Latin american debt: an international bargaining perspective*

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Introduction

No assessment of new or recently re-established democracies in Latin America can overlook the threat to these regimes posed by debt service obligations that are often heavier and more durable than the reparations imposed on Weimar Germany. No discussion of the weakening of the liberal international economic order (the trend towards trade protection, chronic instability in currency and financial markets) can disregard the extreme pressures to export, to compress imports, and to conserve foreign exchange that shape the economic policies of the heavily indebted LDC nations. No analysis of the scope and limitations of monetary policy in the developed countries (and especially in the United States) will be complete unless it takes into account the consequences for the major banks of a sovereign debt exposure which remains even now very large in relation to shareholders' equity, and which still frequently appears in bank accounts at an unrealistically optimistic valuation.

However, serious literature on the debt issue has tended to isolate specific facets of the problem, no doubt reflecting the academic background or the policy concerns of individual authors. *Economists* have written extensively about the 'adjustment' process by which the economies of indebted countries are expected to adapt to the abrupt reversal of net capital flows. Some of the implication for long-run development strategy have been studied, and a great deal has been written about short-term macro-economic policy, especially concentrating on fiscal balance and export promotion. Much of this literature treats the individual indebted country as the unit of analysis. Of course international economists, also consider the 'problem of aggregation' that arises when a large number of countries simultaneously attempt the same policy switch (perhaps competing against each other for a relatively fixed supply of external assistance).[1]

Political scientists have also contributed to the case-by-case approach, notably by discussing the political constraints on 'adjustment' in individual

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[1] Recent examples include Rudiger Dornbusch, *Dollars, Debts, and Deficits* (Cambridge, Mass., 1987); Rosemary Thorp and Laurence Whitehead, *Latin American Debt and the Adjustment Crisis* (London, 1987); William R. Cline, *Mobilizing Bank Lending to Debtor Countries* (Washington, DC, 1987); and Richard E. Feinberg and Ricardo Ffrench-Davis (eds.), *Development and External Debt in Latin America: Bases for a New Consensus* (Notre Dame, 1988).

countries, and sometimes by speculating on the longer term political consequences of protracted austerity.[2] Perhaps the most interesting result of their discussion has been a negative finding – it has proved harder than expected to identify clear political constraints to even the harshest forms of economic adjustment; there is as yet no strong correlation between protracted austerity and political authoritarianism; popular protest against economic hardship has been less widespread and less effective than anyone would have dared to predict five years ago.[3] But these are very tentative results and in any case they are muffled by the intricate particularities of each national experience.

From the other side *financial analysts* have examined the predicament of the creditor banks, carefully considering not only the accounting and regulatory framework, but also the diverse interests and rival bargaining strategies of different types of bank – large versus small; American v. European v. Japanese; official v. commercial and so forth. Although these writers often display a great deal of sophistication and ingenuity in their treatment of the technical aspects of the problem, they may overstate the scope for devising 'solution' to the underlying conflicts of interest by resort to financial wizardy. They tend to rely on traditional banking concepts like 'insolvency versus iliquidity' which assume a framework of commercial law that can perhaps be applied unambiguously to corporate debtors in advanced capitalist markets, but which may obscure more than it illuminates when transferred to the international arena and applied to sovereign debt.[4]

Some international aspects of the debt crisis have also received considerable attention,[5] although this has been focused on a limited range of relatively precise issues especially those of interest to policy-makers and advisers in the principal bureaucratic agencies affected (such as the IMF, the World Bank, the Bank for International Settlements, UNCTAD, GATT, and the UN Economic Commission for Latin America and the Caribbean and so on).[6] In the first few years after the debt crisis broke (August 1982) much of this literature rested on the assumption that these agencies were faced with a short-term emergency. Provided the parties concerned worked together on correctly designed remedial measures, it was assumed that there would shortly be a return to something like the status quo ante. The alternative was thought to be some very dramatic and destructive upheaval – a danger to be averted at all costs, but not in truth a very likely outcome or one worthy of precise analysis. Authors

2 For example Robert R. Kaufman, *The Politics of Debt in Argentina, Brazil and Mexico: Economic Stabilization in the 1980s* (Berkeley, 1988).

3 Karen Remmer, 'Debt and Democracy? The Political Impact of the Debt Crisis in Latin America', Paper delivered to an International Conference on Financing Latin American Growth at the Jerome Levy Economics Institute, Annandale-on-Hudson, New York.

4 An interesting and constructive recent example of this approach is provided by the Chairman of American Express, James D. Robinson III, 'A Comprehensive Agenda for LDC Debt and World Trade Growth' (Overseas Development Council, Washington, DC, February 1988).

5 One useful collection is Miles Kahler (ed.), *The Politics of International Debt* (Ithaca, NY, 1986).

6 Part One of the UNCTAD *Trade and Development Report 1988* (New York, September 1988) is a good, up-to-date example of this genre, from the debtor countries' point of view.

working within this framework naturally tended to exaggerate the wisdom, autonomy and leverage of the agencies with which they were associated. Only recently has this outlook been reconsidered as it became apparent that there was a third alternative between the return to normalcy and a catastrophic breakdown – namely a protracted, gruelling and inconclusive tussle between debtors and creditors, which mediating agencies would have no more than a limited capacity to ameliorate.

Finally there have been a succession of declaratory statements and programmatic documents, claiming to address the many ramifications of the debt issue. The Cartagena Group of Latin American leaders set up in 1984 has produced one set of position papers, and keynote speeches at Annual Meeting of the Brank/Fund have summarized the 'First World' response. Few of these statements and documents are of much lasting value. The most celebrated initiative was the so-called 'Baker Plan', launched in an address to the September 1985 meeting of the Bank/Fund by the then US Treasury Secretary James Baker III.[7] A brief consideration of the Baker Plan should suffice to illustrate the limitations of all the declaratory statements of the kind that have been made to date. Secretary Baker's speech was regarded as a major shift of ground by the Reagan administration after three years of 'malign neglect' under his predecessor in the Treasury Donald Regan. The Baker Plan not only conceded many of the analytical points made by Third World critics of the Western policy response, it also specified a new strategy with a definite volume of additional resources to be made available for fifteen named debtor countries within a relatively short period of time. Even those critics who considered the whole initiative quite inadequate had to concede that it seemed like a major step in the right direction. But unlike say the Marshall Plan or the Alliance for Progress, the Baker Plan in fact created no institutional framework to guarantee or even to monitor its implementation. Three-and-a-half years later there is no objective way to assess the results of the initiative, other than to note that the hope for 'new money' from the commercial banks never materialized. No one can even say which of the fifteen debtors was a beneficiary under the plan. It is thus impossible to give a rigorous answer to such questions as 'was the Baker Plan a success?' or 'was it adequate to the situation?' let alone 'what lessons can we draw from this experience?' According to the circumstances almost everything that has been done for the debtors by the West since October 1985 could be attributed to 'the Baker Plan' – or nothing.

In March 1989 Baker's successor at the US Treasury, Nicholas Brady, opened a new phase of negotiations by conceding the need for debt reduction (not forgiveness, however). It is too early to judge the impact of this initiative, but the Brady approach does implicitly recognise the inadequacies of the Baker plan, and for the first time it loosens the bonds uniting creditors into a common front.

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There are several aspects of the debt issue that should be of particular interest to students of international relations. Clearly a narrowly state-centred approach would fail to account for the major roles played by such non-state actors as the commercial banks, the international financial institutions, and such

[7] Pedro-Pablo Kuczynski, *Latin American Debt* (Baltimore, for the Twentieth Century Fund, 1988) reprints the text of Baker's speech as an appendix.

'trans-national' actors as the fraternity of central bankers, or indeed the networks of public and private financial institutions within the debtor countries. Indeed, it could be argued that even adding such non-state actors to the analysis would be inadequate for the debt problem reflects structural characteristics of the international economic system that go beyond the scope of all actor-centred interpretations. Capital flight is a major complication that requires a structural explanation. But in the 1980s the Latin American debt problem has been punctuated by episodes of crisis – such as the Mexican rescue packages of August 1982 and July 1986 and the Brazilian interest moratorium of February 1987 – in which the deliberate actions of governments have come to the fore. If a structural situation gives rise to manifestly harmful and destabilizing consequences, major actors will attempt to modify that structure (often, no doubt, with unintended results). In conditions of national economic crisis or emergency, governments will intervene, even in areas which in more normal times are the responsibility of private agents.

Thus although a narrowly state-centred approach would be inadequate for explaining the Latin American debt problem, it would be equally mistaken to ignore the privileged role of state action in shaping, precipitating (and conceivably even in resolving) that problem. After all, Latin American governments chose (or were forced?) to socialize much of the debt of their private corporations at the same time that they confronted an acute public external debt squeeze. The major commercial creditors bargain directly with Latin American presidents and economic cabinets, and their strategies are closely monitored (even perhaps supervised) by their home finance ministries and Central Banks. At least in the 1980s, and at least in Latin America, the debt crisis has uncovered the last resort character of state involvement in the international lending process. African experience has been different in that private capital flows were never so important, and East Asian experience is also different in that for the most part the last resort role of the state has remained pretty much hidden behind the activities of private agents. But an international relations perspective on the power realities uncovered by the Latin American debt crisis should be of more than purely regional interest.

This article focuses on a few issues, which frequently arise in international relations, and which reapper in a distinctive guise in discussions of Latin American debt. The brief historical survey to follow looks particularly at the relationship between private creditors and the US government, to identify the circumstances in which the power of Washington may be enlisted in the cause of sovereign debt collection. In the 1980s the Reagan administration resisted demands for overt government involvement, and the bargaining process largely involved the private banks and multilateral financial institutions dealing 'case by case' with individual debtor nations (although no doubt there was orchestration by creditor governments in the background). The next section shows that the result has not been the restorations of voluntary capital flows, but a protracted deadlock in which the development objectives of the debtors habe been sacrificed, and the creditor banks have run out of concessions to offer, while broader American foreign policy interests have been neglected. Sections 4 and 5 consider several facets of this outcome, discussing the underlying structural asymmetries between the two sides, and offering an interpretation of debtor disunity.

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The Historical Background

It is instructive to compare the interaction between today's debtor governments and creditor banks with what took place in earlier eras. Before the First World War it was fairly standard practice (certainly in the Caribbean) for creditor banks to enforce their claims against recalcitrant debtor governments by taking control of the customs house and appropriating the tax revenue until arrears were cleared. To do this the private bankers required military backing, which was periodically made available by their own governments. Problems arose when creditors of more than one nationality induced their respective governments to enforce their claims. The 1904 Roosevelt Corollary to the Monroe Doctrine inaugurated a period of 'Dollar Diplomay' in Latin America in which the US government undertook to collect debts on behalf of European creditors, thereby removing any pretext for extra – continental military intervention.[8] Under this regime debt collecting from theoretically sovereign governments was functionally rather similar to conventional bankruptcy proceedings. The creditor had access to sufficient 'legitimate' means of compulsion to seize the assets of the reneging debtor and to enforce the priority of this claim.

By the time of the Great Depression most debtor governments had secured rather more leeway. The last US Marines were withdrawn from the last Caribbean protectorate in 1934 (under the 'Good Neighbour Policy') and no more would be sent until 1965. In fact this method has not been used for debt collection since 1917 – subsequent military interventions have all been primarily for reasons of national security. Theoretically, ever since the defeat of the Kaiser United States ascendancy in the western hemisphere has been the ultimate guarantee against the use of force for debt collection by any non-American creditor. But British bondholders found they had no redress when most of their Latin American paper went into default in the early 1930s. (This episode marked the virtual eclipse of a British economic and financial pre-eminence that had existed for over a century.) In fact American bondholders fared no better during the 1930s since former Assistant Navy Secretary Franklin Delano Roosevelt was determined not to revert to the methods of dollar diplomacy that he had practised in his youth. Moreover, creditors of all nationalities were also hampered by the legal form in which most debts had been contracted in the interwar period. The only issue for negotiation was whether or not full debt service would be resumed, and all arrears made good, in accordance with the original contract. Representatives of the bondholders were not empowered to vary their terms or to offer any other kind of inducements to comply, unless they could secure the *unanimity* of all claimants. Since many bondholders were private individuals each with a small proportion of the total debt, this requirement posed an insuperable obstacle to renegotiations. Since the slump made it a

[8] Cf. Bruce J. Calder, *The Impact of Intervention: The Dominican Republic during the US Occupation of 1916-24* (Austin, Texas, 1984). The corollary 'sought, in the case of the Dominican republic, to eliminate the danger of another foreign government physically intervening to enforce the demands of its creditor-citizens by having the US act as a collecting agent... to satisfy the claims of foreign bondholders, both European and North American... the Dominican Customs Receivership, headed by an appointee of the President of the United States, would 'collect all customs, keeping 55 per cent of the total revenues to pay off foreign claimants and remitting 45 per cent to the Dominican government" (p.4).

material impossibility for many debtors to meet their obligations in full the result was total impasse. Only one avenue of escape from the deadlock was explored before the Second World War. Since 'busted bonds' (i.e. government bonds on which no interest had been paid or was expected to be paid) could be purchased on the stock market for a small fraction of their nominal value, some debtor governments were tempted to buy in and cancel their debt. But bondholders and the legal establishment in London and New York regarded such practice as little different from outright theft.

The impasse was broken by the Second World War, which elevated the claims of US national security above the mere defence of bondholders property rights. Under the Lend-Lease Act of 1940, and various bilateral negotiations organized from the White House in the early years of the Second War, American creditors were in effect compensated or bought-off by the American taxpayer. This cleared the way for close wartime economic and security co-operation between the United States and the Latin republics. (Note that European creditors were not so fortunate – FDR was not an upholder of the Roosevelt Corollary.) It can, in fact, be argued that from 1940 until 1982 it was the last resort availability of American public funds that provided the ultimate security to Latin America's creditors.[9] If the worst came to the worst Washington would no longer send the Marines to protect the rights of the lenders but it would (either directly or through such multilateral agencies as the IMF) interpose the authority of the United States – backed by public funds or public guarantees – to induce debtor governments to offer concessions, and to promote a constructive collective response from the private creditors. If a debtor government considered the concessions required were too draconian only two means of escape from this system were possible – either by delinking from all conventional financial circuits (as in the case of Haiti under "Papa Doc' after his re-election in 1963), or by an outright reversal of alliances and full integration into the Soviet bloc (a course adopted by Cuba, and perhaps attempted, although with less success, by Chile and Nicaragua). Since the political and economic costs of such a withdrawal were so high, and since participation was generally not too onerous, this system became so well-entrenched it came to be viewed as the natural order of things in the hemisphere. So much so that by the late 1970s most commercial bankers subscribed to the theory that 'sovereign debt' was less risky (and thus required lower margins and less evaluation) than all but the most highly rated corporate debt.

But in private financial markets 'confidence' is a volatile commodity. Bankerly discussions of the risklessness of sovereign debt displayed great sophistication on peripheral matters combined with a cavalier attitude to the central question, namely the reliability of their ultimate source of security. The unspoken assumption went that if anything was seriously wrong the entire western financial system would be at risk, and not just the balance sheet of individual banks. Therefore a collective public remedy would be sure to emerge.

[9] Barbara Stallings reports considerable evidence that in the 1970s many private bankers *perceived* an implicit US government guarantee or 'safety net' for their sovereign lending to Latin America, even though Washington had made no explicit commitments of that kind – other than to endorse the IMF system of stand-by lending with rising levels of conditionality. *Banker to the Third World: US Portfolio Investment in Latin America 1900-86* (Berkeley, 1987), p. 144.

Little attention was paid to the marked erosion of US political and military authority in Latin America since the 1940s; or to the fact that during the 1960s and 1970s sanctions for non-fulfilment of international contractual obligations had gradually eased; or to the significance of the fact that sovereign debt was being made available on a large scale and on relatively easy terms, to a much wider array of borrowers than in the past. In short 'confidence' rested on complacency and forgetfulness. The available remedies against default had lost much of their potency from disuse.

The Logic of the Bargaining Process

'If you owe the bank a thousand pounds you are at their mercy; if you owe a million pounds they are at your mercy.' Five or six digits must be added to this old dictum before it can be applied to Third World debt in the 1980s. Even then it overstates the shift in bargaining power from creditor to debtor. In a traditional banking regime a large individual debtor might turn the tables on his creditors by fleeing the country or otherwise destroying the collateral. By contrast, in August 1982, when the government of Mexico ran out of foreign reserves while owing eighty billion dollars to its bankers, all parties to the transaction could at least feel certain that Mexico would continue to trade with the United States. Thus at least for this debtor there could be no question of withdrawal from the western financial system or the liquidation of the long-term collateral represented by her prospective foreign exchange earnings. This is why Mexico's 'sovereign debt' was rated so highly by the commercial bankers, and also why the crisis was instantly classified as one of temporary illiquidity only. The 'insolvency' of Mexico was assumed to be unthinkable.

We now have almost seven years experience of the bargaining process between the Mexican government and her creditors. (The Mexican experience serves well to illustrate the underlying logic of the relationship. As we shall see below, although some other Latin American debtors may be less tightly integrated into the international financial system, or of less strategic importance to Washington, the essential principles remain the same.) Since both sides know that in some form the relationship is sure to continue there is always some degree of tacit collusion. For example, it is not in the interests of either side to invoke the word 'default'. 'Arrears of payment' only become a formal 'default' if one or other of the parties to the transaction publicly declares so. But debtors have no interest in making any such declaration, which would almost inevitably trigger various forms of retaliation. So long as the money due is not being paid they will be willing to use softer language[10] that keeps open the option of an eventual resumption of payments.

Since 1982 creditor banks have also judged it to be in their interest to avoid or postpone any formal declaration of default. The reason for this is the one indicated by the old dictum. Too many debtors might turn out to be in default on too much debt, inflicting more losses than the balance sheets of even the largest and richest banks could absorb. Since to declare Mexico in default would amount to commercial suicide by most of America's leading banks, they will prefer some less confrontational stance under almost any circumstances.

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10 Compare Mike Faber, *Beware of Debtspeak* (Sussex, 1988).

This was spectacularly true in 1982, and I believe it remains the case even now, despite all the efforts made by the money centre banks to reduce their vulnerability since then. The point to emphasize is that at least the three largest debtors (Brazil, Mexico and Argentina) are individually so important that each on its own could seriously destabilize the US banking system. Moreover the debt crisis is sufficiently systemic and region-wide to raise the possibility of a 'domino effect' if any one of these countries was seen to be 'getting away' with default. This is the reverse of the 'normal' banking relationship, in which each bank expects a small proportion of its debts to go bad, with consequences that will be exemplary for other borrowers, but not devastating to the lender.

So what options are left open to Latin America's creditors if they can neither send the Marines, nor requisition the assets of non-payers, nor accept their losses and walk away from the area of business? They are condemned to a protracted and unsatisfying succession of negotiations, with only a modest range of inducements or punishments at their disposal. The remaining methods of influence fall into three main categories. First, there is praise (or condemnation) for particular debtor governments and for specific political leaders, meted out according to their conduct in negotiations. This is a surprisingly prominent element in the bargaining process even though its efficacy may seem doubtful. (Currently Latin American leaders are more likely to achieve popularity as *bêtes noires* of the bankers than as their proteges.) One reason why praise-blame has figured so prominently is that most Latin American leaders hold a common set of assumptions and liberal values which they share (or aspire to share) with the leaders of the developed capitalist world. Most would go to some lengths to avoid being blamed for damaging the world financial system, or for economic irresponsibility, even if on a narrow calculation of national self-interest there might seem nothing to lose. Praise and approval at the Annual Meeting of the Fund and Bank has been seen as a desirable goal in its own right, and for some it may lead to personal and political advancement, even if the policies being praised are not generally considered successful by the populace at home. There are exception of course (President Garcia of Peru seems to have courted international unpopularity, and so did the late Brazilian Finance Minister Funaro). Moreover this form of bankerly influence tends to wane over time, as the intractability of the issues becomes apparent and 'debt fatigue' sets in.

Second, there is the offer of financial inducements (or sanctions). Obviously this method of influence is closely linked (though not reducible) to the first. Committees of bank creditors (usually in co-ordination with the IMF) have been convened virtually continuously since 1982 to work out the terms and conditions they would attach to debt rescheduling agreements. Setting aside the often intricate details, the essence of all these negotiations is under what conditions the creditors will agree to soften the terms of outstanding debt service arrangements, and how much 'new money' they will add. Compared with the initial terms of the loan, the creditors will regard any concessions as additional costs. The 'financial inducement' they can offer is therefore their willingness to commit themselves to these costs. In principle such inducement is most likely to be offered to those Third World borrowers whose governments are receiving praise for their economic policies. It is most likely to be withheld

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from those whose governments are under criticism. That, as least, is the theory underlying the 'case by case' approach to debt rescheduling.

Over time, however, it has become apparent that the reality is rather different. Some of the best behaved and most highly praised debtor governments may not enjoy much bargaining power. Even Colombia and Venezuela seem recently to have concluded that the effort to behave like exemplary debtors was not worthwhile, considering the poor response from creditor banks. Many commercial bankers seem unwilling or unable to discriminate in favour of the better managed Latin American debtors. Instead they have used the time made available by such stop-gap measures as the 'Baker Plan' to reduce their exposure to Latin American risks of all kinds. Such private creditors thus have less interest than either debtor or creditor governments in 'solving' the debt problem. They will just turn their backs on it.

Not only have 'model' debtors lacked worthwhile rewards, but in some cases 'bad' debtor behaviour has extracted concessions from the creditors – at least in the short run – that might otherwise have been unavailable. Some major debtor governments which seem on the brink of an uncontrollable crisis (perhaps even caused by their own mismanagement) may be in a position to frighten their creditors into otherwise undesirable concessions. Bankers try not to admit this reality (which they call 'moral hazard') but after seven years of debt crisis this evidence is all too plain. A conspicuous example of this latter kind was the Mexican rescue package of August 1982, which precipitated the Third World debt crisis. According to Joseph Kraft, who conducted extensive interviews with policymakers in Washington and Mexico City, the US financial community were completely unresponsive to Mexican warnings and appeals for help before the crisis broke.[11] The only way for the Mexicans to secure sufficiently high level attention was by going over the brink. This element in the bargaining problem has recurred time after time, most notably in the recent past as the debt situation has deteriorated. (Examples include Mexico's near default in June 1986, Brazil's suspension of interest payments in February 1987, and Argentina's apparent use of duress against the IMF in October 1987. The 'Acapulco Pact' of November 1987 can also be viewed in this light.)

An important feature of the creditors' bargaining stance in the 1980s as compared with the preceding forty years, is that the cost of any concessions must be borne directly by the private commercial bankers. Although the international agencies and the US administration have intervened strenuously at times to encourage flexible rescheduling and 'involuntary lending' there has been a great reluctance to back these recommendations with public funds. In the end, of course, western taxpayers will be landed with a substantial proportion of the costs, as commercial bankers make provision for their bad loans which reduce their liability for taxation.[12] But this use of public money confers far less initiative and leadership on the governments of the western countries than if they were directly and visibly committeed to underwriting a 'new deal' for the debtors. The creditors are therefore locked into a much more defensive

11 Joseph Kraft, *The Mexican Rescue* (New York, 1984).

12 In the UK, for example, the 'Big Four' clearing banks took £3 billion in provisions for Third World loans in the first half of 1987, at an estimated cost to the British taxpayer of £850 million. *Financial Times* (London, 5 January 1988).

and reactive stance than was the case for example under the Marshall Plan or the Alliance for Progress.

The third, and in the long term the most prowerful, of the methods of influence available to the creditors is the ability to offer, or to withhold market openness. Here the initiative shifts from the financial institutions to creditor governments and decisions are taken not only in response to the debt crisis but also with other (trade, security, and political) considerations in mind. US policies towards Mexico and the Caribbean offer examples of the use of market access as an inducement to the debtors to co-operate (consider especially the Caribbean Basin Initiative, launched in 1983). But in *South* America restrictions of market access are aggravating the debt crisis, and in part they are being used to pressurize recalcitrant debtors. Thus, for example, Mexico could be 'rewarded' by the United States for its efforts at co-operative debt management with the prospect of a bilateral free trade agreement that would shelter Mexico from prospective US protectionism. Argentina, on the other hand, has found its capacity to export (and therefore to service its debts) severely crippled first by EEC protectionism and then by aggressive US promotion of competitive agricultural exports. Brazil could easily slip into a trade war with the United States, one element of which appears to reflect Washington's frustration o ver Brazil's uncooperative behaviour on debt servicing.

Summing up, the methods of influence available to the creditors seems much weaker than in the past. Those methods most directly available to the financial community seem increasingly ineffective as the debt problem drags on and grows worse. Stronger inducements are in principle available to western governments, but these are governed by other powerful considerations and not just by the requirements of debt management.

Now consider the perspective of the debtors. They need to attract high level attention in the dominant centres of power. They also need to reassure long-suffering domestic opinion that national interests and priorities are not being needlessly sacrificed to the unreasonable demands of foreign bankers. In Latin America there is now a widespread view that unless debtor governments take forceful action on the debt servicing front the home economy will suffer indefinite stagnation and disruption, while a major fraction of domestic savings will be transferred abroad in debt service payments. (The net transfer of resources from Latin America averaged $30 billion per year in 1983/85. It was cut to $24 billion in 1986, and to $17 billion in 1987, but climbed back to $29 billion in 1988. In any case this amounted to 3.5 per cent of regional GNP, or a fifth of its export earnings since 1982. By comparison German reparations payments averaged 2.5 per cent of GNP 1925-32.) The result is that nearly all debtor governments have felt periodically constrained to mount displays of firm resolve. President Sarney's address to the United Nations in September 1985, President de La Madrid's dramatic nationwide television broadcast of February 1986, and President Alfonsin's emotional press conference in November 1987, all provide illustrations of this. However, in each ease the visible results of these displays of resolve have been relatively modest, and the underlying crisis has continued to fester.

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The essential problem for debtor governments is that even when they are tempted to take measure which punish the creditors for their unhelpfulness, the risks of retaliation and self-harm always appears to be too great. This was what finally persuaded President de la Madrid to back off from confrontation with the banks in the middle of 1986 (it was a very finely balanced decision, however). Brazil has not yet produced a clearcut policy either way. Only Peru has chosen outright defiance – initially with some success, but with disastrous consequences over the medium term.

Here it is worth noting that various economic analysts have proposed interpretative frameworks intended to indicate when it is 'rational' for a debtor nation to default on its obligations.[13] However, the results have not been very illuminating. This is partly because the most elegant models seem to require binary choices (namely, either 'unilateral default' or 'unqualified compliance') whereas Third World diplomacy almost invariably involves clouding the issue (for example, 'undeclared arrears' and 'tacitly accepted moratoria'). By the time of President Bush's inauguration the debate had narrowed to a choice between 'voluntary debt reduction' schemes favoured by the creditors, versus the 'generalized debt relief including some element of forgiveness' favoured by the most ambitious of the debtor governments. It is also because in the real world debtor governments rightly consider the consequences of a unilateral default to be extremely unpredictable. The debt situation is rather like a tense and reluctant peace. Each government considering whether to launch a war may be deterred by extreme uncertainty about how all others will react. The likely strategy is then to prepare for war, but to wait for someone else to break the peace. If so, the outcome will be determined more by accident or miscalculation than by any rational calculos of national self-interest. Indeed, too much reliance on such 'economic' models of decision-making could lead the creditors to a dangerous complacency.

In summary then, the debtors are driven to use strong rhetoric against the demands of the creditors, but their implied threats are less than fully credible. Most debtor governments would much prefer to reach a permanent accommodation with the creditors that would settle the issue once and for all, but many commercial bankers may prefer a protracted process of disengagement which gives them time to rebuild their capital and which preserves a united front against the principle of 'forgiveness'. Thus, so long as creditor governments refuse to step in and assume part of the risk borne by the commercial banks both sides seem locked into a frustrating cycle of threats and reconciliations, neither of which overcome the underlying issues of contention. Optimists used to hope that with the passage of time and the recovery of the world economy the intensity of these conflicts would gradually diminish. Less optimistic observers at least assumed that shifts in bargaining strength would occur which would lead to a clear-cut outcome within say five years. But after almost seven years the alternative hypothesis of endemic tension seems more plausible. With the passage of time the intractability of the conflict of interest could become more evident and the prospect of any eventual negotiated resolution may recede from ciew. If so, frustration could well lead some debtors to the adoption of apparently suboptimal strategies – that is, what commentators on the autarchy of the 1930s used to call 'beggar my neighbour' policies, which in fact beggar

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[13] T. Enders and R. Mattione, *Latin America: The Crisis of Debt and Growth* (Washington, DC, 1984) and Anatole Kaletsky, *The Costs of Default* (New York, 1985).

oneself. Several of the existing leaders of Latin America have at some point contemplated such a possibility, only to back away from it. President García of Peru did not back away, but many in his country now wish he had. For this course is in fact a gamble (not really a rational calculation of probabilities) that a desperate act may call forth otherwise unobtainable concessions. Although the experience of the past few years suggests that the gamble will fail, newly elected leaders in some Latin American countries may well come to office pledged to take the risk, and perhaps be completely unaware of where it could lead them.

The Underlying Asymmetry ('They hired the money, didn't they?)

In the liberal model of 'arms length' transactions all agents are formally equal, free to choose between alternative courses of action according to their respective views of self-interest. They accordingly assume full responsibility for the contracts that they make. That is the assumption underlying Calvin Coolidge's celebrated rebuff to the recalcitrant Latin American debtors of the 1920s.

But most Latin American leaders have been raised on the 'patron-client' model of reciprocal exchange, in which typical relationships are hierarchical and mediated through particularistic networks. The clients must accept a partial surrender of autonomy, in return for which the patron accepts a responsibility to protect them in times of adversity. Anglo-Saxon and Latin American perceptions of the debt crisis differ not only because the former are the creditors and the latter are the debtors, but also because (despite an assumed framework of common values) there are also important, if unspoken, social and cultural differences between the two societies.

Certainly if we compare the domestic financial systems of the main Latin American nations with that of the United States, it is clear that they must operate on very different assumptions. (Actually most Latin American find it difficult to believe that liberal individualism provides a truthful account oh how even US institutions actually operate, an understandable scepticism, but not a topic to be explored in this paper.) When the debt crisis broke, for example, it was considered quite natural for the Central Banks in almost all Latin American republics (even in 'Chicago School' Chile) to take over responsibility for the external debt obligations of troubled private enterprises (effectively to 'socialize' bad private debt). Since 1982 attempts have been made to 'nationalize' the domestic banking system in Mexico, El Salvador and Peru, not to mention post-embargo Panama. Even in such financially sophisticated countries as Brazil, no one is really surprised to find that, when the government changes, friends and business associates of the outgoing administration lose their privileged access to the financial system. They may even face severe audits and the early calling-in of loans, whereas credit becomes much more generously available to those well-connected with the new incumbents. With three digit inflation the norm, rather than the exception, in post-1982 Latin America access to good financial intelligence and control over the intermediation of domestic savings is fr more vital to economic survival than in the developed OECD economies.

More generally the idea of equal treatment for all potential clients is not built into the structure of the Latin American financial system. Insted there is actually a multiplicity of specialized banking institutions (one for the trade unions, another for members of the armed forces, another for low income housing, and so on) with overlapping remits and offering differing degrees of 'favouritism'. There is usually also an operating assumption that the Central Bank will be obliged to bail out any subordinate financial intermediaries that run into severe difficulties, at least *unless* there is a political decision to the contrary. (In the United States the presumption is the opposite, although the practice may be rather mixed as the current experience of the savings and loan associations and some of the farm credit institutions indicate. At any rate, in the 1980s American banks have been failing at a rate not seen since the early 1930s. In Latin America on the other hand, more banks than ever have been 'intervened' or nationalized.)

Since this is how the domestic financial system operates in the typical Latin American republic, it is almost inevitable that such experiences will be reflected in popular (and even some elite) assumptions about the international financial system. One such assumption would be that America's most loyal allies (most reliable clients) are entitled to a degree of protection from Washington when the international economy turns sour. Another would be that even if the formal answer from the international community is 'no', surely there must be some particularistic route to special concessions (for example, Silva Herzog's friendship with Paul Volcker, Simonsen's position on the board of Citicorp). If at first these expectations are not confirmed by experience, the inference may be drawn that the crisis has yet to peak. At a later stage the crisis will still elicit the protective intervention that *must* eventually be dispensed by a patron to his distressed clients, for the underlying relationship to be preserved.

In fact the experience of the past seven years suggests that neither the Coolidge approach nor the 'patron-client' model of creditor/debtor relations does full justice to the facts. The myth that all debtors receive formal equality of treatment has been progressively eroded, as when the IMF relaxed its normal criteria to assist Mexico (summer 1986) or when the US government used financial pressure as a means of political discipline in Central America. But so far the limits on favouritism have been extremely narrow, notwithstanding the scale and duration of the debt crisis. The critical sticking point appears to be that neither private nor public international creditors can allow themselves to be seen lending to distressed debtors at less than their own 'cost of funds'. To do so, they maintain, would undermine the entire rationale of commercial banking practice, and would destroy the confidence of their depositors. Only a formal guarantee, or subsidy, backed by taxpayer's funds, would enable them to give ground on this point. But neither Lend-Lease nor the Alliance for Progress were viewed as acceptable precedents in Reagan's America, and indeed the US fiscal crisis almost precluded such remedies. Herein lies the basic asymmetry between the two sides. To some extent it reflects a difference of doctrine, to some extent an inequality of power. But above all it expresses a weakening of US authority in the western hemisphere.

In summary then, the debtors are driven to use strong rhetoric against the demands of the creditors, but their implied threats are less than fully credible.

Despite the 'cost of funds' limit to concessions the creditors are not entirely locked into a stance of Coolidge-like inflexibility. In fact *before* the debt crisis broke the banks were lending so profitably that there was initially considerable scope for concessions. But it seems that the final sticking point was reached in February 1987. Before then a great deal of ingenuity was expended on blurring the limits. But the possibilities for softening the conflict between two clearly opposed positions now seem practically exhausted. Table 1 shows in stylized form the series of concessions that have typically been made as debt rescheduling has proceeded.

TABLE 1. Latin American debt renegotiations

	Margin over LIBOR (%)	Repayment period (years)	Grace period (years)
1982/83	21/4	8	3
1984/85	13/8	12	4
1986/87	7/8	16	6

Source: Derived from Robert Devlin, 'Los Procesos de Reprogramación de la deuda externa latinoamericana 1982-87' (SELA, May 1987).

LIBOR is London Inter-Bank Offer Rate, the lowest cost of funds available to the most credit-worthy banks. If 'margin over LIBOR' fell to zero, banks would be onlending funds at the cheapest rate they themselves could obtain. (In fact only the most credit-worthy banks can borrow at LIBOR, whereas the credit ratings of 12 major North American banks are currently under threat of downgrading because of their heavy exposure to Argentina, Brazilian and Venezuelan debt.) This would leave no surplus for administrative overheads. Even for the largest most credit-worthy and most efficient bank the true 'cost of funds' cannot be far below LIBOR + 7/8 per cent, and that would now typically involve borrowing short-term money to finance a sixteen-year-long commitment. Moreover, Table 1 does not include the 'involuntary lending' which banks have been pressured into undertaking since 1982, often simply so that their creditors can be recorded as current in their interest payments. (Such 'involuntary lending' began with the Mexican rescue of 1982; it has become more difficult to organize since the Brazilian interest moratorium of February 1987.)

In addition to the gradual softening of repayment terms by the private creditors shown in the Table there has also been a softening of the macro-policy conditions required by the public agencies that are also a party to most reschedulings. Thus IMF 'conditionality' has become somewhat more flexible, in part because otherwise it was feared that some major debtors might reach agreements with their commercial creditors bypassing the Fund altogether. Since the 'Baker Initiative' the Fund and Bank have been engaged in a major reshaping of their lending operations to take into account the urgency of the debt crisis. Large increases in capital are envisaged, and other important operational reforms are in prospect. However, as with the commercial banks, there are some major 'sticking points' beyond which these official institutions would begin to undermine their own foundations. Indeed, in the view of many Latin American observers, these institutions seem near to the limits of their own capacity for 'adjustment' to the debt crisis.[14]

One further source of flexibility has been the relaxation of monetary policy that took place during President Reagan's second term, partly in response to the oil price collapse of 1986 and then the stock market slump of October 1987. For a while this permitted a considerable decline in the dollar interest rates payable by mos sovereign debtors, but such relief has not continued into the Bush administration. This policy shift was not, of course, adopted solely or even mainly to grant relief to Third World debtors. But it bought them some time, and it constituted the only form of Northern assistance to the South that could be extended without aid-legislation or other politically impractical initiatives.

At the time of writing this paper it seems that all these methods for easing the financial burdens faced by Third World debtors are nearing their limits, and still the difficulties of debt servicing remain as intractable as ever.

TABLE 2. Secondary market value of Latin American external public debt (% of face value)

	July 1985	Dec. 1986	Dec. 1987	Nov. 1988
Argentina	60	62	35	20
Brazil	75	74	45	40
Chile	65	65	60	55
Colombia	81	80	67	56
Ecuador	65	63	34	13
Mexico	80	54	51	43
Peru	45	16	7	5
Venezuela	81	72	49	40

Source: UN Economic Commission for Latin America and the Caribbean, *Preliminary Overview of the Latin American Economy 1988* (Santiago, Chile, 3 January 1989), Table 21.

Commercial banks have little more to offer in the form of softer rescheduling terms, unless they go below the cost of funds. The resale value of Third World debt has now fallen to a low fraction of its face value (see Table 2), so low that further private bank lending (even of an 'involuntary' variety) becomes a commercial nonsense. A growing number of debtor countries have accumulated such interest arrears with the IMF that they are barred from further borrowing by the Fund under any policy conditions and many others have commited themselves to Fund performance targets that are known to be unrealistic. This is a situation of weakness that can hardly be allowed to continue if the Fund is to remain in business. Monetary relaxation in the developed countries must also be reaching the limits of effectiveness. Fiscal conditions in the North mean that the chances of a large and far-reaching programme of relief and assistance for distressed debtors of the Third World still seem to be highly problematical. Many innovative debt schemes have been canvassed in the course of President Reagan's last year, and a far-reaching review od debt options has been one of the first foreign policy priorities of the incoming Bush

But above all it expresses a weakening of US authority in the western hemisphere.

[14] W.Max Corden lays this bare in 'An International Debt Facility', *IMF Staff Papers*, xxxv, 2 September 1988. The most crucial problem about all such schemes concerns 'the interests of the potential owners or underwriters of the facility' (i.e. the Bank and Fund) because any scheme large enough to ease te overall debt problem would involve 'a large transfer or risk internationally from private banks to the underwriting governments or multilateral institutions' (p. 420).

administration. But the basic difficulty with all these alternatives is that as a continuing business US commercial banks will not voluntarily lend on depositors funds below cost, without some public guarantee that would have to be backed by taxpayers' funds. The prospective Federal budget deficits of the early 1990s and the US constitutional structure present almost insuperable obstacles to such an initiative, even if the administration were in sympathy with this approach, and even if Congressmen were not preoccupied with the cost of bailing out troubled domestic financial institutions, such as the savings and loans banks and the farm credit system.

At the heart of the matter is the fact that since the mid-1980s the United States has become a major debtor nation, and for years to come the US Treasury will be competing with Latin American sovereign debtors for international dollar borrowings. Admittedly many of the schemes under consideration envisage the involvement of Japanese and West European banks and governments, and the use of multilateral agencies such as the IMF and World Bank to supervise the provision of new loans to Latin America. But the basic political difficulty remains – without strong US government involvement these schemes are unlikely to go ahead, both because a Washington guarantee is required to persuade others to assume their share of the risk, and because US foreign policy and security interests (and the Monroe mystique) would be affected if non-American governments were to bypass the United States in her own hemisphere.[15]

Most debtors, on the other hand, believe that on unchanged policies the prospects confronting them are so grave that 'something will have to give'. Naturally they view the problem from a self-interested vantage point, and they also view it through a somewhat different perceptual lens. In practical terms they have to decide whether to continue making the agreed debt service payments (even though this may involve indefinite economic stagnation) in conformity to a system of ideas that they do not wholly share. The underlying asymmetry is only partly a function of the limited bargaining power of the debtors. It also reflects the authority of dominant western economic and financial doctrines. These ideas still hold sway to some extent in most of Latin America, although without the unchallengeable ascendancy they have recently enjoyed in New York and London. It is because these ideas have so far retained most of their international authority that Latin American debtors have displayed only hesitant, sporadic, and half-hearted resistance through seven years of massive negative resource transfers. (Imagine what the response would have been if debtors with identical objective bargaining power had been steeped in Islamic ideas about usury, or Marxis ideas about the exploitative nature of market transaction.) Fortunately for the western creditors, patron-client relationships are non-ideological in character, or to be more precise the client customarily defers to most of the assumptions of his patron.

Moreover the Latin American republics confronting these debt problems also have many other features in common – ties of language, religion, culture, a shared history of political emancipation, and of peripheral 'dependent' development.

15 In January 1989 the Institute for International Finance, a Washington-based organization reflecting the view of the major banks, published *The Way Forward for Middle-Income Countries* hoping to influence the debt policies of the Bush administration. 'The debt problem has gone on too long for the governments of industrialised countries to view it as something that can be owrked out just between the debtor countries and their banks' it argued, calling for creditor governments or the World Bank to guarantee interest on principal, and for the easing of tax rules and banking regulations.

Another feature of patron-client relations which serves to maintain hierarchy is that the patron characteristically keeps his clients divided and in competition with each other for his favour. In fact most patron-client systems undergo periodic tests of strength, whereby a dissatisfied or alienated client probes the resolve of the patron and the loyalty of his other clients. System maintenance therefore requires periodic episodes of assertive leadership, in which the patron disciplines challengers and distributes favours to loyal clients. This model captures the essentials of the 'case-by-case' approach towards Third World debt that has so far predominated in Washington. Of course if the clients manage to negotiate a united stance the underlying asymmetry of power may be shifted. But even after the Cartagena Club and the 'Acapulco Pact' of November 1987,[16] a distinguishing feature of the Latin American response to seven years of 'debt crisis' has been the persistent disunity of the debtors.

The Disunity of the Debtors

An outsider with no knowledge of the customs and traditions of the region would surely conclude on the basis of structural considerations that Latin American debtors were exceptionally well-placed to achieve agreement on some collective strategy of self-defence. The debt crisis struck all countries in the region at the same time; seven years later they are all, without exception, still under the same shadow; there are no clearcut examples of successful escape from the problems besetting the rest. (Chile is often cited, but see Table 2.) Moreover successful debt management is a top priority for all governments in the region. There are no 'cross-cutting cleavages' so pressing as to over-ride the solidarity generated by the common predicament (for example, no regional wars, no acute geopolitical imbalances). Even in Central America, where ideological polarization is most acute, the presidents of the five Central Banks have always maintained a degree of co-operation on the debt issue (and of course since August 1987 the presidents of the five republics have established broader common ground motivated essentially by the need to tackle common economic problems). Moreover the Latin American republics confronting these debt problems also have many other features in common – ties of language, religion, culture, a shared history of political emancipation, and of peripheral 'dependent' development. They are nearly all 'middle income' countries, with similar deficiencies of domestic savings in relation to the investment requirements for 'catch up' growth. (Which is why in the 1970s commercial creditors regarded them all as 'bankable' propositions.) A decade ago they almost all shared a strong preference for 'sovereign borrowing' rather than private foreign investment or equity flotations and they all considered it almost 'natural' to borrow in *dollars*, at floating rates, mainly from US banks.

This is a remarkably constraining list of shared characteristies. Consider the potencial sources of disunity that it excludes. The region contains no cred-

16 There is a lengthy history of joint consultations among Latin American debtor governments with the aim of establishing common ground. The most substantial effort was made by eight civilian elected presidents, who met in Acapulco in November 1987 to propose collective negotiations with the region's creditors on the basis of a halving of the debt service burden. The follow-up meetings a year later had scant progres to report.

"Simpósio Democratizing Economics/88". Agência USP, Jorge Maruta

itor countries (although several Latin American nations are major oil exporters and some are even members of OPEC). There are no 'East Asian NICs' (Hong Kong, Taiwan) whose irrepressible export orientation would undermine debtor unity. Only Cuba and Nicaragua are under US embargo, and even they have accumulated substantial dollar debt with non-US banks. There is no ethnic minority with a political or economic orientation radically different from that of the majority, to sow regional dissension (cf. the Jewish population in the Middle East, the Afrikaner population in South Africa, the Chinese traders of South-East Asia). With the arguable exception of Puerto Rico there is no privileged ally of the dominant creditor power helping to 'divide and rule' the debtors.

Yet this remarkable list of unifying factors has not so far been sufficient to produce much effective co-operation or unity of action among the Latin American debtors. Despite the rhetoric of the 'Cartagena accord' and, the more ambitious and urgent meeting of efected heads of state (in Acapulco in November 1987), there is still little prospect of the 'debtors' cartel' initially feared by many western banks. Why not?[17] United action would require an authoritative source of leadership; individual debtor governments would have to surrender a substantial margin of discretion; there would need to be a tacit 'insurance scheme' to share the risks of possible retaliation; all this implies a degree of forward planning that would be regarded as aggressive by the creditors. Yet the only aim around which the debtors could unite would be to spur their bankers

[17] Compare Guillermo O'Donnell, 'External Debt: Why Don't Our Governments Do The Obvious?' *CEPAL Review*, xxvii (Santiago December 1985).

into negotiating a more generous and far-reaching co-operative solution. They fear that overly aggressive action is more likely to jeopardize such a response than otherwise. Consequently debtor solidarity can only be constructed on a defensive and reactive basis.[18] In large measure the Cartagena and Acapulco rhetoric is designed to mask this underlying weakness.

Let us consider each of these assertions more closely. So far two Latin American Chief Executives have volunteered as leaders of a radical debtors' front. Fidel Castro's offer was of course immediately discounted, given Cuba's exceptional dependence on soviet aid. President García's stance has been greeted with widespread admiration in political assemblies outside Peru, but those who applauded have not had the responsibility for conducting the economic affairs of their own countries. In practice there are only three Presidents who can realistically aspire to lead a united Latin American front. These are the ones responsible for the three largest debtors – Brazil (with a public debt of $115 billion at the end of 1988), Mexico ($97 billion) and just possibly Argentina ($57 billion). Over the past seven years each of these countries has teetered on the brink of default, only to be pulled back at the last moment, at least in part by a sense of isolation. Thus the first flashpoint was Mexico in 1982, the Brazil in 1983, Argentina in 1984, Mexico again in 1986, and finally Brazil once more in 1987. But the three governments never acted in concert. On the contrary they have been systematically out of phase with each other. A collapse in oil prices benefits Brazil, just as it pushes Mexico into crisis. When Argentina was on the brink of measures that might have undermined the credit-worthiness of all Latin America debtors, Mexico actually drew on its own reserves to sponsor a bail-out. (At that time Mexico was being singled out by the western financial establishment as a model debtor.) The most plausible leader of a debtors' front is Brazil because it has both the largest debt, and the most flexible and diversified economy. But in 1987 Brazil's capacity for international leadership was crippled by President Sarney's economic mismanagement, and by the domestic legitimacy crisis. Despite an appearance of unity at Acapulco, these underlying obstacles to the emergence of an authoritative source of leadership for a debtors' front probably remain as intractable as ever. This explains why the Acapulco Pact contained no precise targets, no deadlines for compliance, and no monitoring apparatus other than an annual summit. In early 1989 Venezuela (with a $32 billion external debt) attempted to provide the leadership unavailable from elsewhere, but the essential obstacles remain.

Even if a source of leadership emerges, potential followers will tend to hang back, at least in part from reluctance to surrender any degree of national autonomy. Suppose that the next president of Brazil persuaded all the debtors to join him in a common front limiting the negative net transfer of resources to a maximum of 2 1/2 per cent of GNP in each country. Not all debtors are capable of running trade surpluses as large as that of Brazil; not all have such large internal markets; nor such diversified patterns of trade. Thus other members of the united front might find themselves under severe pressure for pursuing Brazil's lead, long before the crunch came for the Brazilians themselves. The

Consequently debtor solidarity can only be constructed on a defensive and reactive basis.

18 Kuczynski argues knowledgeably that in any case the will is lacking. He mentions 'middle class voting strenght' as an indicator of this, but since he wrote inflation and recession have intensified in many countries, and in 1989 fear of a radicalized electorate has become a major argument for concessions from the creditors.

citizens of each republic would naturallu hold their own government accountable for the national consequences of a more confrontational debt policy. But by agreeing to join a common front each government would be forgoing much of the flexibility needed to mitigate such consequences.

In theory an 'insurance scheme' might meet this objection, but in practice this would be almost impossible to devise or operate. The consequence of confrontation most feared by all debtors is some form of retaliation by their creditors. Individual creditors might seek legal redress (for example, confiscation of assets held in the United States) even though the creditors as a whole had taken no decision in favour of retaliation. Different debtors (and different interests within each debtor nation) face widely differing degrees of exposure to retaliation. The weakest and most exposed could be running very considerable risks. The strongest and least exposed are mos unlikely to underwrite schemes of compensation broad enough to cover the full range of retaliatory possibilities. Even if such promises were made it would be unwise for the most vulnerable debtors to assume that they would be fully and promptly honoured.

The creditors would be unlikely to remain inactive while the debtors undertook the laborious and time-consuming process of negotiating a front, delegating authority to certain leaders, and defining the scope and limits of their mutual commitments. Quite the contrary, we can assume that bankers in general and US government agencies in particular would respond to such a development with an active and co-ordinated strategy. Certainly the Bush administration has decided to include national security and general foreign policy considerations in its debt review, and perhaps for that reason Mexico expects relatively favourable treatment even if other Latin American debtors are disappointed. The 'patron-client' model still shapes international expectations in 1989. The main aim would surely be to scare off the least resolute. Probably there would also be an increased emphasis on the distinction between 'insolvency' and 'illiquidity' ('can't pay' and 'won't pay'). Some concessions might be offered to debtors who, due to what could be classified as 'factors beyond their control', were unable to continue their debt service payments despite displaying every evidence of goodwill ('conciliatory' default). As for those whose inability to pay was a result of deliberately uncooperative policy choices ('aggressive' default) every effort would surely be made to isolate, demoralize, and if necessary punish them.

Conclusion

The debt issue can be considered from many different angles. This article has adopted an international relations perspective, and has dwelt on the logic of the bargaining process, the underlying asymmetry of power between debtors and creditors, and the factors explaining Latin America's failure (so far) to establish a debtor's cartel. It has not attempted to assess the costs or benefits of alternative responses to the debt crisis, and it has deliberately steered away rom consideration of the feasibility, or merits of, alternative policy packages.

Perhaps a 'patron-client' model may be of heuristic value in thinking about this relationship between creditor financial institutions and debtor governments. There are some family resemblances between this approach and the 'dependency' literature that has been so much in vogue in writings about Latin

The 'patron-client' model still shapes international expectations in 1989.

America. However, the dependency school tended to attribute extraordinary importance to the power and influence of multinational corporations, and it downplayed the possibility of discretionary action by national governments. It also ranged almost without limit across many different topics, trying to include everything from consumption patterns to ecological problems within a single (very loose) analytical framework. By contrast this article has been confined to a single major issue which unquestionably reflects severe international equalities of power and divergences of interest. It has emphasized the limiting conditions operating in a specific geographical region at a given historical moment. Multinational corporations with branches in Latin America have been conspicuous by their absence from the analysis (indeed Latin American distrust of the MNCS made an important contribution to the build-up of sovereign debt in the 1970s). The only corporate enterprises that have received consideration here are *external* commercial banks.


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Although it has been suggested that Latin American governments currently seem to possess only a very limited room for manoeuvre in response to the debt crisis, this is a conclusion that must be reached through open-minded historical and comparative analysis, rather than by assumption. The 'patron-client' framework seems to be a helpful interpretative device, but should certainly not be used to imply structural necessity, or to preclude the possibility of constructive change in the direction of a more genuine international community.

One explanation for the limited scale of concessions received by Latin American debtors since 1982 is that they did not press their creditors hard enough, and this article has explored some of the reasons for that. But it has also argued that times of economic crisis expose the last resort character of state guarantees for market processes. Why then have the governments of the creditor nations still not directly stepped in to take over management of the debt crisis which remains manifestly unresolved by the private banking system? Many commercial bankers would now welcome such a development, which since 1984 has been sought with growing insistence by almost all Latin American leaders, and which also commands some prestigious support among exporters and within the Western policy-making establishment. In fact both the Japanese and the French governments have indicated a willingness to adopt this course, which received the general assent of the major industrial powers at the Toronto summit of June 1988 in the case of sub-Saharan Africa, so the real question is not why creditor governments in general hold back, but why Washington in particular is so averse.

Although it has been argued that US national security and foreign policy objectives could be jeopardized by further procrastination over Latin American debt, the US administration has not yet felt pressed by the same sense of imminent crisis as the Latin American leaders experience. In contrast to the Alliance for Progress reaction to the Cuban revolution, and the Lend-Lease reaction to the Second World War, there is not the overriding sense of urgency required to overcome domestic resistance to a costly new Federal commitment. The 'case-by-case' or patron-client approach still may serve Us interests provided the debtors have nowhere else to turn. The alternative of direct government involvement would require both the repudiation of cherished doctrines, and a great mobilization of domestic support to overcome constitutional impediments (not an easy task in the absence of a Pearl Harbor or a cold war). In any case taxpayer involvement would almost inevitably be channelled through some multilareal institutions in which non-American (especially Japanese) capital would have considerable weight. The national security argument is thus two-edged – the risk of Latin American disorder will be weighed against the risk of undermining Monroeism.

Some of these considerations could be classified-as 'structural' explanations for the intractability of the Latin American debt problem, a few of the points could even be re-expressed in the language of dependency theory. On balance however, the interpretation presented in this article privileges the traditions, perceptions, calculations, and bargaining power of national governments, a conventional set of considerations no doubt, but they still seem to possess substantial explanatory power.

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