

February 6, 2002

Mr. Horst Kohler
Managing Director
International Monetary Fund
700 19th Street NW
Washington, DC 20431

Dear Mr. Kohler:

This letter is in response to a recent proposal by First Deputy Managing Director Anne Krueger on a new approach to sovereign debt restructuring. We applaud the efforts that the IMF has made and is continuing to make in order to strengthen the architecture of the international financial system, particularly the emphasis that the IMF has placed on crisis prevention, increased transparency and voluntary and market-oriented solutions to debt problems. Unfortunately, the proposal advanced by Ms. Krueger would represent a step backward in the area of crisis resolution, because it would threaten legitimate creditor rights and severely interfere with the voluntary and market-based resolution of sovereign financial crises. Indeed, we are concerned that the principal effect of Ms. Krueger's proposal will be to further reduce the flow of private portfolio capital to developing countries, resulting in lower rates of growth and higher levels of poverty in developing countries with consequent spillover effects in the developed world.

Concerning the proposal itself, we would like to comment on several issues. First, we disagree strongly with several of the key assumptions that were used by Ms. Krueger as the basis for her proposal: (1) that there is a collective action problem preventing creditors as a group from reaching agreement on restructuring terms for countries that have an "unsustainable" level of external debt; (2) that IMF assistance to debtor governments has the effect of "bailing out" private creditors; and (3) that the proposed framework offering a debtor country legal protection from creditors would be analogous to domestic bankruptcy procedures.

We believe that the so-called collective action problem is more theoretical than real. Since this problem was first identified, debtor countries such as Russia, Ecuador, Pakistan and Ukraine have successfully been able to restructure all or a substantial portion of their external bonds through the use of exchange offers, which in some cases were accompanied by exit consents to encourage full participation. Experience has shown that so-called rogue creditors have not obstructed these restructurings. Even in the most widely cited (and possibly only) example of "rogue" behavior, a single creditor in fact failed to disrupt Peru's restructuring in 1997 and only collected payment three years later. Accordingly, we believe that the danger of rogue creditors has been highly exaggerated. On the contrary, the more tangible danger may be in the overly aggressive use by debtor countries of exit consents to compel creditor participation in sovereign restructurings.

At the same time it is important to point out that the restructuring process can work only when both sides face appropriate incentives and disincentives. In her paper Ms. Krueger noted the success of 1980's debt rescheduling effort without acknowledging that the success of those efforts were due, in part, to a balance of rights and potential actions that brought both debtors and creditors to the negotiating table and helped to keep them there. We believe that Ms. Krueger's proposal would upset this balance by severely eroding creditors' rights while also possibly giving debtor governments the incentive to seek an officially sanctioned debt restructuring rather than making painful but necessary choices regarding their economic policies.

We also disagree with the argument that private creditors have been bailed out through official loans to developing countries. Far from being "bailed out", private creditors have and undoubtedly will continue to experience substantial losses on their exposure to emerging market sovereign debtors who have experienced payments difficulties. Meanwhile, multilateral and bilateral official creditors, in particular the IMF and the IBRD, have not absorbed comparable losses and have managed to maintain their position at the head of the payments queue.

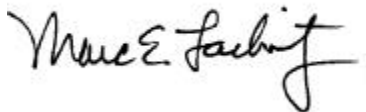
Finally, we disagree strenuously with the notion that the mechanism envisioned by Ms. Krueger could be considered as analogous to a domestic bankruptcy procedure. According to the Krueger proposal, the IMF would effectively act like a bankruptcy court by endorsing a standstill so that it would be able to review the country's proposed economic policies. However, in addition to enforcing creditor standstills and mandating a creditor agreement, in a normal bankruptcy the court is also able to force the debtor to restructure its business and marshal its assets in order to satisfy valid creditor claims. Moreover, creditors have the ability to attach a debtor's assets, which can be used for full or partial recovery of their claims. These types of creditor protections, an integral part of an effective bankruptcy regime, are either not feasible or are severely limited under the Krueger proposal.

Instead of a mechanism to ensure that creditors receive full or partial restitution of their claims, the Krueger proposal implies that creditors will benefit from the adoption of IMF-mandated economic policies in the debtor country. However, severely compromising creditors' rights in exchange for an unenforceable promise by debtor countries to put in place policies that would prevent future payments interruptions is a trade-off that few creditors, with good reason, would accept voluntarily. The history of sovereign defaults, particularly in the past two decades, is filled with similar promises that were not fulfilled. More often than not, IMF targets set for debtor countries have not been met and structural adjustment programs linked to debt relief have lapsed without achieving the needed reforms. In addition, Ms. Krueger proposes that any new debt issued by the borrower would have to have seniority over existing debt, as a means to encourage private lenders to extend credit to the country. Existing creditors, as a result, would see the value of their claims on the borrower further diluted.

An additional concern with the proposal is the inherent conflict of interest that the IMF would face if the proposal were put into effect. The IMF, a principal creditor itself and agent of other official creditors to the troubled debtor, would also be acting as an arbitrator since it would decide when a debt standstill would be officially sanctioned and would in effect oversee the debt restructuring process. This inherent conflict of interest raises substantial concerns throughout the private sector about the legitimacy of the IMF's role as an impartial arbiter under the proposal.

In closing, we would like to stress once again that we believe more can be done to strengthen the architecture of the international financial system, particularly in the area of crisis prevention. Moreover, we strongly believe that the most constructive approach to both crisis prevention and resolution is through enhanced dialogue and cooperation between public and private sector creditors. One important lesson that has been learned over the past few years is that sovereign debt negotiations proceed at a faster pace, with less extraneous distractions, when there is trust and dialogue between the official sector and private creditors. The IMF itself has recognized the importance of improved dialogue between the official sector and private creditors as a means to smooth the restructuring process. In that respect, this proposal represents a step backward since it is clearly prejudicial toward the interests of private sector creditors. IMF support for the Krueger proposal, therefore, could drive a wedge between official and private creditors, weakening the basis for cooperation in the future.

Sincerely,



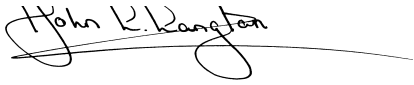
Marc E. Lackritz
President
Securities Industry Association



Michael M. Chamberlin
Executive Director
Emerging Markets Traders Association



Clifford R. Dammers
Secretary General
International Primary Market Association

A handwritten signature in black ink, reading "John L. Langton". The signature is fluid and cursive, with a long horizontal line extending from the end of the name.

John L. Langton
Chief Executive and Secretary General
International Securities Market Association

A handwritten signature in black ink, reading "Micah S. Green". The signature is cursive and compact, with the first name being the most prominent.

Micah S. Green
President
The Bond Market Association