Can Argentina v. Vulture Funds Bring System Down?

by Cynthia R. Rush

It is with good reason that Federal Reserve Chairman Alan Greenspan found it distasteful to discuss Argentina, when asked about it during his Jan. 13 appearance in Berlin [see article above]. The Fed and its allies are panicked over Argentina's current brawl with creditors holding bonds on which the country defaulted in 2001—many of them the notorious "vulture funds." In the context of the deepening global financial crisis and dollar crash, this battle holds the potential to bring down the whole rotten International Monetary Fund system. Evidence of that panic was seen Jan. 14, when the New York Federal Reserve, the U.S. Treasury, and the New York Clearinghouse Association filed *amicus curiae* briefs on Argentina's behalf in the court of New York Federal judge Thomas Griesa. Bondholders, who reject Argentina's plan to restructure $99 billion in debt with a 75% writedown, are beseeching Griesa to allow them to seize Argentine assets worldwide, including bringing injunctions allowing them to block Argentina's payments to the IMF. The Fund is the only one of the country's creditors to have been faithfully paid in full, to the tune of $12.3 billion, since the December 2001 default.

There should be no "privileged" creditors, bondholders scream, demanding that Griesa make a liberal interpretation of the *pari passu* clause, according to which all creditors have equal standing. This would allow them to start embargoing any Argentine funds sent abroad—that is, to the IMF—as payment for what they say they are owed. Bondholders have already filed a series of legal suits against the Kirchner government, and are awaiting Jan. 31, the date on which Griesa may enforce execution of an October ruling by which vulture fund godfather Kenneth Dart was awarded $724 million on an initial $500 million investment in Argentine bonds, plus unpaid interest. Should Dart be allowed to collect, this would be the signal for a bondholder onslaught to seize Argentine government assets abroad.

But the international implications of any blocking of Argentina's payments to an IMF which is in de facto bankruptcy itself, was more than the Fed and Treasury wanted to contemplate. In its *amicus* brief, the New York Fed warned in urgent tones that, were Argentina prevented from paying multilateral lenders, this would disrupt the banks' payment systems, most particularly the "Fedwire" system of international payments and settlements, involving billions of dollars. "The availability of such injunctions would create uncertainty as to the finality of payments and settlements generally," the New York Fed said, which, in turn, would "threaten the speed, efficiency, reliability, and cost of payment and settlement systems, and could seriously impact financial stability."

There's no missing the message there.

With the Treasury and Fed breathing down his neck, Judge Griesa opted to postpone his interpretation of the *pari passu* clause until Jan. 31, saying he needed more time to analyze the situation. He reportedly denied Argentina's request that bondholders be stopped *pre-emptively* from blocking payments to the IMF; but told plaintiffs they must give 30 days' notice before filing papers to stop payments under the *pari passu* clause.

Combined with President Néstor Kirchner's very vocal attacks on the vulture funds, and on bondholder demands that the 75% writedown included in the restructuring offer be reduced to 35%, these developments aren't likely to comfort the Fed or the Treasury.

Nor has Argentina's relationship with the IMF improved, following the conflict provoked last December by the Fund's deliberate delay of a three-month performance review of the loan agreement signed last September. Tensions reached a new high on Jan. 16, when IMF Deputy Managing Director Anne Krueger provocatively praised the free-market policies imposed by former President Carlos Menem in the 1990s—they gutted the economy and plunged the country into crisis—saying they had produced "significant economic progress."

While Buenos Aires state Governor Felipe Solá said that the "ignorant" Krueger had obviously forgotten to "take her medication," an angry Kirchner charged that "Krueger was one of the people directly responsible for Argentina's indebtedness. . . . With these remarks, [Krueger] is trying to justify the harm these policies did to Argentina. . . . She should come and see in what condition her project left us—a scorched earth." Kirchner vows he will not budge from the original restructuring offer. After foreign bondholders met in Rome Jan. 12 to form the Global Creditors Committee, and threatened to lobby the IMF and G-7 nations to pressure Argentina into making a better offer, Kirchner called them "disrespectful." Those "who indebted the nation are those who say we have to pay more," he charged Jan. 20. "We're finished with the idea of building to pay [debt] abroad, at the expense of the hunger of the Argentine people." Speaking from the World Economic Forum at Davos Jan. 21, Central Bank President Alfonso Prat Gay repeated that creditors "would have to accept big losses."

There is already great worry about what will happen in March, when Argentina is scheduled to make a $3 billion payment to the IMF. Anne Krueger now refuses to confirm the Jan. 28 date set for the IMF board to finally approve the first performance review. And should the Fund continue its provocations, the Kirchner government has made known it has the option not to pay. Whether it would take such a bold step is another question.