

Third, the Greek debt exchange deal was in itself historic and unprecedented in terms of its scale and implications for Greece itself, the financial losses sustained by private creditors, and the expectations it has created that similar debt restructurings might be needed in other countries in the region. One feature of the Greek debt crisis was that it was the first sovereign debt crisis to occur under the market valuations–based accounting rules amid an environment of tightening capital adequacy regulatory requirements that had an immediate impact on the balance sheets of banks and other regulated financial institutions. The declining value of Greek government and other sovereign securities in the secondary market had direct financial implications on these financial institutions even before a debt exchange deal was concluded.

Fourth, the Greek debt crisis has stimulated a host of regional policy innovations and challenges that are still at the center of the economic policy debate in the Euro Area, including the reversal of the regional financial integration experienced over the previous decade and fragmentation along national lines of the bank-funding and sovereign debt markets.

Finally, the protracted process for reaching an agreement on the Greek debt exchange and the way it has been handled by the official sector, as well as the broad range of creditors covered by the deal, the tools used in the exchange, and the retroactive modification of the terms of the Greek law bonds, have raised concerns with implications for the demand for sovereign debt.

Box 7. Iceland—Strengthening Relations With Creditors

Iceland's economic recovery is evidenced by its rapid return to growth and a stabilized exchange rate. Glitnir, Landsbanki, and Kaupthing—the three largest Icelandic banks put into receivership—and their creditors have continued their cooperation; adherence to the guidelines of the *Principles* has contributed to the bank resolution progress, benefiting in broader terms the country's emergence from its 2008 financial collapse.

In March the Icelandic Parliament made amendments to the capital controls regime in order to halt increasing circumvention through the bond market and contain possible negative effects of large capital outflows resulting from the winding-up process of the failed Icelandic banks.

Both Kaupthing and Glitnir are aiming to finish winding-up proceedings through composition, thereby giving creditors control of the future of the estates.

The winding-up boards of Glitnir and Landsbanki made disbursements in the past 12 months to their priority claim holders. These payments will now be subject to the control of the Central Bank. According to the authorities, the remaining payments due to domestic assets could have a serious detrimental effect on Iceland's balance of payments if not managed in a suitable manner. It would not be in the interest of claim holders if the economic and financial stability of Iceland is put at risk through disorderly capital outflows.

The EFTA Court in Luxembourg heard oral arguments in the so-called Icesave case in September. The case was brought before the Court by the EFTA Surveillance Authority. The EFTA Court case is an infringement case, where the Authority seeks a general declaration from the Court. It is expected that the EFTA Court will deliver its ruling before the end of the year.

In March and June 2012, Iceland repaid ahead of schedule over half of its obligations to the IMF and its Nordic bilateral creditors in connection with the 2008–2011 economic program.

For all these reasons it was deemed vital to review and assess the recent experience in the Euro Area and draw lessons for policymakers at the country and regional levels, as well as relevant international financial institutions and the private investor community. The key objective of the Joint Committee was to evaluate the need and make recommendations for the amplification of the existing guidance for the practical application of the *Principles*, including through the possible issuance of an addendum to the *Principles*.

The Joint Committee was co-chaired by **Jean Lemierre,** Senior Advisor to the Chairman, BNP Paribas, and Co-Chair of the IIF Special Committee on Financial Crisis Prevention and Resolution; **Thomas Wieser**, President, Eurogroup Working Group; **David Mulford,** Vice-Chairman International, Credit Suisse Group; and **Gerardo Rodríguez Regordosa**, Undersecretary of Finance and Public Credit, Mexico. The Joint Committee also comprised 35 prominent representatives from the public and private sectors with extensive experience in sovereign debt restructuring in the Euro Area and elsewhere (the membership of the Joint Committee is shown in Annex II). IIF staff served as Secretariat to the Joint Committee. To address its agenda, the Joint Committee held several conference calls and three physical meetings in Washington, DC, in April and in Paris in June and September 2012.

The Joint Committee's main findings are twofold. First, the Joint Committee reconfirmed that guidelines underlying the *Principles for Stable Capital Flows and Fair Debt Restructuring* remain an appropriate, relevant, and effective framework for sovereign debt crisis prevention and resolution. Their fundamental emphasis on sound policies and data and policy transparency by debtors is of critical importance in crisis prevention. Moreover, the underlying guidelines for voluntary, cooperative, market-based procedures for debtor-creditor dialogue and good-faith debt restructuring negotiations remain an essential cornerstone of sovereign debt crisis management and resolution and should continue to guide the interaction between sovereign issuers and their creditors. Such a cooperative approach would facilitate early restoration of market access, which is of critical importance in achieving debt sustainability over time, and would allow the official sector to gradually reduce its exceptional financial assistance to the countries under official sector–supported reform programs.

Second, the Joint Committee noted that, while the voluntary overall framework of the Greek PSI negotiations was broadly consistent with the *Principles*, some aspects of the process through which the actual debt exchange deal was reached and some specific features of the coverage and terms of the deal raise concerns going forward. With regard to the process, there have been at times uncertainties about the official sector commitment to a voluntary approach and, especially in the last critical stage of the negotiations, limited transparency of information on the details of Greece's future policy plans, specific policy targets and likely macroeconomic outcomes, and the associated determination of the volume and terms of the contribution of private creditors. The multiplicity of statements often at member state level in the context of domestic political debates has often created confusion in the private sector. The complexity of the Euro Area decision-making process and the fact that Euro Area authorities needed some time to develop the required response to the crisis complicated the situation significantly.

With regard to specific features, the exclusion of bonds held by EU official entities (such as the ECB, national central banks, and the European Investment Bank [EIB]) from the debt exchange has raised concerns about equal treatment of creditors holding similar paper and the subordination of private investors, with possible lasting adverse effects on the demand for Euro Area sovereign debt in general. In addition, the retroactive modification of the legal framework to introduce a collective action mechanism in the Greek government bonds issued under Greek law has raised concerns about the sanctity of contracts and questions about the future demand for sovereign securities issued under domestic law, notwithstanding its contribution to the high participation in the voluntary debt exchange.

To help address these concerns and reinforce the guidance for the implementation of the fundamental

guidelines of the *Principles*, the Joint Committee has presented a coherent set of recommendations, which are listed in the *Addendum to the Principles* in Annex II. These fairly sensible and noncontroversial practical suggestions have been endorsed by the Group of Trustees and are expected to be easily accepted and applied by policymakers and financial market participants alike. The key recommendations of the Joint Committee emphasize *inter alia* the following:

- Debtors should pursue sound policies and release on a timely basis accurate and comprehensive data and other information related *inter alia* to their fiscal developments and debt positions and on current and future policy plans. These data should be verified by domestic and regional authorized agencies for their consistency with established standards;
- Effective sovereign debt crisis prevention is a shared responsibility of debtors, creditors, regional and international institutions, regulators, and private early warning groups, such as the IIF's Market Monitoring Group;
- Private creditors and market participants are responsible for formulating accurate and appropriate assessments of underlying trends in market risks and the credit and sovereign risks of individual issuers;
- Mature market countries could benefit from the adoption of IRPs and the incorporation of CACs containing aggregation clauses in their new bond issues;
- Good-faith negotiations remain the most effective framework for reaching voluntary debt restructuring agreements and containing adverse market impact;
- In the debt restructuring process, an early exchange of views is necessary between the representative private creditor committee and the sovereign debtor, in close consultation with the official sector, on the setting of the overall multiyear macroeconomic framework and objectives, including the formulation of the broad fiscal policy targets and the underlying outlook for output growth and public debt under alternative assumptions on the debt restructuring terms and other key parameters.
- The early restoration of market access is of critical importance in achieving debt sustainability over time;
- The IMF has an important role to play as an honest and independent broker, including by providing objective analysis and information on macroeconomic policies and prospects and on the sovereign debtor's medium-term funding needs, consistent with debt sustainability considerations;
- Early formation of a broadly based representative private creditor committee is desirable; in the case of countries relying on financial assistance from a multitude of official bilateral creditors, a streamlining of the collective decision-making process by these creditors would facilitate the timely conclusion of good-faith debt restructuring negotiations;
- Sovereign issuers should introduce CACs and possibly other options to enhance the credit quality of the new debt instruments used under debt restructuring exercises so as to enhance the prospects for high voluntary creditor participation;
- Retroactive legal changes to unilaterally modify the terms and conditions of contracts undermine the integrity of financial markets and the sanctity of contracts and should be avoided; and
- Fair and comparable treatment of all creditors and the avoidance of subordination of private creditor claims are critical.

IV. Investor Relations and Data Transparency

Since the establishment of the *Principles* in 2004, a growing number of sovereign borrowers have recognized the importance of active IRPs and strong data dissemination practices as tools to strengthen their relationship with the investor community (Table 1). The *Principles* build on best practices of both issuers and investors and are complemented by the support of these practices by other agencies and international financial institutions, such as the IMF and the World Bank.

The emphasis on transparency and strong IR placed by the *Principles* proved particularly useful during the global financial crisis of 2007–2009; experience has demonstrated that countries with strong policy performance and active IRPs have done well relative to others during this period of market turbulence. For example, Indonesia, Poland, and Turkey—countries with strong debt management practices—have lately benefited from record-low bond yields. Limited new bond issues and sustained net private capital inflows during 2011 and most of 2012 have also reduced the yields on Latin American sovereign bonds, prompting some governments, such as Colombia, Peru, and Uruguay toward opportunistic taps or new issues in international markets. Such trends illustrate investors' improving perception of credit risk in these countries. Amid intensified global risk aversion that affected every asset class, a number of emerging market countries with solid track records in data transparency and close engagement with their private creditors have remained active

Table 1. Active Investor Relations Programs

Country	Date of Launch of IRP	Location
Mexico	1995	Ministry of Finance and Public Credit
Brazil Central Bank Brazil Treasury	April 1999 2001	Banco Central do Brasil The National Treasury
The Philippines	July 2001	Bangko Sentral ng Pilipinas
Korea	2004	Ministry of Strategy and Finance
Turkey	August 2005	Prime Ministry Undersecretariat of Treasury
Indonesia	February 2006	Bank Indonesia
Peru	April 2006	Ministry of Economy and Finance
Morocco	December 2007	Ministry of Economy and Finance
Colombia	2008/Upgraded 2010	Investor Relations Colombia, Directorate of Public Credit, Ministry of Finance
Chile	Upgraded 2009	Ministry of Finance
Poland	February 2009	Investor Relations Division, Public Debt Department, Ministry of Finance
Dominican Republic	September 2009	The Public Debt Office, Ministry of Finance
Panama	April 2011	Ministry of Economy and Finance
Uruguay	April 2011	Ministry of Economy and Finance
South Africa	June 2011	National Treasury

in international capital markets. Furthermore, a sustained record of sound economic policies, solid fundamentals, and a good track record of observance of the *Principles*—including the provision regarding data transparency—have been helpful in enabling Colombia, Mexico, and Poland to remain eligible for assistance under the IMF's facility for short-term liquidity support, the Flexible Credit Line.

Over the past year, a growing number of countries have stepped up efforts in refining IR practices and resource-intensive data release practices, some with financial and technical support from multilateral and bilateral sources.

Emerging market sovereign debtors have made enormous strides over the past several years in improving their IR practices and data transparency. The number of countries with formal IRPs in place has increased from five in 2004 to 15 at present, comprising (listed according to the timing of the commencement of their programs) Mexico, Brazil, the Philippines, Korea, Turkey, Indonesia, Peru, Morocco, Colombia, Chile, Poland, the Dominican Republic, Panama, Uruguay, and South Africa.

Through consultation with the private sector, the IIF has developed a set of 20 criteria for the evaluation of IR practices and a set of 23 criteria for the evaluation of the data dissemination practices of emerging market sovereign debt issuers. The IIF's IR and data practice assessments support the implementation of the *Principles*, as well as other initiatives on crisis prevention and resolution. By reporting advances in sovereign IR practices, this report provides information to both borrowing countries and the investor community. In addition to its role in serving as secretariat for the PCG, the IIF provides value to its members by providing sovereigns with IR best-practice recommendations, including best practices on the format and frequency of data dissemination to the market.

The full scoring of each country in the IIF IR and data transparency index are shown in Tables 2 and 3. These best practices can be used by emerging market economies to design country-specific IRPs. The index is a summation of the IR and data release practices scores on a prioritized basis. A detailed explanation of each criterion is provided in Appendix A. The complete IIF Best Practices for Investor Relations is provided in Annex V.

Rankings for both IR and data transparency in 2012 remain largely unchanged relative to 2011, although there have been some notable improvements, detailed below. The 2012 rankings of IR practices indicate that Brazil, Indonesia, and Turkey attained the highest score. They were followed by Chile, Peru, and South Africa in second place, and by a broader, third layer of countries that comprised Colombia, the Dominican Republic, Hungary, Korea, Mexico, the Philippines, Poland, and Uruguay.

The data dissemination rankings in 2012 are headed by Turkey, which attained the highest possible score (42) followed closely by Chile (41). The second layer included Brazil, the Dominican Republic, Indonesia, South Africa, and Uruguay. Following closely behind, was the third layer of countries comprising Croatia, Egypt, Hungary, Mexico, Morocco, Peru, and Poland.

Brazil, Chile, the Dominican Republic, Indonesia, South Africa, Turkey, and Uruguay continue to set preeminent examples in data dissemination practices in their respective regions.

Based on these IIF evaluations, this report provides key borrowing countries with an opportunity to convey to market participants the efforts they are making to strengthen the dialogue with investors. In addition, it offers investors a comprehensive comparative evaluation of communication and data dissemination practices for 38 countries and a guide to locating available information relevant to investors. At the same time, investors are better equipped to assess whether country practices meet their expectations and needs. Both the official and private sectors increasingly recognize that prevention is the first line of defense against a financial crisis. As demonstrated by recent episodes of sovereign debt crises, close engagement and cooperation by sovereign debt issuers with private sector creditors are essential ingredients for the resolution of a country's debt difficulties.

Section V of this report documents recent innovations in sovereign IRPs and data transparency. The PCG has underscored that a regular briefing of

Table 2. Overall Assessment of Investor Relations and Data Transparency Practices (Prioritized)

Investor Relations Practices Criteria		Investor Relations Office/Staff		Investor Relations Website			Dissemination of Macroeconomic Data and Policy Information							Investor Relations Contact List	Feedback and Communication Channels						Regular Self-Assessment	
		Presence of institutionalized investor relations activities	Investor relations staff identifiable and reachable through website(s)	Central Bank and government agency website(s) available in English	Reciprocal links to Central Bank, Ministry of Finance, and other government agency websites	Investors able to register for website subscription	Country subscribes to SDDS	Effective data transparency of market-relevant data	Macroeconomic data presented in market-friendly format	Historical policy information available	Forward-looking policy information available	Structural (legal, regulatory) information available	Active investor contact list	Web-based communication with investors	Bilateral meetings with investors	Non-deal roadshow(s)	Investor conference call(s)	Archives of investor presentations and/or conference call materials available on website(s)	Investor feedback reflected in policy decisions, per country	Senior policymakers accessible to investors	Regular self-assessment of investor relations activities	
	Weight	2	3	3	1	1	1	3	2	2	3	2	3	2	1	1	1	1	3	2	1	
Country	Score																					Country
Belize	7	0	0	3	0	0	0	1	0	0	0	2	0	0	1	0	0	0	0	0	0	Belize
Brazil*	38	2	3	3	1	1	1	3	2	2	3	2	3	2	1	1	1	1	3	2	1	Brazil*
Brazil (Gerin)	38	2	3	3	1	1	1	3	2	2	3	2	3	2	1	1	1	1	3	2	1	Brazil (Gerin)
Brazil (Treasury)	38	2	3	3	1	1	1	3	2	2	3	2	3	2	1	1	1	1	3	2	1	Brazil (Treas.)
Bulgaria	21	0	0	3	1	0	1	3	2	2	3	2	0	0	1	0	0	0	3	0	0	Bulgaria
Chile	36	2	3	3	1	1	1	3	2	2	3	2	3	2	1	1	0	0	3	2	1	Chile
China	3	0	0	0	0	0	0	0	0	0	0	2	0	0	1	0	0	0	0	0	0	China
Colombia	32	2	3	3	1	1	1	2	0	0	3	2	3	2	1	1	0	1	3	2	1	Colombia
Costa Rica	11	0	0	0	0	1	1	1	0	0	0	0	0	0	1	1	0	0	3	2	1	Costa Rica
Croatia	11	0	0	3	1	0	1	3	0	0	0	2	0	0	1	0	0	0	0	0	0	Croatia
Dominican Republic	34	2	3	3	1	1	0	3	2	0	3	2	3	2	1	1	0	1	3	2	1	Dom. Rep.
Egypt	13	0	0	3	0	0	1	2	0	2	0	2	0	0	1	0	0	0	0	2	0	Egypt
Gabon	2	0	0	0	0	0	0	1	0	0	0	0	0	0	1	0	0	0	0	0	0	Gabon
Ghana	8	0	0	3	0	0	0	0	0	2	0	2	0	0	1	0	0	0	0	0	0	Ghana
Hungary	32	2	3	3	0	1	1	3	2	2	3	2	3	0	1	0	0	0	3	2	1	Hungary
Indonesia	38	2	3	3	1	1	1	3	2	2	3	2	3	2	1	1	1	1	3	2	1	Indonesia
Kenya	10	0	0	3	1	0	0	1	0	2	0	2	0	0	1	0	0	0	0	0	0	Kenya
Korea	34	2	3	3	1	1	1	2	2	2	3	2	3	0	1	1	0	1	3	2	1	Korea
Lebanon	24	0	0	3	1	1	0	1	2	2	3	0	3	0	1	1	0	0	3	2	1	Lebanon
Malaysia	17	0	0	3	1	0	1	2	2	2	0	0	0	0	1	0	0	0	3	2	0	Malaysia
Mexico	34	2	3	3	0	1	1	3	2	2	3	0	3	2	1	0	1	1	3	2	1	Mexico
Morocco	19	2	3	3	0	1	1	1	2	0	0	0	3	2	1	0	0	0	0	0	0	Morocco
Nigeria	9	0	0	3	0	0	0	0	0	0	3	2	0	0	1	0	0	0	0	0	0	Nigeria
Pakistan	24	0	0	3	1	1	0	2	2	2	1	2	3	0	1	1	0	0	3	2	0	Pakistan
Panama	30	2	3	1	1	1	0	2	2	0	1	2	3	2	1	1	1	1	3	2	1	Panama
Peru	36	2	3	3	1	1	1	3	2	2	3	2	3	2	1	1	0	0	3	2	1	Peru
Philippines	34	2	3	3	1	1	1	2	0	2	3	2	3	2	1	1	0	1	3	2	1	Philippines
Poland	34	2	3	3	1	1	1	2	2	2	3	2	3	2	1	1	0	0	3	2	0	Poland
Romania	16	0	0	3	0	0	1	1	0	2	0	2	3	0	1	0	0	0	3	0	0	Romania
Russia	9	0	0	3	0	1	1	3	0	0	0	0	0	0	1	0	0	0	0	0	0	Russia
South Africa	36	2	3	3	1	1	1	3	2	2	3	2	3	2	1	1	0	0	3	2	1	South Africa
Tanzania	4	0	0	3	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	Tanzania
Thailand	21	0	0	3	1	1	1	2	0	2	0	2	3	0	1	0	0	0	3	2	0	Thailand
Tunisia	6	0	0	0	0	0	1	2	0	0	0	2	0	0	1	0	0	0	0	0	0	Tunisia
Turkey	38	2	3	3	1	1	1	3	2	2	3	2	3	2	1	1	1	1	3	2	1	Turkey
Ukraine	11	0	0	0	0	0	1	1	0	0	0	2	3	0	1	0	0	0	3	0	0	Ukraine
Uruguay	32	2	3	3	1	1	1	3	2	2	0	2	3	0	1	1	0	1	3	2	1	Uruguay
Venezuela	10	0	0	0	1	1	0	2	0	0	0	0	3	2	1	0	0	0	0	0	0	Venezuela
Vietnam	9	0	0	0	0	0	0	0	0	0	0	2	3	0	1	0	0	0	3	0	0	Vietnam
Zambia	4	0	0	3	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	Zambia

*Reflects a combined score of the Gerin office at the Banco Central do Brasil and the IRU office at the National Treasury.

Table 3. Assessment of Data Dissemination Practices (Prioritized)

Elements in Data Practices		Central Government Operations (CGO) **							Central Government Debt (CGD) ***				
		SDDS subscriber*	CGO periodicity	CGO timeliness	Time series availability	Domestic and external financing availability	MGFS 1986 (cash accounting)	GFSM 2001 or transition toward GFSM 2001 (accrual accounting)	CGD timeliness	CGD debt periodicity	Time series availability	Domestic and external debt breakdown availability	Contingent liabilities availability
	Weight	2	1	2	3	1	1	3	2	1	3	1	2
Country	Score												
Belize	16	1	1	0	3	0	0	0	0	1	3	1	0
Brazil	39	2	1	2	3	1	1	0	2	1	3	1	2
Bulgaria	35	2	1	2	3	1	1	3	2	1	3	1	2
Chile	41	2	1	2	3	1	1	3	2	1	3	1	2
China	8	1	1	2	0	0	0	3	0	0	0	1	0
Colombia	32	2	1	2	3	1	1	0	2	1	3	1	2
Costa Rica	26	2	1	2	0	1	1	0	2	1	3	1	2
Croatia	37	2	1	0	3	1	1	3	2	1	3	1	2
Dom. Rep.	39	1	1	2	3	1	1	3	2	1	3	1	2
Egypt	37	2	0	2	3	1	1	3	2	1	3	1	2
Gabon	15	1	1	0	0	1	0	0	2	1	0	1	0
Ghana	12	1	1	0	3	1	1	0	2	1	0	0	0
Hungary	37	2	1	2	3	1	1	3	2	1	3	1	2
Indonesia	39	2	1	2	3	1	1	3	2	1	3	1	2
Kenya	24	1	1	0	3	1	1	0	2	1	3	1	2
Korea	30	2	1	2	3	1	1	0	2	1	3	1	2
Lebanon	26	1	1	2	3	1	1	0	2	1	3	1	0
Malaysia	26	2	1	2	3	1	1	0	2	1	3	1	2
Mexico	37	2	1	2	3	1	1	0	2	1	3	1	2
Morocco	36	2	1	2	3	1	1	0	2	1	3	1	2
Nigeria	13	1	1	2	0	1	1	0	2	1	0	0	0
Pakistan	28	1	1	0	3	1	1	3	2	1	3	1	2
Panama	25	1	1	1	3	1	1	0	2	1	3	1	0
Peru	38	2	1	2	3	1	1	3	2	1	3	1	0
Philippines	28	2	1	2	3	1	0	0	2	1	0	1	2
Poland	37	2	1	2	3	1	1	3	2	1	3	1	2
Romania	33	2	1	2	3	1	1	0	2	1	3	1	2
Russia	35	2	1	0	3	1	1	3	2	1	3	1	0
South Africa	39	2	1	2	0	1	1	3	2	1	3	1	2
Tanzania	19	1	1	2	3	1	1	0	2	1	3	1	0
Thailand	34	2	1	2	3	1	0	3	2	1	3	1	2
Tunisia	28	2	1	2	3	1	1	0	2	1	3	1	2
Turkey	42	2	1	2	3	1	1	3	2	1	3	1	2
Ukraine	25	2	1	2	3	1	1	0	2	1	3	1	2
Uruguay	39	2	1	2	3	1	1	0	2	1	3	1	2
Venezuela	31	1	1	0	3	1	1	0	2	0	3	1	2
Vietnam	4	1	0	0	0	0	0	0	0	0	0	0	0
Zambia	9	1	1	0	0	1	1	0	2	1	0	1	0

* Countries subscribing to the IMF Special Data Dissemination Standard (SDDS).

** Central Government Operations (CGO):
Timeliness: 1 month after the end of the reference period
Periodicity: Monthly
MGFS 1986: Identifies countries that use classification of fiscal statistics according to the IMF's *A Manual of Government Finance Statistics, 1986* (MGFS 1986).
GFSM 2001: Identifies if government accounting follows the definition and classification of the IMF's *Government Finance Statistics Manual, 2001* (GFSM 2001).

*** Central Government Debt (CGD):
Timeliness: 1 quarter after the end of the reference period
Periodicity: Quarterly
Amortization Schedule for CGD:
Preferably, dissemination of government debt service presented at least annually for a period of at least five years from the effective date of the debt data.
Annual data should be supplemented with quarterly data at least for the year immediately ahead.

Central Government Debt (CGD) ***			External Debt****								
Term break-down done by original maturity	Amortization schedule disseminated at least every 3 months	Amortization schedule presents contingent liabilities	External debt timeliness	External debt periodicity	Time series availability	Resident holdings of public debt issued internationally	Non-resident holdings of public debt issued domestically	Non-resident holdings of private debt issued domestically	Amortization schedule disseminated at least every 6 months	Amortization schedule presents private and public sector separation	
1	3	2	2	1	3	1	1	1	3	2	
											Country
0	0	0	2	1	3	0	0	0	0	0	Belize
1	3	2	2	1	3	1	1	1	3	2	Brazil
1	3	0	2	1	3	1	1	1	0	0	Bulgaria
1	3	2	2	1	3	1	0	1	3	2	Chile
0	0	0	0	0	0	0	0	0	0	0	China
1	3	0	2	1	3	1	1	1	0	0	Colombia
1	0	2	2	1	3	1	0	0	0	0	Costa Rica
1	3	0	2	1	3	0	1	1	3	2	Croatia
1	3	2	2	1	3	1	1	1	3	0	Dom. Rep.
1	3	0	2	1	3	1	0	0	3	2	Egypt
1	3	0	2	1	0	0	0	1	0	0	Gabon
1	0	0	0	1	0	0	0	0	0	0	Ghana
1	3	0	2	1	3	1	1	1	2	0	Hungary
1	3	0	2	1	3	0	1	1	3	2	Indonesia
0	0	0	0	1	3	1	0	1	0	2	Kenya
1	3	0	2	1	3	0	1	0	0	0	Korea
1	3	0	2	1	3	0	0	0	0	0	Lebanon
1	0	0	2	1	3	0	0	0	0	0	Malaysia
1	3	0	2	1	3	1	1	1	3	2	Mexico
1	3	2	2	1	3	0	1	1	3	0	Morocco
1	0	0	2	1	0	0	0	0	0	0	Nigeria
1	0	0	2	1	3	0	1	1	0	0	Pakistan
1	0	0	2	1	3	0	0	0	3	0	Panama
1	3	0	2	1	3	1	1	1	3	2	Peru
1	3	0	2	1	3	1	1	1	0	0	Philippines
1	3	0	2	1	3	1	1	1	0	2	Poland
1	0	0	2	1	3	0	1	1	3	2	Romania
1	3	0	2	1	3	0	1	1	3	2	Russia
1	3	2	2	1	3	1	1	1	3	2	South Africa
0	0	0	2	1	0	0	0	0	0	0	Tanzania
1	0	0	2	1	3	0	1	0	3	2	Thailand
1	0	0	2	1	3	0	1	1	0	0	Tunisia
1	3	2	2	1	3	1	1	1	3	2	Turkey
1	0	0	2	1	0	0	1	1	0	0	Ukraine
1	3	2	2	1	3	1	1	1	3	2	Uruguay
1	3	0	2	1	3	1	1	1	3	0	Venezuela
0	0	0	2	1	0	0	0	0	0	0	Vietnam
0	0	0	0	0	0	0	1	0	0	0	Zambia

Timeliness: 1 quarter after the end of the reference period
Periodicity: Quarterly

**** External Debt:
Timeliness: 1 quarter after the end of the reference period
Periodicity: Quarterly
Amortization Schedule for External Debt:
It is important that data cover both public and private sector debt.
Preferably, amortization payments presented at least annually for a period of at least five years from the effective date of the debt data.
Annual data should be supplemented with quarterly data at least for the year immediately ahead.
Timeliness: 1 quarter after the end of the reference period
Periodicity: Quarterly

creditors regarding economic policy developments can play a key role in allowing market participants to better assess the authorities' policy and plans objectives.[1] More generally, the *Principles* can help strengthen the international financial system by encouraging countries to fill data gaps through improved dissemination. The IIF website provides links to the sovereign websites and contact information for persons responsible for communication with investors.[2]

Sovereign issuers are investing more effort in improving IR practices, as evidenced by continual improvements in rankings over the years. Countries with high data scoring typically complement those best practices with strong investor outreach, including conference calls and non-deal roadshows. It is encouraging to note that countries recently accessing international capital markets for the first time have dedicated more resources to improve IR as well as data dissemination practices. The efforts of Turkey, Peru, Ghana, the Russian Federation, Pakistan, and Nigeria are detailed in Section V below.

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[1] See Appendix B for the differences between investor relations offices and investment promotion agencies.
[2] See http://www.iif.com/emp/ir.

V. Country Innovations in Investor Relations and Data Transparency

Innovations in Funding Sources

Several emerging market issuers have diversified or expanded their sources of market funding through new issues of sukuk bonds and Samurai bonds. These initiatives are reviewed in Box 8.

Turkey Advances Data Dissemination Practices

Leveraging on active IR practices and a sound statistical data system, the Turkish authorities have stepped up their efforts to meet international standards for data dissemination, which was reflected in Turkey's increased ranking in the IIF's data dissemination assessments. In particular, in compliance with the Public Financial Management and Control Law, the Ministry of Finance, in close coordination with the Turkish Treasury, has initiated the compilation and dissemination of fiscal statistics for central government operations on an accrual basis broadly in line with the *European System of Accounts 1995* and the IMF's *Government Finance Statistics Manual, 2001*.

The IMF reports that the scope and quality of data coverage has steadily improved in other areas. Contingent liabilities in the form of Treasury-

Box 8. New Funding Sources for Emerging Market Issuers

With tightening credit markets and worsening international funding conditions for every asset class, emerging markets have witnessed the search by investors for quality high-yield securities. This yield search coincided with a general trend of a flight to safety and heightened risk aversion and has shifted market attention to new sources of financing for emerging markets.

The international issuance of bonds based on Islamic banking principles (the global sukuk market) represents an active part of the Islamic financial system and is increasingly gaining visibility and demonstrating remarkable growth. This expansion has been led by regular issuers such as Malaysia and Indonesia. Indonesian sukuk issuances have grown considerably since the country launched a sukuk program for project financing in late 2011. Indonesia is currently in the process of constructing a regulatory framework for Islamic capital markets. This process was launched in June 2008, when the country passed a Sukuk Law, which established a body charged with approving all Sharia financial products and services.

However, inaugural sovereign issuances that are under way from other countries, such as South Africa, Nigeria, and Turkey, will further strengthen the sovereign sukuk market and diversify the access to credit by emerging market sovereign issuers. South Africa is preparing to launch sub-Saharan Africa's first sukuk bond, paving the way for issues by other countries in the region. The amount of the inaugural sukuk is potentially US$500 to US$700 million. A successful debut by South Africa could then encourage Kenya and Nigeria to follow suit, as they have also been planning sukuk issues. Turkey issued its first sukuk in September 2012, and will subsequently issue a lira-denominated sukuk. Countries such as Egypt and Tunisia are also reportedly developing their regulatory environments for future sukuk issuances for 2013 and beyond.

New issues of Samurai bonds are also envisaged. In addition to a planned $1 billion of global sukuk, Indonesia also plans to issue $750 million in yen-denominated bonds in 2012, following its first successful sale of 10-year yen-denominated bonds in 2009. Indonesia has benefited from upgrades of its sovereign debt to investment grade, by both Fitch in December 2011 and Moody's in January 2012. Furthermore, Indonesia has signaled its intent to issue bonds denominated in the currencies of China and South Korea next year. Poland also issued in March 2012 a 25-billion-yen five-year Samurai at a coupon of 1.49%, the first retail-targeted transaction of a foreign issuer on the Japanese market in 2012. In other yen-denominated sales, Mexico concluded a $1 billion issue of Samurai bonds in June 2012 in two tranches—three-year notes at 1.29% and five-year bonds at 1.56%—taking advantage of low costs and investor interest.

Finally, Mexico carried out a successful swap of global bonds during summer 2012, reopening several long-term issues, including its 100-year bond. The swap allowed Mexico to lengthen the average maturity profile of its public debt by more than two years.

guaranteed debt and repayments are displayed under General Government Debt, publicly available on the Treasury's website. Stock and repayment projections of contingent liabilities are estimated for the following three years, available in a monthly debt management report.

Peru Enhances Relations With Investors

Since the formal setting-up of Peru's Investor Relations Office in 2006, Peru's Ministry of Economy and Finance has gradually strengthened its IR practices, supporting the debt management framework in place. Amid a challenging global environment, Peru's debt management was instrumental in the implementation of countercyclical fiscal policy.

Proactive IR practices, including the dissemination of fiscal reports tailored to investors' needs, have been instrumental in the government's efforts to gain market confidence and minimize financial market volatility. Against the background of deteriorating global economic conditions, the country's investment-grade status has been further consolidated by recent rating upgrades by S&P and Moody's.

The Investor Relations Office conducts user satisfaction surveys on an annual basis, aimed at improving the availability of its publications.

Efforts Under Way to Strengthen Ghana's Debt Management Framework

Ghana's debut Eurobond in 2007 has provided impetus for upgrading the country's debt management framework and its statistical system. The nascent debt management framework in the country is advancing with the preparation of a three-year debt management strategy under the recently strengthened Debt Management Division of Ghana's Ministry of Finance. The dissemination of Ghana's statistics has advanced, as the country currently subscribes to the IMF's General Data Dissemination Standard. Ongoing projects to enhance the compilation and dissemination of Ghana's statistics include the presentation of higher frequency national accounts data with assistance from the IMF and the UK Department for International Development (DFID).

The positive sentiment by local and international lenders toward Ghana's economic prospects has helped generate interest for investing in Ghana (especially in new oil production and in the construction sector) and supported the demand for Ghana's sovereign bonds.

Ghana has successfully completed the issuance of a five-year bond, with the proceeds earmarked to fund several infrastructure projects. This is Ghana's second five-year bond issued this year and the fourth medium- to long-term bond issued this year.

The Russian Federation's Transition to Active Debt Management

Capitalizing on its investment-grade status and pent-up demand for its sovereign bonds, the Russian Federation has remained an active player in international capital markets, including by placing, among others, the largest Eurobond issued in local currency by a major emerging market in March 2011.

Despite the uncertain external financial environment, and in order to maintain a regular presence of the country in international capital markets, the Russian Federation has formalized the implementation of an active sovereign debt management program. It has established the Russian Financial Agency within the Ministry of Finance, to be in charge of nurturing Russia's relations with investors. Going forward, adherence to the work program described in the *Public Debt Management Policy of the Russian Federation for 2012–2014* will facilitate authorities' goals, including a permanent and effective communication channel with the investor community. The Ministry of Finance has further laid the groundwork for enhanced communication with investors by providing a subscription service for press releases and other relevant information. Russia's improved scoring in the IR index reflects this change. As the scope of information available through the Ministry improves, this will serve as a critical vehicle to deliver timely information directly to market participants.

Pakistan Makes Strides Toward Implementing a Medium-Term Budgetary Framework

Since 2003, Pakistan has successfully been

implementing in stages several steps to establish a Medium-Term Budgetary Framework, with technical assistance supported by the DFID. Complementing these efforts, Pakistan has made economic and debt data increasingly available through the Pakistan State Bank website, in market-friendly excel format with a database of noteworthy archives.

Nigeria Publishes Medium-Term Expenditure Framework

As of late 2011, the Nigerian Budget Office has made available on its website the country's Medium-Term Expenditure Framework (MTEF). Since 2007, Section 11 of the Fiscal Responsibility Act requires the Minister of Finance to prepare the MTEF along with a Fiscal Strategy Paper (FSP) and provide them to the Federal Executive Council and the National Assembly for consideration.

The MTEF is composed of the macroeconomic framework, providing analysis of key macroeconomic trends and insight on forward-looking budgetary direction. The FSP outlines the country's fiscal strategy; analyzes expenditure and revenue figures for the years under review; details the assumptions underlying these projections; reviews implementation of the previous budget; and provides an overview of the consolidated public debt, including an assessment of its potential risks.

Nigeria has gained prominence in the sub-Saharan market recently, being the fourth sovereign to issue an international bond in the region. In January 2011, it debuted in international capital markets with a $500 million Eurobond issue. In response, JPMorgan has since announced that it will add Nigeria to its Government Bond–Emerging Markets Index in three phases beginning in October 2012. The greater visibility is expected to encourage further improvements in the transparency of Nigeria's public finances. Despite several shortcomings in the compilation and dissemination of macroeconomic data, including those for the fiscal sector, investors consider the presentation of Nigeria's fiscal framework a welcome step toward greater transparency and enhanced communication of the authorities' policies.

Appendix A. Evaluation Criteria for Investor Relations Programs

Described in this section are the 20 criteria that have been used to assess IR practices in this report, as well as the three key categories of data dissemination.

Presence of institutionalized IR activities
A formal IRP is characterized by an Investor Relations Office (IRO), designated IR officers, and an IR website. The office may be an independent entity or a department within another financial agency, such as the Ministry of Finance (or Treasury), or Central Bank. Most IROs maintain a separate website; however, in some cases IROs share a website with another government agency. In some cases a country can have institutionalized IR activities without having a formal IRP. The country must have these functions built into the existing framework of the Central Bank, Ministry of Finance, or government agency responsible for debt management. There must be staff responsible for communication with investors who fulfill these duties and are recognized by investors as reliable and accessible.

IR staff identifiable and reachable through website(s)
One or more official websites must contain contact information of at least one individual identified as an IR staff member and available to receive investor questions or comments. The information should be clearly marked and easy to access. The appropriate official may be either a designated IR officer or responsible for investor communications as one of his or her core duties. General information for webmasters or staff listings of those who are not responsible for IR functions does not meet this criterion.

Central Bank and government agency websites available in English
An IRO website in English is sufficient to meet this criterion. If there is not an IRO website, both the Central Bank and Ministry of Finance (or Treasury) websites must be in English. Ideally, the statistics agency website and other additional government agency websites will be published in English, but it is not a requirement to meet this criterion.

Reciprocal links to IRO, Central Bank, and Ministry of Finance websites
Key websites include the IRO, Central Bank, and Ministry of Finance (or Treasury) websites. This criterion is not met if one agency website contains links, but others do not reciprocate. Additional links to government agencies such as the debt management agency or national statistics office are recommended but not required to meet this criterion.

Investors able to register for website subscription
Investors can register on the IRO, Central Bank, or Ministry of Finance (or Treasury) website to subscribe to the website and receive relevant information such as data releases, policy information, or notices about roadshows or conference calls on a regular basis via email.

Country subscribes to SDDS
The country must subscribe to the IMF's SDDS, which was established by the IMF to guide members that have or that might seek access to international capital markets in the provision of their economic and financial data to the public. The SDDS identifies four dimensions of data dissemination: (1) data coverage, periodicity, and timeliness; (2) access by the public; (3) integrity of the disseminated data; and (4) quality of the disseminated data. For each dimension, the SDDS prescribes two to four monitorable elements—good practices that can be observed, or monitored, by the users of statistics.

Effective data transparency of key elements
Country authorities must disseminate key data related to central government operations, central government debt, and external debt in a timely manner. (See section on data transparency for

further detail.) Countries that meet this criterion score 15 or more out of a total of 42 points with respect to timeliness and periodicity criteria for these three areas of data. In addition, the effectiveness of dissemination has been evaluated on a 3-point scale, with the maximum points awarded to countries with the highest levels of data transparency.

Macroeconomic data presented in market-friendly format

To qualify for this criterion, data are presented in a format that can be easily manipulated in Microsoft Excel. Some data should be available in time series. Policy information is provided on one or more websites in a clear, succinct format that delivers the central points that authorities are seeking to convey. Countries must provide data and policy information on one or more websites in English.

Historical policy information available

Investors are able to locate recent retrospective policy information for various areas of data per the IMF's SDDS.

Forward-looking policy information available

Investors are able to identify the country's economic policy planning through the presentation of comprehensive economic outlook reports for the relevant period. This includes the identification of monetary and fiscal policy objectives, as well as assumptions of the economic variables relevant for the individual country. The presentation of the country's debt management strategy is encouraged but not required to meet this criterion.

Structural information available

Information on structural factors (e.g., legal, regulatory, governance frameworks) supported by the data must be available as appropriate.

Active investor contact list

Country authorities maintain a list of investors to meet this criterion. Ideally, authorities update and maintain their investor contact lists at least twice annually, and the officials from one or more government agencies should distribute policy and macroeconomic information to the investor list via email at least every 2 weeks.

Web-based communication with investors

Authorities respond to investor queries or concerns via email or via an HTML-based feedback mechanism. To meet this criterion, a general email box, specific email address, or HTML-based form must be provided on the IRO, Central Bank, or Ministry of Finance (or Treasury) websites. Responses should be received within 36 hours to fulfill this criterion.

Bilateral meetings with investors

Country authorities conduct bilateral meetings with investors on a regular basis. The meetings may be held domestically or abroad.

Non-deal roadshow(s)

Country authorities must conduct one or more non-deal roadshows annually.

Investor conference call(s)

Country authorities conduct regular investor conference calls on key economic data and policies at least every quarter. To qualify for this criterion, the call must be public. Investors should be invited via email and/or an announcement on a government agency website. The call should be led by the IRO head and senior department heads, with involvement of senior policymakers such as the Undersecretary of Finance or Deputy Governor of the Central Bank as needed. "Closed" calls, meaning that only a small group of investors is invited and the date and time of the call is not published on the website, do not qualify for this criteria.

Archives of investor presentations and/or conference call–related materials available on websites

Relevant official websites must contain an archive of materials presented to investors at roadshows, conference calls, or other meetings or seminars. Materials may include conference call replay and associated documents, investor presentations, and transcripts of speeches by key policymakers.

Investor feedback reflected in policy decisions
To fulfill this criterion, senior policymakers should have taken market input into account in their policy decisions. This criterion has been assessed on the basis of survey responses by country authorities and does not account for investor perceptions of whether feedback has been reflected in policy decisions.

Senior policymakers' participation in IR activities
Participation by senior policymakers (Minister, Central Bank Governor, or one of their deputies) is necessary when appropriate. Increasing involvement of senior policymakers is particularly significant at times of diminishing market confidence. To meet this criterion senior policymakers must be involved in at least two of the following three activities: (1) conference calls, (2) bilateral meetings, and (3) non-deal roadshows.

Regular self-assessment of IRP
Country authorities must conduct regular self-assessments of their IR efforts on an annual basis to identify successes and gaps. The self-assessment may be conducted through a survey distributed to the entire investor base or to a representative sample of the investor base.

DATA DISSEMINATION PRACTICES

We have assessed countries on the basis of 24 elements of data transparency. In addition to a country's subscription to the SDDS or GDDS, these elements capture six categories in the area of central government operations, eight categories in the area of central government debt, and eight categories in the external debt area. One critical area not covered in this report is financial sector information. Despite much progress—especially by the IMF and the World Bank—to assess financial sector vulnerabilities through Financial Sector Assessment Programs (FSAPs), few emerging markets have reporting systems in place that would allow regular dissemination of key financial sector indicators to the marketplace. At the same time, investors have expressed concern about the cross country comparability of data, for example, due to a lack of uniform definition of key data. Therefore, we have not attempted to capture data release in this important area.

Central government operations
Elements of timeliness and periodicity have been evaluated against the prescribed and encouraged elements set by the SDDS and IIF standards for central government operations. Special emphasis has been placed on compliance with encouraged data provision in this area.

With the introduction of the IMF's Government Finance Statistics Manual in 2001 (GFSM 2001), countries have gradually incorporated an accrual-based reporting system for the presentation of central government operations data. However, this methodology is significantly more time consuming, and progress has been modest. Moreover, the statistical expertise varies across countries. In our assessments, we have documented the progress toward the adoption of the GFSM 2001 standards.

We also have identified countries that have adopted a formal process toward implementation.

Central government debt
Individual assessments describe the current practices for the release of central government debt data assessed against the prescribed and encouraged elements of the SDDS and IIF standards for central government debt. In addition, we have placed special emphasis on data dissemination practices for government debt service projections. The IMF and IIF standards encourage quarterly reporting of interest and amortization on medium- and long-term debt for the next four quarters and then annually thereafter. Similarly, reporting of data on short-term debt falling due on a quarterly basis is encouraged.

We have identified instances in which amortization schedules are presented in a timely fashion, either as part of a particular report or in a section of the fiscal authority's website. Whenever the information is not presented in periodic publications available to the public, we have benefited from direct consultation with agencies involved in the compilation of fiscal statistics. Indeed, several countries are ready to provide the calendar of future debt payments upon request.

External debt
Disclosure of external debt data can be evaluated based on the criteria established by the IMF's SDDS and IIF data standards. Most countries covered in this exercise follow the template set by the SDDS with three levels of disaggregation: (1) by institutional sector, (2) by short-term and long-term maturities on an original maturity basis, and (3) by instrument. We also have reviewed the dissemination practices for the provision of more comprehensive and timely information in areas that are not prescribed by those standards, including the availability of debt amortization schedules, the relevant breakdowns by institutional sector, and the timely availability of those schedules.

In the case of external debt amortization schedules, our assessment of dissemination practices shows that Central Banks usually prepare and release this information. However, provision of central government debt data varies considerably across countries; in some cases, analysts will search hard to locate the schedule. Also, countries rarely meet the IIF's encouraged element of providing quarterly data for at least the immediate 12-month period.

Some data categories, which are neither prescribed nor encouraged by the IMF's SDDS, are nevertheless provided on an ad hoc basis. For example, ratings agencies often use external debt ratios as indicators of debt sustainability. We have identified cases in which countries disclose this information on an ad hoc basis outside of the SDDS framework.

Additional aspects explored in the individual country assessments include the identification of resident holdings of public debt issued internationally, the non-resident holdings of public debt issued domestically, and the non-resident holdings of private debt issued domestically.

Appendix B. Differences Between Sovereign Investor Relations Offices and Investment Promotion Agencies

Investment Promotion Agencies (IPAs) and Investor Relations Offices (IROs) share many elements, but are unique in purpose. Proactive investor relations (IR) practices by an IRO support investment in the public sector through the management of sovereign debt instruments, while IPAs promote private sector investment. One cannot be viewed as a substitute for the other; due to their unique approach and goals, it is recommended that IROs and IPAs function separately.

While they are both government agencies designed to provide information to investors, the information they provide and the investors they target are quite different. Both convey targeted information to prospective investors via websites and in response to investment inquiries.

IPAs help to facilitate foreign direct investment (FDI) by advertising investment opportunities to multinational corporations interested in making overseas investments. IPAs help match foreign private companies and local private companies. Operationally, IPAs utilize traditional marketing and advertising techniques such as slogans and branding.

In contrast, IROs are defined by their straightforward approach. IROs can be located within the Ministry of Finance or the Central Bank. If a country does not have an institutionalized IRO, the function of communicating with investors is typically carried out by the debt management office or the government agency responsible for sovereign debt management. IROs are designed to be an institutionalized communication channel between sovereign debt issuers and investors. It is important that the information conveyed to investors be delivered directly by government officials as opposed to third-party analysts. The purpose is to establish open two-way communication that promotes trust between the policymakers and investors.

On a day-to-day basis, IROs facilitate the communication between investors and country authorities. In addition, IROs play a broader role in increasing the stability of the financial system. The financial crises that have occurred over the past decade have galvanized actions by the international financial community to limit the severity and frequency of such crises, as well as to bolster the financial system more broadly. IROs have proven to be important pillars for helping avoid crises and are also crucial building blocks for a more effective approach to managing them.

An increasing number of emerging market authorities and market participants agree that IR programs are proven vehicles for advancing dialogue with investors, building on the delivery of data on key economic variables, and improving financial policies and performance. Regular, proactive strategies of IR programs enable country authorities to understand and communicate more effectively with their investor base, address concerns or questions, and shape market-informed policies.

Regular interaction with key officials regarding economic data, financial policies, and economic performance enables investors to make sound lending and investment decisions and provide feedback to country authorities. Such programs can also help authorities navigate through turbulent periods of market sentiment. When market conditions deteriorate, IROs allow policymakers to distinguish themselves within their asset class. Conversely, IROs strengthen the ability of investors to assess and manage risks.

Press and IR

The press office and IRO need to coordinate their activities because the message of both of these offices has to be consistent. A press office and an IRO can benefit from working closely together, as a press release from the press office may also be circulated by the IRO. A press release issued by the press office is not a substitute for IR. Sophisticated investors require a more detailed explanation of recent developments and policies. Following a press release, it is important for the IRO to be prepared to provide more detailed information on request.

Several authorities have explored co-mingling press and IR functions. Press and IR should be kept separate as the job of the IRO is to establish two-way communication with investors. Press officers deliver information in only one direction and do not need to be tuned into the market. The scope of a press office is far-reaching, while the focus of an IRO is specific to debt investors.

Annex I. Principles for Stable Capital Flows and Fair Debt Restructuring[1]

PREFACE

Since the mid-1990s, sovereign debtors and their private sector creditors have generally sought to put in place policies and procedures likely to promote and maintain sustained market access.

Most issuers have recognized the importance of implementing sound economic and financial policies (including monetary, exchange rate, and debt management policies), as well as developing domestic public support for those policies. Equally important are policies that preserve the rule of law and, in particular, maintain the sanctity of contracts, as well as other measures needed to advance an open investment environment. In maintaining sound policies, debtors have been guided by internationally accepted standards and codes to strengthen financial stability and to enhance transparency by providing timely economic and financial data.

For their part, most creditors make investment and lending decisions on their own merit, accept full responsibility for these decisions, and do not expect official sector bail-outs. As part of this process, creditors have sought to implement good practices in risk management, including thorough analysis of a borrowing country's implementation of sound economic and financial policies, as well as adherence to key standards and codes.

More recently in a significant step toward strengthening the resilience of the system, most debtors and their creditors have opted for the voluntary inclusion of collective action clauses (CACs) in international bond terms and conditions. These bonds have provided for amending payment terms through supermajority voting and for limiting precipitous legal actions through higher acceleration hurdles; a few bonds have also included provisions for debtor-creditor engagement.

In a growing number of cases, both issuers and creditors have pursued effective, two-way communication through robust investor relations programs (IRPs). This communication includes information and data on the issuer's key economic and financial policies and performance, with creditors providing feedback.

The *Principles* outline actions and behavior of private sector creditors and emerging market sovereign debtors to promote and maintain stable private capital flows to emerging market economies in the context of growth and financial stability. They are based on extensive and broadly based discussions among private creditors and sovereign emerging market issuers. Because individual cases will invariably involve different circumstances, the *Principles* should be applied flexibly on a case-by-case basis and are strictly voluntary. Accordingly, no party is legally bound by any of the provisions of these *Principles,* whether as a matter of contract, comity, or otherwise. Moreover, nothing in these *Principles* (or in any party's endorsement thereof) shall be deemed to constitute a waiver of any such party's legal rights.

The *Principles* build on the progress since the mid-1990s to identify effective measures in order to shore up crisis prevention and encourage their continued implementation. The *Principles* promote early crisis containment through information disclosure, debtor-creditor consultations, and course

[1] The *Principles* were launched in 2004 and welcomed and supported by the G20 Finance Ministers and Central Bank Governors in their meetings in Berlin, Germany, on November 20–21, 2004, and in Xianghe, Hebei, China, on October 15–16, 2005. During the annual meeting of the Group of Trustees on October 10, 2010, the Trustees agreed to broaden the applicability of the *Principles* to go beyond the traditional emerging market sovereign issuers to encompass on a voluntary basis all sovereign issuers, as well as cases of debt restructuring in which the state plays a major role in influencing the legal and other key parameters of debt restructuring, based on the recommendation of a PCG Working Group on the Applicability of the *Principles.* The Group of Trustees also agreed to drop the reference to emerging markets from the title of the *Principles.* For more details, see Annex II of the October 2010 *Report of the PCG on the 2010 Implementation of the Principles for Stable Capital Flows and Fair Debt Restructuring.*

correction before problems become unmanageable. They also support creditor actions that can help to minimize market contagion. In cases where the debtor can no longer fulfill its payment obligations, the *Principles* outline a process for market-based restructuring based on negotiations between the borrowing country and its creditors that involve shared information, are conducted in good faith, and seek to achieve a fair outcome for all parties. Such a process maximizes the likelihood that market access will be restored as soon as possible under sustainable macroeconomic conditions.

PRINCIPLES

1. Transparency and Timely Flow of Information

General disclosure practice. Issuers should ensure through disclosure of relevant information that creditors are in a position to make informed assessments of their economic and financial situation, including overall levels of indebtedness. Such disclosure is important in order to establish a common understanding of the country's balance of payments outlook and to allow creditors to make informed and prudent risk management and investment decisions.

Specific disclosure practice. In the context of a restructuring, the debtor should disclose to all affected creditors maturity and interest rate structures of all external financial sovereign obligations, including the proposed treatment of such obligations; and the central aspects, including assumptions, of its economic policies and programs. The debtor should inform creditors regarding agreements reached with other creditors, the IMF, and the Paris Club, as appropriate. Confidentiality of material non-public information must be ensured.

2. Close Debtor-Creditor Dialogue and Cooperation to Avoid Restructuring

Regular dialogue. Debtors and creditors should engage in a regular dialogue regarding information and data on key economic and financial policies and performance. IRPs have emerged as a proven vehicle, and countries should implement such programs.

Best practices for investor relations. Communication techniques should include creating an investor relations office with a qualified core staff; disseminating accurate and timely data/information through email or investor relations websites; establishing formal channels of communication between policymakers and investors through bilateral meetings, investor teleconferences, and videoconferences; and maintaining a comprehensive list of contact information for relevant market participants. Investors are encouraged to participate in IRPs and provide feedback on such information and data. Debtors and investors should collaborate to refine these techniques over time.

Policy action and feedback. Borrowing countries should implement economic and financial policies, including structural measures, so as to ensure macroeconomic stability, promote sustainable economic growth, and thereby bolster market confidence. It is vital that political support for these measures be developed. Countries should closely monitor the effectiveness of policies, strengthen them as necessary, and seek investor feedback as warranted.

Consultations. Building on IRPs, debtors should consult with creditors to explore alternative market-based approaches to address debt service problems before default occurs. The goal of such consultations is to avoid misunderstanding about policy directions, build market confidence on the strength of policy measures, and support continuous market access. Consultations will not focus on specific financial transactions, and their precise format will depend on existing circumstances. In any event, participants must not take advantage of such consultations to gain a commercial benefit for trading purposes. Applicable legal restrictions regarding material non-public information must be observed.

Creditors' support of debtor reform efforts. As efforts to consult with investors and to upgrade policies take hold, the creditor community should consider, to the extent consistent with their business objectives and legal obligations, appropriate requests for the voluntary, temporary maintenance of trade

and inter-bank advances, and/or the rollover of short-term maturities on public and private sector obligations, if necessary to support a borrowing country's efforts to avoid a broad debt restructuring. The prospects of a favorable response to such requests will be enhanced by the commitment to a strong adjustment program, but will also depend in part on continued interest payments on inter-bank advances and continued service of other debt.

3. Good-Faith Actions

Voluntary, good-faith process. When a restructuring becomes inevitable, debtors and creditors should engage in a restructuring process that is voluntary and based on good faith. Such a process is based on sound policies that seek to establish conditions for renewed market access on a timely basis, viable macroeconomic growth, and balance of payments sustainability in the medium term. Debtors and creditors agree that timely good-faith negotiations are the preferred course of action toward these goals, potentially limiting litigation risk. They should cooperate in order to identify the best means for placing the country on a sustainable balance of payments path, while also preserving and protecting asset values during the restructuring process. In this context, debtors and creditors strongly encourage the IMF to implement fully its policies for lending into arrears to private creditors where IMF programs are in place, including the criteria for good-faith negotiations.

Sanctity of contracts. Subject to their voluntary amendment, contractual rights must remain fully enforceable to ensure the integrity of the negotiating and restructuring process. In cases where program negotiations with the IMF are under way or a program is in place, debtors and creditors rely upon the IMF in its traditional role as guardian of the system to support the debtor's reasonable efforts to avoid default.

Vehicles for restructurings. The appropriate format and role of negotiation vehicles such as a creditor committee or another representative creditor group (hereafter referred to as a "creditor committee") should be determined flexibly and on a case-by-case basis. Structured, early negotiations with a creditor committee should take place when a default has occurred in order to ensure that the terms for amending existing debt contracts and/or a voluntary debt exchange are consistent with market realities and the restoration of growth and market access and take into account existing CAC provisions. If a creditor committee is formed, both creditors and the debtor should cooperate in its establishment.

Creditor committee policies and practices. If a creditor committee is formed, it should adopt rules and practices, including appropriate mechanisms to protect material non-public information; coordinate across affected instruments and with other affected creditor classes with a view to form a single committee; be a forum for the debtor to present its economic program and financing proposals; collect and analyze economic data; gather, evaluate, and disseminate creditor input on financing proposals; and generally act as a communication link between the debtor and the creditor community. Past experience also demonstrates that, when a creditor committee has been formed, debtors have borne the reasonable costs of a single creditor committee. Creditors and debtors agree jointly what constitute reasonable costs based on generally accepted practices.

Debtor and creditor actions during restructuring. Debtors should resume, to the extent feasible, partial debt service as a sign of good faith and resume full payment of principal and interest as conditions allow. Debtors and creditors recognize in that context that typically during a restructuring, trade lines are fully serviced and maintained. Debtors should avoid additional exchange controls on outflows, except for temporary periods in exceptional circumstances. Regardless of the specific restructuring mechanics and procedures used (i.e., amendment of existing instruments or exchange for new ones; pre-default consultations or post-default committee negotiations), restructuring terms should be subject to a constructive dialogue focused on achieving a

critical mass of market support before final terms are announced. Debtors should retain legal and/or financial advisors.

4. Fair Treatment

Avoiding unfair discrimination among affected creditors. The borrowing country should avoid unfair discrimination among affected creditors. This includes seeking rescheduling from all official bilateral creditors. In line with general practice, such credits as short-term trade-related facilities and inter-bank advances should be excluded from the restructuring agreement and treated separately if needed.

Fairness of voting. Bonds, loans, and other financial instruments owned or controlled by the sovereign should not influence the outcome of a vote among creditors on a restructuring.

Annex II. Report of the Joint Committee on Strengthening the Framework for Sovereign Debt Crisis Prevention and Resolution

I. BACKGROUND

The ongoing sovereign debt crises in the Euro Area over the past two and a half years, including the Greek voluntary debt restructuring, are the first sovereign debt crises in mature market countries in recent decades. They reflected essentially a range of factors, including underlying weaknesses in fiscal positions, inefficiencies in public sectors, unsustainable public debt, unsustainable bank credit expansion, deteriorating competitive positions, structural rigidities, weak growth potential, and, in many cases, housing price bubbles—many of which have been amplified by some design flaws of the European monetary union. Some of these underlying vulnerabilities were magnified in the aftermath of the major financial crisis of 2008–09 that has led to persistently weak economic growth in mature market countries and bouts of market turmoil. While exhibiting unique features, these vulnerabilities are reminiscent in several respects of the experience with debt crises in Latin America and other emerging markets over the previous three decades. The *Principles for Stable Capital Flows and Fair Debt Restructuring* were in fact conceived and launched in the aftermath of the sovereign debt crises in Latin America and Eastern Europe and influenced by the experience of the Asian crisis, and it was in late 2010 that the Group of Trustees of the *Principles* endorsed a recommendation by a special Principles Consultative Group (PCG) Working Group on the Applicability of the *Principles* to essentially extend the applicability of the *Principles* to all sovereign debtors and to the debt restructurings by banks or other non-sovereign entities in which the sovereign plays a major role in setting the legal framework.

The guidelines stemming from the *Principles* have usefully contributed to the development of the modalities for engaging with the private sector (summarized in the March 2011 "Term Sheet") of the European Stability Mechanism (ESM), the permanent institution set up for the channeling of Euro Area financial assistance to member countries facing sovereign debt difficulties, which has replaced the European Financial Stability Facility (EFSF) established in June 2010. Besides the EFSF/ESM, the Euro Area sovereign debt crisis management framework encompasses a range of other initiatives, including reinforced regional surveillance (new macro-imbalances procedures at the European Union level) and fiscal discipline (especially under the strengthened budgetary surveillance framework at the EU level—"six-pack" and "two-pack"—and the fiscal compact at the member country level), which complement stepped-up reform measures taken by individual member countries.

The *Principles* have also served as a guiding framework for the good-faith negotiations between the private creditor representatives and Greece, in consultation with the official sector, on a voluntary exchange of the outstanding Greek public debt held by domestic and foreign private creditors, from the outset of these discussions in June 2011 until the eventual execution of the debt exchange in March/April 2012.

In the discussions on the private sector involvement in Greece (PSI), private creditors were initially represented through an IIF-led Task Force on Greece during June–October 2011, and subsequently through the Steering Committee of the Private Creditor–Investor Committee (PCIC) for Greece during November 2011–April 2012. The debt exchange was concluded during March–April 2012. The dialogue with the Greek authorities and the official sector in general, the negotiations with Greece over the terms and conditions of the debt exchange, and the concessions made both by private creditors and the official sector were instrumental in facilitating the successful conclusion of the voluntary PSI deal with a very high private creditor participation rate—amounting to 83.5% and to almost 97% with the activation of Collective Action Clauses (CACs).

The successful conclusion of the voluntary debt exchange for Greece has provided Greece with a major upfront nominal debt reduction and cash-flow benefits. It has also given Greece some breathing space to enable it, together with the large official

financial support, to be in a position to effectively implement the needed economic reforms in order to correct present imbalances and attain over time renewed growth and debt sustainability. The PSI was instrumental in facilitating the second program for Greece.

The experience with the protracted negotiations—which were partially the result of the complexities of Greece being a member of a currency union that explicitly prohibited exceptional assistance for its members, the complex decision-making procedures within the Euro Area, as well as the initial absence of any assistance mechanism—and the scope and spillover effects of the Greek debt exchange have given rise to a number of broader issues that go well beyond the impact of the debt exchange on Greece itself. They have major implications for sovereign debt crisis management policies and the existing framework for preventing and resolving sovereign debt crises, as embodied in the guidelines underlying the *Principles.* It is vital that this experience be assessed to draw appropriate lessons for policymakers at the country and regional levels, as well as relevant international financial institutions and the private investor community.

Notable features of the Greek sovereign debt crisis resolution include the following:

- It was the first sovereign debt crisis and resolution in modern history in a mature market economy and in the Euro Area;
- It was the largest debt exchange in history, covering €206 billion of government debt and the largest sovereign debt restructuring (including on a pre-default basis), entailing significant debt relief aimed at achieving a revival of growth and debt sustainability;
- It involved government bonds and not just loans, and a very broad range of domestic and foreign private investors, not just banks;
- It had significant contagion risks for other countries in the Euro Area and the regional banking system, and the world economy as a whole;
- It required contributions by both official and private creditors;
- It entailed formal negotiations between private creditors through their representative committee with the Greek authorities, and extensive consultations with the official sector. This involved complex coordination issues both among private creditors and among Euro Area member countries;
- It has clearly demonstrated that a voluntary, market-based approach is more effective and appropriate than a unilateral, top-down approach to debt restructuring (as mooted during the debt restructuring negotiations);
- It has influenced the evolution of the Euro Area sovereign debt crisis management framework, which was not in place when the Greek debt crisis erupted, and has given rise to policy issues that continue to dominate the policy debate; and
- It had a major impact on the Greek banking system, necessitating Euro Area official support for its recapitalization.

Moreover, the emergence of the Greek sovereign debt difficulties and the actual modalities pursued for the resolution of the debt crisis have revealed a number of weaknesses. The issues that have been identified related broadly to several weaknesses in crisis prevention, notably inadequate policies and data and policy transparency, inadequate risk management, and underestimation of the credit and sovereign risks by the private sector of investments in sovereign bonds of mature market countries. Other issues emphasized by private investors included the too frequent changes in the macroeconomic framework for the debt exchange, which, in their view, had an adverse impact on market sentiment and expectations; the apparent focus on fixed quantitative objectives of the debt sustainability methodology, with high prominence given to the nominal public debt/GDP ratio relative to the potential positive effects of a lengthening of the maturity profile and cash-flow debt relief; the protracted negotiating process between Greece and its private creditors on the one hand and between Greece and its official creditors on the other; the subordination of private creditor claims;

and the retroactive modification of the governing legal framework to introduce a collective action mechanism (similar to CACs) in Greek government bonds (GGBs) issued under domestic law.

Overall, the combined developments in these areas have posed at times some challenges to the adherence to the guidelines for the behavior of private creditors, sovereign debtors, and other official bodies underlying the *Principles*—namely, open dialogue, transparency, good faith negotiations, and the fair and comparable treatment of all creditors. At some instances, the multiplicity of official statements at the member country level included suggestions to resort to a unilateral, top-down approach to achieve the desired debt relief, but eventually a voluntary, consultative approach was followed. The extensive experience with the handling of the Euro Area sovereign debt crises has highlighted the potential costs to creditors, debtors, and the financial system as a whole from deviations from the *Principles*. In a broad sense, non-adherence to the guidelines advocated by the *Principles* could result in a debt resolution process that is inefficient and sub-optimal, with major risks to the normalization of market access and the promotion of financial stability.

II. FORMATION AND TERMS OF REFERENCE OF THE JOINT PUBLIC–PRIVATE SECTOR COMMITTEE

Against the above background, the four Co-Chairs of the Group of Trustees of the *Principles* agreed in mid-March 2012 with the two Co-Chairs of the IIF Special Committee on Financial Crisis Prevention and Resolution on the formation of a Joint Public–Private Sector Committee to assess the recent experience with sovereign debt crisis prevention, management, and resolution in the Euro Area and elsewhere,[1] draw appropriate lessons, and make recommendations on the strengthening of the existing framework for sovereign debt crisis prevention and resolution as embodied in the guidelines of the *Principles*.

The key objectives of the Joint Committee on Strengthening the Framework for Sovereign Debt Crisis Prevention and Resolution were:

- To assess the recent experience with sovereign debt crisis prevention at both the country and regional levels, draw lessons, and identify measures to strengthen the framework for crisis prevention—data transparency, open dialogue between the sovereign debtor (and other related authorities) and private creditors on current and future policy plans, and investor relations.
- To assess the recent experience with sovereign debt crisis resolution in Greece, taking into account the role played by Euro Area authorities (both country and regional) and international and European institutions and identify measures to strengthen the framework for debt crisis resolution: the role played by the Euro Area debt crisis management framework, the effectiveness of the decision making process, the role played by the IMF, the European Commission, and the ECB in defining the macroeconomic framework and debt sustainability parameters, the effectiveness of creditor committees and the role they should play in contributing to the policy dialogue, and the importance of facilitating the regaining of market access for sustained economic growth.
- To analyze the current and prospective implications for private creditors from actual and potential changes in the seniority of their existing and future claims resulting from official actions and for the debtors themselves (resulting from the Greek debt restructuring and the ESM Treaty provisions), particularly as it regards the potential volume and terms of future private creditor financing.
- To evaluate the need and make recommendations for the amplification of the existing guidance for applying in practice the *Principles*, including through the possible issuance of an Addendum to the *Principles*,

[1] In parallel with the debt exchange for Greece, in March 2012, St. Kitts and Nevis, a small island in the Caribbean, concluded a comprehensive voluntary restructuring—consistent with the *Principles*—of its public debt held by domestic and foreign private creditors, as well as official bilateral creditors, with a participation rate of 97% and 100% after the activation of CACs.

for the consideration of the Group of Trustees at their meeting on October 14, 2012, on the occasion of the IMF/Work Bank and IIF Annual Meetings in Tokyo.

The Joint Committee was co-chaired by **Jean Lemierre**, Senior Advisor to the Chairman, BNP Paribas, and Co-Chair of the IIF Special Committee on Financial Crisis Prevention and Resolution; **Thomas Wieser**, President, Eurogroup Working Group; **David Mulford,** Vice-Chairman International, Credit Suisse Group; and **Gerardo Rodríguez Regordosa**, Undersecretary of Finance and Public Credit, Mexico. The Joint Committee also comprised 35 prominent representatives from the public and private sectors with extensive experience in sovereign debt restructuring in the Euro Area and elsewhere (the membership of the Joint Committee is shown in Attachment I). IIF staff served as secretariat to the Joint Committee. To address its agenda, the Joint Committee held several conference calls and three physical meetings in Washington, DC in April and in Paris in June and September 2012.

III. JOINT COMMITTEE FINDINGS AND RECOMMENDATIONS

1. Overall Assessment

The guidelines underlying the *Principles for Stable Capital Flows and Fair Debt Restructuring* remain an appropriate, relevant, and effective framework for sovereign debt crisis prevention and resolution. Their fundamental emphasis on sound policies and data and policy transparency by debtors is of critical importance in crisis prevention. Moreover, the underlying guidelines for voluntary, cooperative, market-based procedures for debtor-creditor dialogue and good-faith debt restructuring negotiations remain an essential cornerstone of sovereign debt crisis management and resolution and should continue to guide the interactions between sovereign issuers and their creditors. Such a cooperative approach would facilitate an early restoration of market access, which is of critical importance in achieving debt sustainability over time, and allow the official sector to gradually reduce its exceptional financial assistance to the countries under official sector–supported reform programs.

The support by the official sector of a voluntary debt exchange agreement for Greece reached through negotiations with private creditors has demonstrated and underscored the validity and usefulness of resolving even the most difficult sovereign debt problems in a manner consistent with the cooperative, market-based guidelines established by the *Principles* with major benefits not only for the parties directly involved, but also for the Euro Area as a whole and global financial stability in general.

However, while the voluntary overall framework of the Greek PSI negotiations was broadly consistent with the *Principles*, some aspects of the process through which the actual debt exchange deal was reached and some specific features of the coverage and terms of the deal raise concerns going forward. As regards the process, there have been at times uncertainties about the official sector commitment to a voluntary approach and, especially in the last critical stage of the negotiations, limited transparency of information on the details of Greece's future policy plans, specific policy targets, and likely macroeconomic outcomes and the associated determination of the volume and terms of the contribution of private creditors. The multiplicity of statements often at member state level in the context of domestic political debates has often created confusion for the private sector. The complexity of the Euro Area decision-making process and the fact that Euro Area authorities needed some time to develop the required response to the crisis complicated the situation significantly.

As regards specific features, the exclusion of bonds held by EU official entities (such as the ECB, national central banks, and the European Investment Bank [EIB]) from the debt exchange has raised concerns about equal treatment of creditors holding similar paper and the subordination of private investors, with possible lasting adverse effects on the demand for Euro Area sovereign debt in general. It is worth noting in this context that the EIB continued to extend credits to Greece during the crisis and the ECB undertook sovereign bond

purchases under its Securities Market Program (SMP) to stabilize financial markets. In addition, the retroactive modification of the legal framework to introduce a collective action mechanism in the Greek government bonds issued under Greek law has raised concerns about the sanctity of contracts and questions about the future demand for sovereign securities issued under domestic law, notwithstanding its contribution to the high participation in the voluntary debt exchange (see Section 4(d) for more details).

These considerations, along with the special or unique institutional features of the Euro Area and the recent experience in sovereign debt crisis management, call for some elaboration or updating of the guidance provided by the *Principles* to make it more practically relevant to the circumstances faced by mature economies, in particular, those that are members of currency unions. The regional features include the significant contagion and spillover risks between Greece and the other troubled sovereign debtors in the Euro Area; the strong negative feedback loop observed between sovereign debt markets and the Euro Area banking system and its adverse regional macroeconomic implications; the large reliance of Euro Area countries on market financing; the broad range of private investors involved, subject to different regulatory requirements; and the added complexity of handling sovereign debt crisis management and resolution in a currency area.

The sections below highlight the Joint Committee's assessment of the recent experience and recommendations in specific areas related to the guidelines underlying the *Principles*—data and policy transparency, debtor-creditor dialogue and cooperation, good-faith negotiations, and fair treatment of all creditors. The Joint Committee's overall assessment and recommendations are summarized in the proposed *Addendum to the Principles* (Attachment II). The proposed *Addendum* is intended to complement the existing text of the guidelines underlying the *Principles* by providing some further amplification or elaboration of the current guidance on how to help ensure an effective implementation of the *Principles*.[2]

2. Data and Policy Transparency for Crisis Prevention

Assessment

A broad range of factors have contributed to poor crisis prevention practices in the period prior to the sovereign debt crises in the Euro Area. First and foremost, there were major weaknesses in data and policy transparency by Greece, and some countries pursued policies that contributed to the emergence of large and widening domestic and external imbalances and/or asset price bubbles and banking sector vulnerabilities. These unsustainable economic trends were not sufficiently well detected and highlighted by the existing economic surveillance procedures of regional and international institutions, or market analysts. Moreover, regulatory practices that *inter alia* treated sovereign debt as a riskless asset contributed to the weak risk management practices by financial institutions and market participants and resulted in misplaced perceptions about the default risks of countries that are members of currency unions. Investors, and in part policymakers, underestimated the credit risks involved in lending to individual sovereign issuers, notably in the Euro Area, contributing to a sharp narrowing of spreads on sovereign bonds. All these factors combined contributed to the emergence of unsustainable economic imbalances and posed contagion and systemic risks.

Major efforts and initiatives are currently ongoing to address these weaknesses. These include a strengthened framework for economic surveillance (the new macro-imbalances procedure) and fiscal discipline by Euro Area countries (notably through the "six-pack," the Fiscal Compact procedures, and the "two-pack" that will enter into force soon) and empowerment of Eurostat (the Euro Area statistical agency) to assess the compliance with established norms of data provision by member states. The regulatory framework and bank supervision

[2] The *Addendum* was endorsed by the Group of Trustees at its 2012 Annual Meeting in Tokyo on October 14, 2012.

arrangements have also been strengthened in the Euro Area and elsewhere, including the monitoring of contingent liabilities. The early warning procedures and multilateral surveillance and spillover analysis by the IMF, the G20, and private sector groups have also been intensified, including by the IIF's Market Monitoring Group. Enhanced risk management practices by financial institutions are also being implemented. But there is still a need for further progress and for continued effective implementation of agreed measures and vigilance by all parties concerned.

Recommendations

Sovereign debtors should pursue sound fiscal and growth-enhancing structural policies, consistent with macroeconomic and financial stability and public debt sustainability.

Sovereign debt issuers should ensure that they release on a timely basis comprehensive relevant data and other information related *inter alia* to their fiscal developments and debt positions (including, when appropriate, contingent liabilities) and on current and future policy plans. These data should be consistent with established accepted standards and norms (i.e. budget data should be released also on an accrual basis, not only cash basis) and verified by authorized domestic and regional agencies, especially with regard to their accuracy, comprehensiveness, and comparability over time.

Effective sovereign debt crisis prevention is a shared responsibility that requires—besides data and policy transparency and open dialogue with creditors by the sovereign debtors—sustained surveillance efforts by regional and international institutions and private sector groups; actions by regulatory agencies, accounting, and other international standard setters; as well as vigilance and enhanced risk management by private creditors and market participants in general.

The effectiveness and timeliness of surveillance by regional and international institutions of the consistency between policy plans and actual execution, and of national policies with regional commitments and undertakings for countries that are members of currency unions are critical for promoting sustainable policies and market confidence. Clarity and transparency of information on actual economic trends and prospects are essential for facilitating effective risk management by market participants and efficient functioning of sovereign debt markets.

Private creditors and market participants are responsible for formulating accurate and appropriate assessments of underlying trends in market risks, and the credit and sovereign risks of individual issuers, thus ensuring a realistic pricing of sovereign debt instruments. In this context, private creditors and market participants should undertake their own due diligence, drawing *inter alia* on all available information from the sovereign issuers themselves and the assessments by regional and international financial institutions. The assessment of current economic and financial developments and the identification of underlying or emerging risks by private sector groups such as the IIF's Market Monitoring Group can also play a useful and constructive role in this process.

Regulatory agencies should take care in setting capital and other requirements for covered financial institutions to avoid distortions in market signals and biasing risk management practices.

Responsible and realistic assessments and timely analysis by ratings agencies can also provide useful complementary information to market participants, investors, and issuers and enhance crisis prevention.

3. Close Debtor-Creditor Dialogue and Cooperation for Crisis Prevention

Assessment

Unlike emerging market issuers, the dialogue and cooperation between mature country issuers and their private creditors has traditionally been less extensive than in emerging markets, and minimal in some cases. This has reflected historical reasons and perceptions about debt sustainability risks, as well as market and institutional developments and practices. In the Euro Area, sovereign bonds have since 1999 primarily been denominated in

euros and issued mainly under domestic law to all investors irrespective of residence, with limited provision for prospectuses on the underlying terms and conditions. In the case of Greece, only a small part of government bonds had been issued under international law (mainly English law) in euros or other currencies with embedded CACs. The European Stability Mechanism (ESM) envisages the inclusion of uniform and standardized CACs and aggregation clauses in all new issues of sovereign bonds by Euro Area countries from January 2013 onward. This initiative has been welcome and supported by private investors.

Recommendations

Mature market country issuers should consider implementing the best practices for investor relations that have evolved. The adherence of emerging market borrowers to these best practices are reviewed annually by the IIF and summarized in the annual Implementation Report of the *Principles* issued by the Principles Consultative Group.

Enhancement of investor relations under Investor Relations Programs facilitates timely data and policy transparency and a regular dialogue between sovereign issuers and their creditors and establishes an effective channel of communication and feedback. The experience over the past few years has demonstrated the value and contribution of IRPs in enhancing market confidence and maintaining market access even during periods of market tensions and turbulence.

Sovereign debt issuers in both mature and emerging market countries should incorporate in new bond issues, denominated in a foreign or a common regional currency, CACs with appropriate aggregation clauses, with comprehensive coverage of their terms and conditions in the bond documentation and easy access to this information by all investors. Issuers of domestic bonds denominated in local currency may also consider such arrangements. Appropriately designed aggregation clauses would allow bond holders across all outstanding issues of government securities to collectively decide on whether to accept potential offers from issuers to modify existing bond terms and conditions. The use of CACs inclusive of aggregation clauses can facilitate voluntary debt restructuring by reducing the chances of a small minority of bond holders acquiring blocking positions in a bond series and imposing demands for preferential treatment.

4. Good-Faith Actions in Cases of Debt Restructuring

(a) Voluntary Good-Faith Process

Assessment

The good-faith negotiations between the Steering Committee of the PCIC for Greece and the Greek authorities, in consultation with the official sector, were critical in facilitating a voluntary consensus on the terms of the debt exchange for Greece. The support provided by the authorities of key Euro Area countries and the leadership of Euro Area institutions to the good-faith negotiations was of critical importance in fending off efforts in some quarters to resort to a unilateral approach and/or consult only with a selected narrow range of private creditors separately rather than through the Steering Committee. The voluntary approach facilitated a consensus on a historic and unprecedented debt exchange deal for Greece that covered the largest volume of securities (both bonds and loans) and involved a large and diverse range of domestic and international creditors. The debt exchange was voluntary, in the sense that its terms and conditions were negotiated and agreed *ex ante* between the Greek authorities and the representatives of the private creditors, in consultation with the official sector, and was supported by a high voluntary creditor participation rate even before the activation of CACs, notwithstanding the major financial losses in net present value terms sustained by creditors.

With the prevailing accounting framework and regulatory requirements for regulated financial institutions to report their exposure to Greece (and other Euro Area sovereign debt), some or most of these financial losses were in fact recognized in their balance sheets as the debt restructuring was being negotiated. In fact, until they were clarified, earlier

differences between the accounting practices and regulatory arrangements across jurisdictions and types of financial institutions had contributed to the complexity and time consuming nature of reaching an agreement on the PSI deal for Greece.

The reliance on a voluntary approach ameliorated the negative pressures in sovereign debt markets and the secondary market bond valuations for Greece and other troubled Euro Area countries and avoided a more adverse impact on market confidence. Nonetheless, concerns among both the official sector and private market participants and investors about the spillover risks from Greece to other Euro Area countries facing debt difficulties remained elevated. These concerns, and at times lack of clarity in the communication of the official sector, have weakened market confidence and the valuation of sovereign debt in Euro Area markets, and influenced the debt restructuring negotiations.

The debt restructuring negotiations were complicated and protracted as a result of institutional factors, collective action problems on both the official sector and private investor sides, and Greece's evolving macroeconomic circumstances and program performance. On the official sector side, coordination issues arose as Greece's financing need was fairly large, requiring bilateral contributions by its Euro Area partners. On the private creditor side, the large number of creditors involved, subject to different regulatory jurisdictions and accounting practices, complicated the decision-making process. Frequent slippages in policy implementation by Greece, against a setting of a deepening contraction in economic activity and employment and a challenging social and political environment, necessitated periodic revaluations of the program policy targets and medium-term funding needs.

The negotiating process was made more difficult and time consuming by the need for Greece to reach understandings with its official Euro Area partners and the IMF on the needed reform policies and the available volume and terms of financial assistance before advancing in its negotiations with its private creditors. Formal negotiations took place between Greece and private creditors, but extensive consultations were also held at the Euro Area official sector level, including the Eurogroup Working Group, the Eurogroup (Finance Ministers' level) and its leadership, senior European Commission officials, the ECB, and key Euro Area Leaders. The decision-making process within the Eurogroup was complicated by the need for unanimity among its members that represented 17 different democratic countries. It also reflected the fact that the Euro Area authorities needed some time to develop an intergovernmental crisis response and assistance mechanism. This also required a political reassessment and adjustment of some key principles underlying the Euro Area. Agreement on the terms and conditions of the private sector involvement was finally reached in an iterative process, once political decisions were taken on the volume and terms of the Euro Area official financial resources, and the macroeconomic framework and adjustment path were finalized by the IMF and other members of the Troika (the European Commission and the ECB).

Recommendations

Good-faith negotiations remain the most effective framework for reaching voluntary debt restructuring agreements among sovereign debtors and their diversified private creditor community, particularly in the complex cases of mature market issuers that are members of currency unions. Such a framework has proved to be efficient in facilitating appropriate agreements on crisis resolution, while containing the adverse impact on market confidence and other disruptions and concerns caused by spillover and contagion risks.

Sovereign issuers and their creditors should strive to reach and effectively implement voluntary agreements on a timely basis to help minimize adverse market reactions and contagion effects. In this context, debtors and creditors should be cognizant of the potential adverse effects of the interaction between sovereign debt and capital markets, to the detriment of the interests of all parties. With the increased sophistication, integration, and complexity of capital markets, for both emerging market and mature economy countries, the interaction among developments in sovereign debt markets, changes in the regulatory

framework, and banking system practices gives rise to major dynamics with significant implications for credit expansion, risk practices, market access by sovereign debtors, and macroeconomic developments.

The dynamics and incentives for debtors and issuers to engage in good-faith negotiations are strongly influenced by the existing accounting and regulatory standards and their interaction across types of financial institutions and jurisdictions. The standard-setting bodies responsible for accounting and supervision rules, as well as the interpretation bodies, should be cognizant of the need to minimize inconsistencies between accounting and supervision practices and conflicts across jurisdictions and types of covered financial institutions.

The early restoration of market access is of critical importance in achieving debt sustainability over time. Early re-accessing of capital markets at reasonable costs is also essential for allowing sovereign debtors to reduce and eliminate their reliance on exceptional IMF financing and financial support from their official bilateral partners, such as is the case under currency unions or regional arrangements.

(b) Debtor and Creditor Actions During Debt Restructuring

Assessment

In the context of sovereign debt restructuring, the macroeconomic framework, the debtor's adjustment policies, the debt sustainability analysis, and the timing of market access are crucial parameters that inform the negotiations between the debtor and its creditors.

In assessing the experience with the Greek PSI negotiations, private investors have held the view that there was inadequate sharing of information, especially during the last critical two–three months of the negotiations, about the way the Greek medium-term growth projections and reform objectives, including the debt sustainability analysis, were prepared and frequently adjusted by the official sector in response to the evolving economic circumstances and changing policy settings during the quarterly program review process. This was perceived by private creditors as limiting an open, informed and productive dialogue between private creditors and the Greek authorities, in consultation with the official sector. In light largely of Greece's evolving economic circumstances, program performance and implementation capacity between the regular quarterly reviews, the macroeconomic framework and policy undertakings by Greece were scaled down significantly in several stages between July 2011 and February 2012. These changes eventually necessitated *inter alia* a more substantial contribution by private creditors than envisaged in the broad understandings reached with the official sector in July and October 2011. The debt sustainability analysis and the derivation of the needed policy adjustments and financial contributions by official and private creditors carried out by the Troika tended to focus, in the view of private creditors, on rather fixed quantitative objectives about the nominal debt/GDP ratio, with insufficient weight attached to the potential positive effect from a lengthening of maturities and cash-flow relief, without an adequate exchange of views on these issues with private creditors. At times, private creditors perceived that their contribution was treated as a residual to fill identified financing gaps, undermining the prospects for restoring market access over time.

As a consequence, questions have been raised about the best ways to encourage greater data and policy transparency, a timely exchange of views, and a more open dialogue with private creditors. The IMF has played a critical role in the Greek PSI discussions, both as an advisor on economic policies and, to a lesser extent, as a provider of financial support. In view of the Euro Area's role as a major provider of financial assistance to Greece, the Euro Area institutions have also played an important role in determining Greece's macroeconomic framework within the Troika.

However, for private creditors to give up their legal rights and accept large financial losses, they need first and foremost an understanding of the changing economic circumstances and

of the adequacy of the sovereign debtor's own reform efforts to address the adjustment needs of its economy. To this end, private creditors need to be adequately informed of the changed circumstances and the details of the reform program in a transparent and timely manner. Moreover, to achieve the broadest support possible for the overall macroeconomic framework, the broad fiscal targets, and the underlying output projections and debt sustainability analysis, it is necessary for private creditors to have an early opportunity to discuss these issues, through their creditor committee, with the sovereign debtor, in close consultation with the official sector. Such discussion and feedback would promote both market confidence in the reform program and, if necessary, facilitate a fair burden sharing between the sovereign debtor (undertaking the adjustment), the official sector (providing financial assistance), and private creditors (providing their contributions). A voluntary agreement on a fair burden sharing is needed to promote the restoration of market access, the resumption of satisfactory economic growth, and the attainment of debt sustainability.

Private creditors stress that it is important that the IMF play an objective role (and as far as the Euro Area is concerned, within the Troika) in finalizing together with the debtor the macroeconomic framework and the appropriate mixture of adjustment and financing, taking into account the availability of official financing, with a view to helping to support and facilitate, where necessary, an efficient, voluntary debt restructuring. It is clear that, under its own rules and practices, the IMF remains independent in preparing and presenting to its Executive Board its formal Debt Sustainability Analysis. It is important that the debt sustainability parameters be set with the benefit of a discussion with private creditors, since their commitments are essential ingredients to the debt sustainability outlook. These parameters include primarily the terms and conditions of a voluntary debt restructuring that need be agreed to in good-faith negotiations between the sovereign debtor and its creditors.

Recommendations

To facilitate good-faith negotiations, sovereign issuers, and regional institutions in case of regional arrangements, should engage in enhanced data and policy transparency and dialogue with private creditors at an early stage, should a debt resolution become necessary. The early release of information on the scale of the adjustment needs and the range and scale of the envisaged corrective policies by the sovereign issuers themselves or in the context of adjustment programs supported by the IMF and/or regional institutions would help minimize adverse market reaction and contagion risks and facilitate continued or early resumption of market access. The sanctity of contracts should be respected. Modifications to these contracts should be avoided wherever possible as a matter of principle.

In the debt restructuring process, an early discussion is necessary between the representative private creditor committee and the sovereign debtor, in close consultation with the official sector, on the overall multi-year macroeconomic framework and objectives, including the broad fiscal policy targets and the underlying outlook for output growth and public debt under alternative assumptions on the debt restructuring. Such a discussion is important in facilitating an effective voluntary debt restructuring agreement on a fair burden sharing, thus promoting high private sector participation, restored market access, renewed output growth, and debt sustainability.

It should be recognized that the attainment of debt sustainability over time is a dynamic, complex process that depends critically on the quality and market credibility of actual and prospective adjustment policies undertaken by the debtor, the direction of macroeconomic policies, the terms and volume of financial support or debt relief provided by official and private creditors, and the prospects for the continuation or resumption of market access at reasonable terms. As such, the debt sustainability analysis entails judgments and assessments that are often not easily amenable to quantitative rules and that require revisions as macroeconomic parameters evolve. The contributions toward achieving debt sustainability

by private creditors as well as other creditors should be considered simultaneously, with no one creditor group considered as a residual source of funding on an *ex ante* basis.

In this context, the IMF has a very important role to play by providing objective analysis and information on macroeconomic policies and prospects and on the sovereign debtor's medium-term funding needs, consistent with debt sustainability considerations.

(c) Creditor Committee Policies and Practices

Assessment

The representation of the private creditor community in the Greek debt restructuring negotiations was somewhat novel and took two distinct forms, reflecting the evolving thinking and views of the official sector on the desirability and depth of any debt restructuring for Greece. Initially, in June 2011, the IIF was invited by the Eurogroup Working Group to engage in a dialogue on the options for securing private creditor involvement, given the IIF's close involvement in the development and the monitoring of observance of the guidelines underlying the *Principles*. To aid this process, the IIF formed for this purpose a Task Force for Greece comprising IIF members and other holders of Greek bonds, after getting authorization from its Board of Directors (representing large financial institutions holding a large share of outstanding GGBs).[2] However, after October 2011, private creditors organized themselves in a broadly based creditor committee (PCIC), represented in the negotiations by a smaller Steering Committee, which reflected the diverse membership of the PCIC and facilitated the effective completion of the negotiations. The Steering Committee and the broader PCIC represented all principal groups of Greek government debt holders, including all major Greek banks, and a large share of the outstanding GGBs and loans covered by the debt exchange. As is common practice in sovereign and corporate debt restructurings, besides their broad representation, the Steering Committee and the PCIC derived their legitimacy and credibility through their actions and positions, which were aimed at advancing the interest of all private creditors, while also promoting financial stability. This legitimacy was confirmed *ex post* by the high degree of creditor participation in the debt exchange, including the acceptance of the retroactive CACs. Greece has agreed to reimburse the legal fees incurred by the Steering Committee.

Generally, private sector creditors should strive to form a single Creditor Committee and a coherent Steering Committee as early as possible, and to provide the Steering Committee with adequate financial and analytical resources to conduct negotiations with the sovereign borrower, in consultations with official bilateral creditors—negotiations that could be protracted.

Recommendations

Private creditors should organize themselves in a broadly based representative creditor committee as early as possible in the debt restructuring process, certainly before debt default, which should be avoided if possible. Sovereign issuers should interact and engage in negotiations with their private creditors through the representative creditor committee and should consult with the creditor committee as part of the process of fulfilling the requirement under IMF policy of lending to debtors in arrears to make good-faith efforts to reach understandings with their creditors. Such a framework would be more conducive to reaching a voluntary agreement on debt restructuring and facilitate market access.

Private creditors that are members of the creditor committee negotiating with the sovereign debtor should abide by established ethical standards and *inter alia* respect the confidentiality of any material non-public information that may become available during this process and notably commit not to use confidential information from the negotiations for trading purposes.

This process will be aided in cases of countries that require financial assistance from multiple

[2] Prior to that, in late 2010 and early 2011, the IIF had participated in informal consultations with the European Commission as part of the process for finalizing the modalities for the ESM.

official bilateral creditors, as is usually the case for countries that are members of currency unions, by the formulation of timely and effective procedures for reaching understandings on the scale, terms, and conditionality of any envisaged financial assistance from these creditors so as to facilitate the negotiations between the sovereign debtor and the private creditor committee.

In line with the evolving practice, the sovereign debtor would be expected to cover reasonable costs incurred by a single private creditor committee for the legal and financial advisor fees, consistent with agreed parameters.

(d) Tools for Debt Restructurings

Assessment

As regards the tools used in the Greek debt exchange, two special features are worth highlighting. First, the adoption, just days before the launching of the debt exchange offer, of legislation modifying retroactively the governing legal framework to introduce a collective action mechanism in existing GGBs issued under Greek law has raised concerns about the sanctity of financial contracts. Notwithstanding the contribution the activation of this collective action mechanism has made to the overall success of the debt exchange—after a voluntary PSI deal had been reached—as a matter of principle, there should not be any changes in the governing law with retroactive effect. This retroactive action was put to the approval of private creditors as an exit clause under the debt exchange offer and was in fact endorsed by a large majority (85.8%) of private holders of Greek law bonds, exceeding the needed 50% threshold, thus allowing the activation of the collective action mechanism. It also exceeded the normal 75% threshold for the activation of CACs for bonds issued under English law. Yet, as a matter of principle, the retroactive change in the legal framework governing sovereign debt instruments is worrisome and sets a bad precedent, as it could encourage investors to prefer international law bonds instead of domestic law bonds to minimize "sovereign risk," and might undermine the functioning of their sovereign debt markets. However, the retroactive introductions of CACs with terms and thresholds consistent with market practice to facilitate debt restructuring when a voluntary agreement with private creditors has already been reached can be considered.

Second, the Greek debt exchange involved a number of credit enhancements for the new GGBs issued under the exchange, intended to raise their market value and the attractiveness of the debt exchange offer. These useful enhancements comprised the use of a co-financing scheme for the servicing by Greece of the coupon and principal payments for both the new GGBs and €30 billion of EFSF financing. They also included the use of English law as the governing legal framework, the incorporation of CACs in the new GGBs, and the issuance of GDP-linked securities that provided the potential for additional coupon payments subject to certain restrictions in case of a higher-than-projected output growth performance by Greece. These credit enhancements were seen by private investors as critical in facilitating a voluntary debt exchange agreement. The issuance of the new bonds under English law was particularly welcome by private investors, who considered such practice as providing more reassurance and protection for their claims, thus helping to raise the participation rate in the debt exchange. Against this background, private investors may favor in the future sovereign bond issuance under international law, especially in cases where sovereign risk is perceived to be elevated. However, the development of domestic capital markets remains a worthwhile and desirable objective. Issuance of sovereign bonds under a legal framework that is perceived to provide protection for creditor rights may facilitate accessing capital markets at more reasonable costs than otherwise would be the case.

Recommendations

Sovereign issuers and their creditors should introduce CACs and possibly other options to enhance the credit quality of the new debt instruments used under debt restructuring exercises so as to enhance the prospects for high voluntary creditor participation. Retroactive legal changes to unilaterally modify the terms and conditions of financial contracts may undermine

the integrity of financial markets and the sanctity of contracts and should be avoided. However, in exceptional cases and after a voluntary debt exchange agreement has been reached, such modifications of the governing legal framework to introduce a collective action mechanism on a timely basis with terms and thresholds consistent with market practices may be necessary in facilitating a voluntary debt exchange and achieving a fair outcome for all bond holders.

5. Fair and Comparable Treatment of All Creditors

Assessment

In line with the *Principles*, the Greek debt exchange excluded short-term government securities (Treasury Bills)—no trade-related government financing instruments were outstanding.

However, concerns about the fair treatment of all creditors arose from two developments in the sovereign debt crisis management experience in the Euro Area.

First, under the Greek debt restructuring offer, holdings of GGBs by the ECB, national Euro Area central banks, and the European Investment Bank (EIB)—amounting to more than 20% of total GGBs outstanding—were unilaterally carved out of the total Greek government securities covered by the debt exchange without consultation with private creditors, even though these holdings by the Euro Area official bodies were identical and non-separable from the holdings of the same bonds held by private investors. The resulting subordination of private claims constituted discrimination against private creditors. Notwithstanding the claimed broad rationale for such action (namely that the Euro Area official sector collectively provided substantial new funding to Greece), this subordination and concerns about similar actions in the future by Euro Area issuers have already had an adverse effect on the perceived credit risk of sovereign debt in the Euro Area, and the relative ranking of private investor claims. As a consequence, this subordination has weakened the incentives of private investors to maintain or increase their exposure to sovereign Euro Area debt.

While the GGB purchases from the secondary market by the ECB (at a discount) undertaken under the Securities Market Program were motivated by monetary policy considerations, the GGB holdings by national central banks and the EIB reflected traditional financial investments similar to those by private creditors. In this light, the exclusion of the ECB holdings from the debt exchange could be rationalized (even though a transfer of the associated net gain to Greece could be considered), but the exclusion of the other official body holdings deviated from the normal principle of non-discrimination. It is worth noting in this context, however, that the EIB continued to extend credits to Greece during the crisis.

Second, the preamble of the ESM Treaty, which outlines the Euro Area permanent debt crisis management framework and came into effect in early October 2012, stipulates that official financial support under the ESM will have a preferred creditor status second only to that of the IMF. This provision essentially subordinates both existing and future claims by private investors in Euro Area sovereign bonds, thus undermining the current and future demand for sovereign securities. This provision needs to be clarified as soon as possible. In a welcome move, the new ECB bond purchases under the Outright Monetary Transactions (OMT) program announced in early September 2012 will be on *pari passu* terms with private holders of similar bonds.

In the long run, from the standpoint of crisis resolution, if full access to private capital markets is to be restored in line with the stated objectives of Euro Area leaders and fair burden sharing re-established, it will be important to remove both the preferred creditor status for official Euro Area lenders and the presumption that private investors will be subordinated in future financing of Euro Area members. In this context, the Euro Area leaders' decision in late June 2012 to allow a potential ESM support for Spain's bank recapitalization program to be on *pari passu* terms with private investors is welcome.

Recommendations

Sovereign issuers should treat fairly and provide comparable treatment to all creditors so as to avoid

discrimination against any individual or groups of creditors. No creditor or creditor group should be excluded *ex ante* from participating in debt restructuring. Any exceptions to this principle should be discussed and agreed to among all creditors on the basis of adequate justification. Broad creditor participation in debt restructuring operations is essential to ensure a fair burden sharing, including the impact of the provision of new financial assistance, as well as to avoid any new or intensify existing subordination of the claims by some classes of creditors.

Fair treatment of all creditors is in the interest of both issuers and creditors. It lessens the burden on all creditors and, by avoiding discrimination, encourages creditors to participate voluntarily in debt resolution and minimizes any adverse impact on the investor demand for existing or new issues of sovereign debt by the issuer undergoing debt restructuring or similar debtors in the region or fellow members of currency unions. Reduced demand for sovereign debt by private investors, and/or delayed resumption of market access by the sovereign debtor due to subordination concerns, increase the potential burden on official creditors and international or regional institutions to provide financial support to the adjusting country in larger volume and/or over a longer period of time than would otherwise be necessary.

Attachment I. Joint Committee on Strengthening the Framework for Sovereign Debt Crisis Prevention and Resolution

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Attachment II. *Addendum* to the Principles for Stable Capital Flows and Fair Debt Restructuring

This *Addendum* presents the recommendations of the Joint Public–Private Committee on Strengthening the Framework for Sovereign Debt Crisis Prevention and Resolution, endorsed by the Group of Trustees of the *Principles* on October 14, 2012, at its 2012 Annual Meeting in Tokyo. The Joint Committee was set up under the auspices of the Co-Chairs of the Group of Trustees in March 2012 to assess the recent experience with sovereign debt crisis prevention, management, and resolution in the Euro Area and elsewhere; draw appropriate lessons; and make recommendations on the strengthening of the existing framework for sovereign debt crisis prevention and resolution as embodied in the guidelines of the *Principles for Stable Capital Flows and Fair Debt Restructuring*. The recommendations included in the *Addendum* complement the *Principles* and provide amplification of the practical guidance for the implementation of the guidelines underlying the *Principles* to make them more practically relevant to the circumstances faced by mature market countries, including those that are members of currency unions.

1. Overall Assessment

The guidelines underlying the *Principles for Stable Capital Flows and Fair Debt Restructuring* remain an appropriate, relevant, and effective framework for sovereign debt crisis prevention and resolution. Their fundamental emphasis on sound policies and data and policy transparency by debtors is of critical importance in crisis prevention. Moreover, the underlying guidelines for voluntary, cooperative, market-based procedures for debtor-creditor dialogue and good-faith debt restructuring negotiations remain an essential cornerstone of sovereign debt crisis management and resolution and should continue to guide the interactions between sovereign issuers and their creditors. Such a cooperative approach would facilitate an early restoration of market access, which is of critical importance in achieving debt sustainability over time, and allow the official sector to gradually reduce its exceptional financial assistance to the countries under official sector–supported reform programs.

2. Data and Policy Transparency for Crisis Prevention

Sovereign debtors should pursue sound fiscal and growth-enhancing structural policies, consistent with macroeconomic and financial stability and public debt sustainability.

Sovereign debt issuers should ensure that they release on a timely basis comprehensive relevant data and other information related *inter alia* to their fiscal developments and debt positions (including, when appropriate, contingent liabilities) and on current and future policy plans. These data should be consistent with established accepted standards and norms (i.e. budget data should be released also on an accrual basis, not only cash basis) and verified by authorized domestic and regional agencies, especially with regard to their accuracy, comprehensiveness, and comparability over time.

Effective sovereign debt crisis prevention is a shared responsibility that requires—besides data and policy transparency and open dialogue with creditors by the sovereign debtors—sustained surveillance efforts by regional and international institutions and private sector groups; actions by regulatory agencies, accounting, and other international standard setters; as well as vigilance and enhanced risk management by private creditors and market participants in general.

The effectiveness and timeliness of surveillance by regional and international institutions of the consistency between policy plans and actual execution, and of national policies with regional commitments and undertakings for country members of currency unions, are critical for

promoting sustainable policies and market confidence. Clarity and transparency of information on actual economic trends and prospects are essential for facilitating effective risk management by market participants and efficient functioning of sovereign debt markets.

Private creditors and market participants are responsible for formulating accurate and appropriate assessments of underlying trends in market risks, and the credit and sovereign risks of individual issuers, thus ensuring a realistic pricing of sovereign debt instruments. In this context, private creditors and market participants should undertake their own due diligence, drawing *inter alia* on all available information from the sovereign issuers themselves and the assessments by regional and international financial institutions. The assessment of current economic and financial developments and the identification of underlying or emerging risks by private sector groups such as the IIF's Market Monitoring Group can also play a useful and constructive role in this process.

Regulatory agencies should take care in setting capital and other requirements for covered financial institutions to avoid distortions in market signals and biasing risk management practices.

Responsible and realistic assessments and timely analysis by ratings agencies can also provide useful complementary information to market participants, investors, and issuers and enhance crisis prevention.

3. Close Debtor-Creditor Dialogue and Cooperation for Crisis Prevention

Mature market country issuers should consider implementing the best practices for investor relations that have evolved. The adherence of emerging-market borrowers to these best practices are reviewed annually by the IIF and summarized in the annual Implementation Report of the *Principles* issued by the Principles Consultative Group.

Enhancement of investor relations under Investor Relations Programs facilitates timely data and policy transparency and a regular dialogue between sovereign issuers and their creditors and establishes an effective channel of communication and feedback. The experience over the past few years has demonstrated the value and contribution of IRPs in enhancing market confidence and maintaining market access even during periods of market tensions and turbulence.

Sovereign debt issuers in both mature and emerging market countries should incorporate in new bond issues, denominated in a foreign or a common regional currency, CACs with appropriate aggregation clauses, with comprehensive coverage of their terms and conditions in the bond documentation and easy access to this information by all investors. Issuers of domestic bonds denominated in local currency may also consider such arrangements. Appropriately designed aggregation clauses would allow bond holders across all outstanding issues of government securities to collectively decide on whether to accept potential offers from issuers to modify existing bond terms and conditions. The use of CACs inclusive of aggregation clauses can facilitate voluntary debt restructuring by reducing the chances of a small minority of bond holders acquiring blocking positions in a bond series and imposing demands for preferential treatment.

4. Good-Faith Actions in Cases of Debt Restructuring

(a) Voluntary Good-Faith Process

Good-faith negotiations remain the most effective framework for reaching voluntary debt restructuring agreements among sovereign debtors and their diversified private creditor community, particularly in the complex cases of mature market issuers that are members of currency unions. Such a framework has proved to be efficient in facilitating appropriate agreements on crisis resolution, while containing the adverse impact on market confidence and other disruptions and concerns caused by spillover and contagion risks.

Sovereign issuers and their creditors should strive to reach and effectively implement voluntary agreements on a timely basis to help minimize adverse market reactions and contagion effects. In this context, debtors and creditors should be cognizant of the potential adverse effects of the

interaction between sovereign debt and capital markets, to the detriment of the interests of all parties. With the increased sophistication, integration, and complexity of capital markets, for both emerging market and mature economy countries, the interaction among developments in sovereign debt markets, changes in the regulatory framework, and banking system practices gives rise to major dynamics with significant implications for credit expansion, risk practices, market access by sovereign debtors, and macroeconomic developments.

The dynamics and incentives for debtors and issuers to engage in good-faith negotiations are strongly influenced by the existing accounting and regulatory standards and their interaction across types of financial institutions and jurisdictions. The standard-setting bodies responsible for accounting and supervision rules, as well as the interpretation bodies, should be cognizant of the need to minimize inconsistencies between accounting and supervision practices and conflicts across jurisdictions and types of covered financial institutions.

The early restoration of market access is of critical importance in achieving debt sustainability over time. Early re-accessing of capital markets at reasonable costs is also essential for allowing sovereign debtors to reduce and eliminate their reliance on exceptional IMF financing and financial support from their official bilateral partners, such as is the case under currency unions or regional arrangements.

(b) Debtor and Creditor Actions During Debt Restructuring

To facilitate good-faith negotiations, sovereign issuers, and regional institutions in case of regional arrangements, should engage in enhanced data and policy transparency and dialogue with private creditors at an early stage, should a debt resolution become necessary. The early release of information on the scale of the adjustment needs and the range and scale of the envisaged corrective policies by the sovereign issuers themselves or in the context of adjustment programs supported by the IMF and/or regional institutions would help minimize adverse market reaction and contagion risks and facilitate continued or early resumption of market access. The sanctity of contracts should be respected. Modifications to these contracts should be avoided wherever possible as a matter of principle.

In the debt restructuring process, an early discussion is necessary between the representative private creditor committee and the sovereign debtor, in close consultation with the official sector, on the overall multi-year macroeconomic framework and objectives, including the broad fiscal policy targets and the underlying outlook for output growth and public debt under alternative assumptions on the debt restructuring. Such a discussion is important in facilitating an effective voluntary debt restructuring agreement on a fair burden sharing, thus promoting high private sector participation, restored market access, renewed output growth, and debt sustainability.

It should be recognized that the attainment of debt sustainability over time is a dynamic, complex process that depends critically on the quality and market credibility of actual and prospective adjustment policies undertaken by the debtor, the direction of macroeconomic policies, the terms and volume of financial support or debt relief provided by official and private creditors, and the prospects for the continuation or resumption of market access at reasonable terms. As such, the debt sustainability analysis entails judgments and assessments that are often not easily amenable to quantitative rules and that require revisions as macroeconomic parameters evolve. The contributions toward achieving debt sustainability by private creditors as well as other creditors should be considered simultaneously, with no one creditor group considered as a residual source of funding on an *ex ante* basis.

In this context, the IMF has a very important role to play by providing objective analysis and information on macroeconomic policies and prospects and on the sovereign debtor's medium-term funding needs, consistent with debt sustainability considerations.

(c) Creditor Committee Policies and Practices

Private creditors should organize themselves in a broadly based representative creditor committee

as early as possible in the debt restructuring process, certainly before debt default, which should be avoided if possible. Sovereign issuers should interact and engage in negotiations with their private creditors through the representative creditor committee and should consult with the creditor committee as part of the process of fulfilling the requirement under IMF policy of lending to debtors in arrears to make good-faith efforts to reach understandings with their creditors. Such a framework would be more conducive to reaching a voluntary agreement on debt restructuring and facilitate market access.

Private creditors that are members of the creditor committee negotiating with the sovereign debtor should abide by established ethical standards and *inter alia* respect the confidentiality of any material non-public information that may become available during this process and notably commit not to use confidential information from the negotiations for trading purposes.

This process will be aided in cases of countries that require financial assistance from multiple official bilateral creditors, as is usually the case for countries that are members of currency unions, by the formulation of timely and effective procedures for reaching understandings on the scale, terms, and conditionality of any envisaged financial assistance from these creditors so as to facilitate the negotiations between the sovereign debtor and the private creditor committee.

In line with the evolving practice, the sovereign debtor would be expected to cover reasonable costs incurred by a single private creditor committee for the legal and financial advisor fees, consistent with agreed parameters.

(d) Tools for Debt Restructurings

Sovereign issuers and their creditors should introduce CACs and possibly other options to enhance the credit quality of the new debt instruments used under debt restructuring exercises so as to enhance the prospects for high voluntary creditor participation. Retroactive legal changes to unilaterally modify the terms and conditions of financial contracts may undermine the integrity of financial markets and the sanctity of contracts and should be avoided. However, in exceptional cases and after a voluntary debt exchange agreement has been reached, such modifications of the governing legal framework to introduce a collective action mechanism on a timely basis with terms and thresholds consistent with market practices may be necessary in facilitating a voluntary debt exchange and achieving a fair outcome for all bond holders.

5. Fair and Comparable Treatment of All Creditors

Sovereign issuers should treat fairly and provide comparable treatment to all creditors so as to avoid discrimination against any individual or groups of creditors. No creditor or creditor group should be excluded *ex ante* from participating in debt restructuring. Any exceptions to this principle should be discussed and agreed to among all creditors on the basis of adequate justification. Broad creditor participation in debt restructuring operations is essential to ensure a fair burden sharing, including the impact of the provision of new financial assistance, as well as to avoid any new or intensify existing sub-ordination of the claims by some classes of creditors.

Fair treatment of all creditors is in the interest of both issuers and creditors. It lessens the burden on all creditors and, by avoiding discrimination, encourages creditors to participate voluntarily in debt resolution and minimizes any adverse impact on the investor demand for existing or new issues of sovereign debt by the issuer undergoing debt restructuring or similar debtors in the region or fellow members of currency unions. Reduced demand for sovereign debt by private investors, and/or delayed resumption of market access by the sovereign debtor due to subordination concerns, increase the potential burden on official creditors and international or regional institutions to provide financial support to the adjusting country in larger volume and/or over a longer period of time than would otherwise be necessary.

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Annex V. Best Practices for Investor Relations[1]

This section expands on the best practices developed in the Institute of International Finance (IIF) Action Plan of 2002. The best practices build on the key elements of the 2002 list. A central feature of a successful investors relations program (IRP) is the country's direct communication with market participants. The "Strengthened Investor Relations Best Practices" highlights the importance of formal communication channels between countries' authorities and market participants. In the countries' efforts to formulate market-informed macroeconomic policies, IR provides the opportunity to obtain investors' feedback in the formulation of economic policies. The new best practices also stress the need for continuous self-assessment. These best practices incorporate the following elements:

IRO/IR Staff

The investor relations office (IRO) is the first and formal point of contact between market participants and authorities. It is a "one-stop shop" through which authorities can provide investors relevant data and information from the diversity of official sources, and investors can access relevant policymakers and provide policy feedback. It is important to have a designated IR officer, or IRO; however, the location of the office is not important (i.e., within the Treasury, Central Bank, or Ministry of Finance).

The job of the IRO staff is a dynamic one. The staff

- Facilitate two-way communication channels with investors through emails, conference calls, and the IR website.
- Brief senior policymakers about market feedback and concerns, overall market sentiment with respect to asset class and general global environment, and anticipated market reactions to policy changes under consideration.
- Disseminate relevant macroeconomic data and policy information (see below) to market participants and answer questions about the data, information, and other related issues.
- Coordinate access of data and information from various official institutions and develop a network of officers in various government agencies and the Central Bank who can answer investor queries.
- Coordinate access of market participants to senior policymakers.
- Coordinate internally the country's "message" and convey this message to investors.
- Present a coordinated and streamlined message and explain any changes in policies or data.
- Maintain credibility by acknowledging weaknesses in policies and the economic situation at investor briefings but should not serve as an advertising campaign for the government.

Both corporate and sovereign IR officials have identified proximity to senior policymakers as one of the most crucial aspects of an IRO. Commitment by senior policymakers at the highest level is crucial to the effective functioning of an IRO. At the same time, it is important that the IRO and its staff be insulated from changes in the political environment.

The core staff should have an understanding of market practices as well as economic policies and should be able to articulate those to both policymakers and investors. Regular contacts with investors also help the IRO staff develop a "fabric of trust" and anticipate and reduce vulnerability to shifts in market perception. In addition, regular use of outside market sources should enable IRO staff to gauge investor perceptions and shape an effective communication strategy. As investor confidence

[1] The Strengthened Investor Relations Best Practices are presented in the report *Investor Relations: An Approach to Effective Communication and Enhanced Transparency – 2005 Assessment of Key Borrowing Countries*, published by the Institute of International Finance in December 2005.

begins to slip, more direct involvement of senior policymakers in the IR process may be required.

IR Website

All IRPs should have, as an essential component, a regularly updated, state-of-the-art website.

The IR website is a vehicle for providing relevant data and information to investors in a user-friendly format. It is a tool to most efficiently convey a country's policy objectives to the market with an option for seeking feedback and answering questions. It enables IRO staff to survey investors regarding future policy direction or to conduct self-assessments. To be effective, an IR website needs to present information simply and in a format that is well organized, user-friendly, and easy to navigate. It should have the following components:

- Information on economic data and policies as defined below. These data should be in a format that can be manipulated by investors.
- Archived PowerPoint presentations or audio/video streaming of investor teleconferences or videoconferences.
- Links to websites for various official agencies and reciprocal links to their own website on those agencies' sites.
- Registration for investors who would like to be included in IR activities.
- Frequently asked questions (FAQs).
- Contact information for the IRO and relevant IR staff.

Dissemination of Macroeconomic Data and Policy Information

The IRO is responsible for coordinating and collecting market-relevant data and information to be disseminated to investors through the IR website or by email to an investor contact list. To be effective, the IR staff should execute this function using the following operating principles:

- **Timely and regular dissemination data releases and policy information.** Use a release calendar to notify the market of upcoming releases well in advance. This will help dispel market rumors that may emerge from lack of information.
- **Limited general information.** Rather, provide specific, tailored interpretations that give insights into the information. This is particularly important when the information is negative or during difficult circumstances arising from higher risk aversion by market participants or challenging domestic economic or political conditions.
- **Clear and user-friendly format.** Provide data in a Microsoft Excel format that can be manipulated, as opposed to providing PDF and Word formats. In addition, present data in a time series of at least 2 years, as opposed to just current data and previous period data. The highest level of "market-friendliness" is the ability for investors to specify parameters such as time period and currency to obtain tailor-made time series that can be downloaded into Excel. Quality data in categories most useful to the market are preferred over large quantities of data that are less useful. In terms of data provision, special efforts should be made regarding forward-looking information. The IRO should "defend" or explain forecasts provided in a timely manner. IROs should let investors know if there have been any changes in the technical definitions of data or revisions made to the data.

The following types of information—core statistics for fundamental economic analysis—should be disseminated regularly to investors through the IR website or to a comprehensive "investor list" via email notification:

- **Data on economic performance** based on the international data standards as they pertain to the International Monetary Fund's (IMF's) encouraged special data dissemination standard (SDDS). This requires timely provision of statistics of the real sector as well as of the fiscal, external, and financial sector statistics. These data should be supplemented as necessary by methodological notes. (See section

on data release practices for further analysis.) The IRO website should contain an indexed archive of the data or links to other government sites where the data are available.

- **Data for the 15 core indicators for financial sector soundness as identified by the IMF.** The IRO website also should contain an indexed archive of this information.
- **Forward-looking information on economic policies** such as budget projections, monetary policy targets, and structural factors (e.g., legal, regulatory, governance frameworks) supported by the data as appropriate. The IRO website also should contain an indexed archive of this information.

Additional Key Data

The Working Group on Crisis Prevention has highlighted the crucial importance of the availability of market-relevant data not currently prescribed by the SDDS but crucial for adequate economic assessment in three key areas: (1) central government operations, (2) central government debt, and (3) external debt. A detailed description of the encouraged and prescribed elements of these data is provided by the IMF and IIF standards.

- **Central government operations.** Tracking data for central government operations allows for a more timely analysis of a country's fiscal position than general government or public sector data.
- **Central government debt.** The assessment of debt sustainability is an integral feature of the country risk assessment. Disclosure of debt service schedules and currency breakdowns are needed to provide a more accurate picture of countries' future payment obligations. Countries also are encouraged to disseminate information that reflects liabilities of the central government in a comprehensive fashion and, where relevant, debt of other entities that is guaranteed by the central government. Disclosure of such information can help identify fiscal risks under different scenarios at an early stage.
- **External debt.** As demonstrated by previous crises, a country's debt profile can influence its resilience to external shocks. The availability of assets and liabilities of the private and public sector held by nonresidents provides a picture of potential balance sheet vulnerabilities in domestic sectors. To carry out an adequate assessment of a country's international position, investors attach importance to the availability of nonresident holdings of private and public debt issued domestically as well as the resident holdings of external debt issued internationally.

IR Contact List

The IRO should develop and maintain a comprehensive list of contact information for investors, analysts, rating agencies, and other market participants who regularly track the country. This list should be supplemented with contact information for institutions that have key relationships with local financial institutions. The list should be maintained regularly and can be enhanced to target specific investors, if appropriate. Countries should maintain comprehensive contact lists so that they know, at any given time, who their investors are and so can evaluate how certain types of creditors will behave during times of vulnerability.

Feedback and Communication Channels

Feedback mechanisms are essential to foster two-way communication between investors and policymakers. Formal, regular channels should be created for responding to questions from investors, encouraging feedback about concerns, and communicating this information to key policymakers to enable them to make market-informed policy decisions.

These channels could be established through

- Teleconferences or webcasts with investors.
- Bilateral meetings between investors and senior policymakers.
- Phone or email contacts via the IRO.
- Interactive deal/non-deal roadshows.

Teleconferences or Internet-based webcasts should be led by senior "decision makers" such as the

undersecretary of finance or deputy governor of the Central Bank and can be moderated by the head of the IRO. Teleconferences/webcasts on key economic data and policies should be conducted on a quarterly basis, at a minimum. In addition, issue-oriented conference calls that are not part of the regular framework can help address questions and dispel rumors related to specific events or policy decisions.

Investors should be alerted about upcoming teleconferences/webcasts via email and should be provided with relevant information in advance to facilitate feedback and questions and to enable policymakers to focus on key issues. Policymakers should understand and communicate in the "language" of the investor community. Presentations should be uncomplicated and "forward looking." Teleconferences and webcasts should be recorded for replay, and any associated material provided in advance to investors should be archived on the IRO website. To provide a level playing field, policymakers should provide the same information to all investors.

Investors value face-to-face interaction with senior policymakers through bilateral meetings. They should be able to **directly contact IRO staff via email or phone** to ask specific questions or to arrange meetings with senior policymakers. If the IRO staff is unable to process the request directly, it should coordinate with counterparts in other government agencies, ensuring that it can respond to investors in a timely manner. Non-deal roadshows to key financial capitals (conducted on a semi-annual basis or as opportunities arise) also are an important tool to foster dialogue. High-level interactions become even more important when a country faces difficult times.

Times of Diminishing Market Confidence

Issuers who support the *Principles* agree that countries accustomed to dealing proactively with market participants will have a head start in stepping up the consultation process with market participants in response to signs of eroding market confidence. Such swings in market sentiment may be attributed to challenging economic and political prospects or contagion from developments in other emerging markets.

As market confidence begins to diminish, authorities should intensify consultations with market participants. IR staff can help deflect contagion by providing investors with a better understanding of policy goals and prospects, respond to investor inquiries, and in effect help investors differentiate among countries within the same asset class. IRO staff are capable of independently responding to contagion risk, in contrast to government polices put in place under challenging conditions that require the support of their authors. In cases where challenging domestic conditions exist, the involvement of senior policymakers in the IR process is essential to adding credibility to policies. Under these circumstances, policymakers at the most senior level should make exceptional efforts to help alleviate market uncertainty by explaining the rationale of economic measures undertaken and demonstrate their preparedness to take market feedback into account when formulating additional action. The frequency of economic data and policy information provided to investors should be maintained or intensified—not reduced.

Teleconferences or webcasts with investors should become more frequent and led directly by finance ministers, Central Bank governors, or other senior policy officials as necessary. In such circumstances, an appropriate tool for engaging in a direct dialogue with investors may be through interactive non-deal roadshows in key financial capitals. The roadshow should be conducted by senior policymakers from all appropriate official agencies.

Regular Self-Assessment

IROs should conduct annual assessments to ensure they are providing the best possible services to policymakers and investors, including providing timely, accurate, and relevant information, reaching all targeted investor groups, receiving and effectively processing feedback, and using the most optimal technology to reach out to investors. IRO staff can conduct self-assessments or use outside consultants such as the IIF's Sovereign Investor Relations

Advisory Service (SIRAS). Investor surveys on the IRO website or to the investor contact list also would be useful. To be effective, IRO activities can be benchmarked against IIF IR best practices or other guideposts, such as corporate IRO best practices.

Press and IR

Several authorities have been explored co-mingling press and IR functions in a single IRO.

While the thrust of these functions is similar, as they both involve communicating with the external environment, the key differences between them provide convincing arguments that they should be kept separate.

- **Audience.** IR staff must deal daily with market participants who track a country's economic performance and policies on a regular basis. These investors and creditors are sophisticated in their knowledge, and they demand specific detail about the environment and outlook for economic policies and data. The press, on the other hand, is more interested in "big-picture" information that would appeal to its own audience rather than in technical details.
- **Content.** Investors require market-relevant information or data on economic policies that conform to international standards, forward-looking information on economic policies such as budget projections and monetary policy targets, and information on legal and regulatory frameworks. This information must be tailored to reflect the different requirements of various investor groups, such as bond holders, in both domestic and international capital markets, as well as equity investors. Press content focuses more on broad issues related to economic policy or political developments that do not require technical explanation or a detailed understanding of policy formulation.
- **Staff.** The skill set of IR staff differs significantly from that of press relations staff. Most importantly, to effectively communicate with market participants, IR officers must be able to speak in the language of the market (i.e., have an in-depth technical understanding not only of a country's economic performance and policies but also of how markets operate). They must be able to answer investor queries and provide market feedback to senior policymakers. While press relations staff must have a basic understanding of economic performance and policies, their skills should mostly be focused on public relations and dealing with press contacts, as well as "managing" both positive and negative political developments.

Annex VI. Best Practices for Formation and Operation of Creditor Committees

I. INTRODUCTION

The best practices for the formation and operation of Creditor Committees are based on extensive discussions among members of the IIF's Working Group on Crisis Resolution. Additionally, these best practices have been broadly endorsed by the Principles Consultative Group. The PCG consists of senior officials from a broad cross-section of emerging market economies and senior bankers and investors involved in emerging markets finance, many of whom have been involved in the formulation of the *Principles for Stable Capital Flows and Fair Debt Restructuring*. This Group has been engaged in both encouraging and monitoring the practical application of the *Principles* through assessments of a variety of country cases. The PCG's input has been important in the shaping of these best practices in order to encourage participation from debtors who support the *Principles*. The *Principles* recommend the use of Creditor Committees in cases in which a debtor defaults on its debt to private creditors and investors. In fact, the key advantage of Creditor Committees for debtors has been that endorsement of the terms of a debt restructuring by the Committee signals acceptability of the deal to the wider creditor community and ensures the support of a "critical mass" of creditors and investors.

The best practice principles for the formation and operation of Creditor Committees are based on established practices of the traditional London Clubs and adapted to the world of capital markets. As such, these principles aim to reflect the impact securities laws may have on both the Committee's operations and creditor-debtor interactions. They also reflect experience gained in corporate restructurings.

Going forward, support from other key bond investors should also be sought. The best practice principles should also be explained to the IMF and G-7 officials in order to facilitate supportive official sector policies, in particular as the IMF reviews its lending into arrears policy. It is important to stress that negotiations in good faith should remain the essence of debt restructurings. A move away from good-faith negotiations between issuers, creditors, and investors on the basis of a limited number of exceptions is inconsistent with the international understandings that have been historically at the heart of sovereign debt restructurings. Such negotiations are also the operational consequences of the restoration of Collective Action Clauses (CACs), which have been welcomed by the G-7 and the IMF.

II. THE ROLE OF GOOD-FAITH NEGOTIATIONS AND CREDITOR COMMITTEES IN THE *PRINCIPLES* FOR EMERGING MARKETS

General Guidelines for Sovereign Debt Restructurings

The *Principles* provide general guidelines that lay the basis for a voluntary, good-faith debt restructuring process. Paramount among these guidelines is the notion of good-faith negotiations between a debtor and its creditors; the *Principles* put these two parties at the center of the negotiation process. The *Principles* recognize the sovereignty of the debtor while upholding the sanctity of contracts during debt restructurings.

Good Faith

The *Principles* place great importance on good-faith negotiations as a key element of the debt restructuring process. They call on creditors and debtors to "engage in a restructuring process that is voluntary and based on good faith. Such a process is based on sound policies that seek to establish conditions for renewed market access on a timely basis, viable macroeconomic growth, and balance of payments sustainability in the medium term." The *Principles* add that "debtors and creditors agree that timely good-faith negotiations are the preferred course of action toward these goals, potentially limiting litigation risk." Such negotiations are thus at

the heart of the restructuring process, including the operation of Creditor Committees.

However, it is very difficult to come to a precise definition of "good faith" and it is neither wise nor practical to seek an exhaustive set of criteria to evaluate this principle. We agree that, rather than defining the principle itself, the most productive approach is for any participant in the negotiation process to indicate when it believes that actions of another party have not been conducted in good faith.

Creditors and Debtors at the Center of the Negotiation Process

As a joint product of issuers and investors, the *Principles* maintain that the final result of the restructuring process should be obtained through cooperative interaction between the debtor and its creditors. (See above section on good faith.) The Principles also maintain that "regardless of the specific restructuring mechanics and procedures used (i.e., amendment of existing instruments or exchange for new ones; pre-default consultations or post-default committee negotiations), restructuring terms should be subject to a constructive dialogue focused on achieving a critical mass of market support before final terms are announced."

Sovereignty of the Debtor

The *Principles* recognize the sovereign nature of the debtor. They emphasize the importance of putting a country back on a sustainable balance of payments path, while preserving and protecting asset values during the restructuring process. At the same time, they also uphold the sanctity of contracts between sovereign debtors and creditors, stating that, "subject to their voluntary amendment, contractual rights must remain fully enforceable to ensure the integrity of the negotiating and restructuring process."

The Role of Creditor Committees in the *Principles*

The *Principles* support debtor-creditor negotiations as the preferred way forward in cases which require a debt restructuring. They also articulate the role of Creditor Committees in such negotiations, especially in cases of default.

Under the sub-principle "vehicles for restructuring" the *Principles* state,

> The appropriate format and role of negotiation vehicles such as a creditor committee or another representative creditor group (hereafter referred to as a "creditor committee") should be determined flexibly and on a case-by-case basis. Structured, early negotiations with a creditor committee should take place when a default has occurred in order to ensure that the terms for amending existing debt contracts and/or a voluntary debt exchange are consistent with market realities and the restoration of growth and market access and take into account existing CAC provisions. If a creditor committee is formed, both creditors and the debtor should cooperate in its establishment.

Recent experience has been mixed, with authorities taking different approaches that were not in all cases seen by creditors as fully consistent with the *Principles*. All of the cases have been complex, involving a diverse set of market participants, instruments, and currencies. In many occasions, creditors have organized themselves into Creditor Committees at an early stage. In some cases, debtors have negotiated in good faith with Creditor Committees to reach restructuring agreements. In others, ad hoc Committees have been formed; debtors have preferred to consult with these Committees as well as with other creditors on a bilateral basis toward the formulation of an exchange offer. In some cases, the approach by sovereigns has been seen by creditors as coercive. In such instances, the spontaneous formation of Creditor Committees has been frequently resisted by the debtor country with the argument that the situation does not call for a Committee or that the Committee is not representative.

As the *Principles* will be reviewed from time to time and possibly updated, the circumstances under which Creditor Committees are the best avenue for a restructuring may be reviewed. For example, in one recent case, the restructuring with the private sector

was preceded by a restructuring with the Paris Club with the usual request for comparability of treatment. The *Principles* do not "require" negotiations with a Committee in non-default cases, but the question has been raised whether a Committee approach should be preferred in circumstances in which a restructuring is mandated by the Paris Club. This seems to be a logical consequence of the comparability of treatment principle.

If a Creditor Committee is formed, the *Principles* provide guidelines in order to enhance its effectiveness. They stipulate that Creditor Committee "should

- Adopt rules and practices, including appropriate mechanisms to protect material non-public information;
- Coordinate across affected instruments and with other affected creditor classes with a view to form a single Committee;
- Be a forum for the debtor to present its economic program and financing proposals;
- Collect and analyze economic data;
- Gather, evaluate, and disseminate creditor input on financing proposals; and
- Generally act as a communication link between the debtor and the creditor community."

In addition, in October 2004 the International Primary Market Association (IPMA)[1] released standard collective action clauses for fiscal agency agreements under English law that contain provisions for the appointment of a single Creditor Committee.

III. BEST PRACTICE PRINCIPLES FOR CREDITOR COMMITTEES

1. Key Concerns Regarding Creditor Committees

Over the past few years, establishing Creditor Committees has faced certain hurdles. On the one hand, debtors have in some cases objected to recognizing Creditor Committees for various reasons: either because they were not involved in the formation of the Committee, had reservations regarding certain Committee members with whom they did not want to negotiate, questioned the Committee's representativeness, or because they simply did not want to negotiate with creditors and investors. On the other hand, some members of the creditor community have been reluctant to join Creditor Committees if they saw it as constraining their range of options.

Perceptions by some issuers that the Committee process is slow-moving and causes delay in the resolution of a debt problem have also been cited as a reason that they have favored a unilateral approach. When considering such an approach, issuers should be aware that refusal to negotiate may result in low participation and expensive lawsuits, and as a result possible constraints on market access.

Much of the debate has centered on the issue of "representativeness" of a Creditor Committee. In some cases, issuers' legal advisors have questioned whether Committee members have secured mandates from other members of the creditor community in order to represent them. Such a request goes against the grain of reality, however. Historically, members of Creditor Committees have not "represented" other creditors and investors but they have reflected the views of the creditor community during the negotiations with a view toward attracting a critical mass of support for negotiated restructuring terms. In a small number of cases, a group of creditors and investors, in particular fund managers, have appointed a representative to the Committee to negotiate on their behalf.

Representativeness has also been interpreted to mean sufficient diversity of creditors and investors. Diversity in turn has caused concerns in some quarters that Creditor Committees are cumbersome to deal with, especially since different members of the creditor community may have divergent interests because they may have purchased credit default swaps or other protections, or because they may have

[1] On July 1, 2005, IPMA merged with the International Securities Market Association (ISMA). The combined entity is known as the International Capital Market Association (ICMA).

acquired instruments on the secondary market and thus are not original holders.

In today's market, a Committee having a diversity of creditors and investors would mean having banks, fund managers, hedge funds, and retail investors either represented and/or directly involved. However, debtors have objected that some types of creditors and investors who would need to have representativeness are not capable structurally of maintaining the needed confidentiality and obeying the applicable insider trading rules.

While confidentiality was protected by unwritten rules in the 1980s and 1990s, today's world of securities offerings has set higher standards.

One issue relates to the type of information a debtor can release ahead of an offering. (Unregistered offerings are speedier and lower cost options but the release of the "wrong" type of information may delay or prohibit the debtor from proceeding with an unregistered form, and instead a registered offering may be required.)

The other issue is that securities laws (in most jurisdictions) preclude trading on non-public material information, and a Committee is likely to come in contact with such information. This is a concern for creditors, investors, and debtors. For creditors and investors, the "stop trading" rules of some previous restructurings are not feasible. For the debtor who may bear many of the negative consequences of information leaks and insider trading, a "no trading" rule may be preferred for Committee members.

As a possible solution, a "code of conduct" has been used in a few cases in the sovereign context but cues have been taken in particular from corporate restructurings. Such a code is an agreement between the debtor and the Creditor Committee on a range of issues. It imposes simple restrictions on confidential information on both sides and offers more flexibility on trading for Committee members who commit to complying with insider trading rules.

The best practice principles articulated below address these key concerns as well as other issues with the aim to develop a better basis for Creditor Committees to be acceptable to issuers and protect the rights of creditors and investors.

2. Creditor Committee Best Practice Principles

A. Initial Formation

The initiative of forming a Creditor Committee can be taken through various approaches: the debtor can ask for a Committee to be formed—this has occurred in a few cases; the debtor and its creditors and investors (hereafter called "the creditor community"[2]) agree to form a Committee—this has been the most common case; or the creditor community initiates the formation of a Committee that reflects their interests.

B. Cooperation and Trust

1. In order for the negotiations to proceed in an orderly manner, an element of trust must be developed between the debtor and the members of the Committee, as well as among Committee members themselves.

2. The *Principles* call on the debtor and the creditor community to cooperate in the formation of the Committee. It is thus important to be aware of certain sensitivities a debtor may have regarding individual creditors and investors.

C. Diversity of the Creditor Community

1. The Committee should consist of creditors and investors who can reflect the interests of the range of members of the creditor community affected in the negotiation process.

2. Diversity of Committee members should encompass not only financial instruments and investment strategies but also regional differences. The latter is particularly useful in order to consider differential tax treatments and regulatory differences that may help design options to facilitate the participation of the creditor community in different jurisdictions in the restructuring.

[2] The "creditor community" includes banks, fund managers, hedge funds, and retail investors.

3. In order to facilitate participation by hedge funds and asset managers who may face conflicts of interest when they come into contact with material non-public information or other constraints (staffing, for example), an external representative could be appointed by either an individual fund or a group of fund creditors and investors, if considered necessary. Such an individual should have appropriate restructuring experience (as described below) and operate under his terms of reference. This representative would be bound by confidentiality parameters (see below) and would provide only the necessary information that his clients need in order to make decisions regarding the restructuring negotiations.

4. The Committee should be of a manageable size, but Committee membership should not be limited only to "large" creditors and investors. At the same time, the Committee as a whole should hold or represent a substantial amount of claims and include a diverse set of creditors and investors (see "Diversity" above).

5. A Committee must have credibility with the debtor and be able to signal that it has influence with a critical mass of all creditors and investors.

D. Speed of Process

1. The creditor community should work closely with the debtor toward the formation of the Committee, recognizing that this process can be initiated through different channels. There should be a presumption that speed is of the essence.

2. Creditors and investors should consider approaches to internal coordination that expedite rather than delay the process.

3. Creditors, investors, and the debtor should agree on the negotiation process that should be followed, including the nature and sequence of the discussions. Such an understanding, which of course should not delay the actual negotiations, could help inform the IMF, for example if judgments on lending into arrears need to be made.

4. Committee members should take into account the time commitment they must set aside from their day-to-day work in order to participate in restructuring negotiations. To ensure continuity, it is important that a particular creditor or investor be represented by the same individual throughout the restructuring process.

5. Effective Committee leadership will be key to ensuring an efficient Committee process.

E. Confidentiality

1. The members of the Committee, the debtor, and advisory firms should consider agreeing on and signing a "code of conduct."

2. Any information not already in the public domain is considered confidential.

3. Under the code, parties have to refrain from disclosing confidential information to anyone other than a list of related parties (provided they also subject themselves to the code) unless required by law.

4. Under the code, parties could issue periodic press releases that comply with applicable securities law to "share information with the market." Information must not be released that either "conditions the market" for an offering or that could be seen as deceptive.

5. Legal advisors to parties should advise on what information can be released.

6. Committee members should implement Chinese Walls or similar measures to ensure that those who make trading decisions are not in the possession of confidential information that is shared in the context of a restructuring negotiation.

7. Negotiations should take place directly between the debtor and creditors, without the participation of multilateral or bilateral organizations. Both debtor and creditors should avoid commenting on the negotiations.

F. Restructuring Experience

1. The "tool kit" of at least some of the Committee members' experience should include practical skills in sovereign and/or non-sovereign restructurings.

2. Creditors and investors who are new to the asset class should not be excluded for lack of experience, in particular if their claims are substantial.

3. Committee members should consider the feasibility of particular restructuring proposals they aim to advance with the debtor.

G. Legal Advisors

1. The law firm representing the Committee should have ample debt restructuring experience.

2. If the firm has business relationships with Committee firms, in particular those with sizable shares of the outstanding debt, potential conflicts of interest should be addressed internally.

H. Logistical Support

1. Creditor Committee members should share responsibilities for providing facilities and staff to arrange meetings and for handling communications with the debtor as well as other members of the creditor community not on the Committee.

2. The clearing system should be leveraged as a communication tool in cases in which a substantial amount of debt is held at the retail level.

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