The Case for the Suspension of Payment or Repudiation of Odious Debts

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Since the 19th century, public debt has been used as a weapon of domination and despoilment in Latin America, China, Haiti, Greece, Tunisia, Egypt and numerous other countries. Ultimately, the combination of debt and free trade has been a fundamental factor in the subordination of whole economies since the 19th century. Local ruling classes have joined forces with major foreign financial powers to subject their countries and people to a system of permanent transfer of wealth from local producers to domestic or foreign creditors. As early as the first half of the 19th century, Haiti was used as a test case. Haiti was the first independent black republic, having freed itself from the yoke of France in 1804. However, Paris did not renounce its claims on Haiti, obtaining a princely settlement for the erstwhile slaveholders. The agreements signed in 1825 with the new Haitian rulers created a monumental independence debt on which Haiti was unable to make its payments by 1828, and which in fact took a century to pay off, making any form of real development impossible. Debt was also used to subject Tunisia to France in 1881 and Egypt to the United Kingdom in 1882.[1] This chapter demonstrates that it is entirely possible to repudiate or suspend

1 Toussaint, Éric (2022). Another look at the debt of Tunisia and Egypt in the 19th century and the colonization of those countries by France and Britain , *Committee for the Abolition of Illegitimate Debt* (CADTM), published 29 September 2022. Accessible at: https://www.cadtm.org/Another-look-at-the-debt-of-Tunisia-and-Egypt-in-the-19th-century-and-the

payment of debts that are regarded as illegitimate or odious without any lasting adverse consequences – quite the contrary. The idea that a country that repudiates or suspends payment of a debt will be boycotted by lenders is belied by reality.

Sovereign debt repudiation is an act by a sovereign state that declares debts claimed by its creditors to be void. Sovereign debt cancellation is an act by creditors who wholly or partially waive payment of their debts. The concept of odious debt has been defined in international law. The definition was drafted in the 1920s and published in Paris in 1927 by Alexander Sack,[2] a conservative Russian jurist and former professor of law under the Tsarist Empire in St. Petersburg, who was exiled to Paris after the Russian Revolution. I mention this to show that he was neither a Communist nor a sympathiser with the Soviets or the Bolsheviks, but was actually shocked by the refusal of the Soviets to honour the Tsarist debt. Sack analysed all the sovereign debt disputes he could find, beginning with the French Revolution in 1789, and formulated a doctrine in international law stating that in the event of succession or change of government, previous obligations are transferred to the new regime regardless of the nature of the regime in question – democratic, tyrannical, religious, or people's republic – except where the debt is odious. When debt is incurred against the best interests of the residents of a state, or against the objective interests of the state – and thus in favour of a privileged minority – and the creditors cannot prove that they were unaware of that fact, then such debt can be described as odious. Thus, according to this doctrine, it is the use of the debt that makes it odious or not, void or not. The democratic or undemocratic nature of the regime that incurred it is irrelevant. In this chapter, I will only discuss debt repudiations or suspensions by countries of the Global South. I have reviewed debt repudiations by Northern states (United States, France, Portugal, Soviet Russia, Baltic states, etc.) in other publications.[3]

2 Sack, Alexander N. (1927). *Les Effets des Transformations des États sur leurs Dettes Publiques et Autres Obligations financières*. Paris: Recueil Sirey.

3 Toussaint, Éric (2023). Du Nord au Sud de la planète: Les répudiations de dettes de la fin du XVIII au XXIe siècle. *Committee for the Abolition of Illegitimate Debt*

Mexico, Costa Rica, China, Indonesia and Ecuador Have Emerged Stronger from Their Debt Repudiation Decisions

In my book *The Debt System A History of Sovereign Debts and their Repudiation*, I analysed debt repudiations decided by sovereign states in the South.[4] What follows is a brief selective summary.

It is indeed possible to stand up to creditors, as demonstrated by Mexico under Benito Juarez, who, in 1867, refused to take responsibility for the loans contracted by the regime of Emperor Maximilian from the Société Générale in Paris two years earlier to finance the occupation of Mexico by the French army.[5] In 1914, in the midst of the revolution, when Emiliano Zapata and Pancho Villa were on the offensive, Mexico suspended payment of its foreign debt, which it viewed as illegitimate, repaying only symbolic sums between 1914 and 1942 in a bid to gain time. Between 1934 and 1940, President Lázaro Cárdenas nationalised the oil industry and the railways without compensation, in addition to expropriating more than 18 million hectares of large landholdings and handing them over to indigenous communities. This tenacity paid off: in 1942, the creditors waived approximately 90% of the value of the loans and agreed to small compensation payments for the companies that had been expropriated. Mexico was able to achieve significant economic and social development in the decades running from the 1930s to the 1960s.

We can also cite the case of Costa Rica, where, in 1919, the Congress repudiated the debt contracted by the deposed government of President

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(CADTM), published 12 January 2023. Accessible at: http://www.cadtm.org/Du-Nord-au-Sud-de-la-planete-Les-repudiations-de-dettes-de-la-fin-du-XVIII-au.

4 Toussaint, Éric (2019). The Debt System A History of Sovereign Debts and their Repudiation. Chicago : Haymarket.

5 Toussaint, Éric (2017). Mexico proved that debt can be repudiated. *Committee for the Abolition of Illegitimate Debt* (CADTM), published 24 March 2017. Accessible at: https://www.cadtm.org/Mexico-proved-that-debt-can-be.

Tinoco from the Royal Bank of Canada.[6] Costa Rica's action led to international arbitration in which the Chief Justice of the United States ruled in favour of Costa Rica against the Royal Bank of Canada, which was supported by Great Britain.

Further examples can be cited: China's decision in the wake of the 1949 revolution to repudiate odious debts incurred by the former regime. China finally won creditor lawsuits against it in the United States in the 1980s;[7] In 1956, independent Indonesia decided to repudiate a debt claimed by the Netherlands, its former colonial power.[8] In 1958, at the time of independence, the President of Guinea Conakry, Sékou Touré, refused to shoulder French colonial debts. After the triumph of the Cuban revolution in January 1959, the Cuban government repudiated a series of debts and expropriated large foreign companies, especially American ones. This led to a court case in the United States in which the private creditors were unsuccessful.[9] In 1960, when the former Belgian Congo achieved independence, the government of Patrice Lumumba refused to accept the debts demanded by Belgium and the World Bank. It was not until the consolidation of the dictatorship of Marshal Mobutu that Congo recognised the debts that Belgium had contracted with the World Bank.[10]

Algeria, which became independent in 1962, repudiated debts claimed by France and led a highly successful fight in the United Na-

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6 Ludington, Sarah; Gulati, Mitu & Brophy, Alfred L. (2009). Applied Legal History: Demystifying the Doctrine of Odious Debts. *Theoretical Inquiries in Law* 11, 247–281.

7 King, Jeff (2016). *The Doctrine of Odious Debt in International Law. A Restatement*. Cambridge: Cambridge University Press, 84–85.

8 Ibid., 80f.

9 US Supreme Court (9064). *Banco Nacional de Cuba v. Sabbatino, 376 U.S. 398*. Accessible at: https://supreme.justia.com/cases/federal/us/376/398/.

10 Toussaint, Éric (2014). *The Life and Crimes of an Exemplary Man*. Committee for the Abolition of Illegitimate Debt (CADTM), published 8 May 2014. Accessible at: https://www.cadtm.org/The-Life-and-Crimes-of-an-Exemplary-Man

tions against colonial debts.[11] After the Shah was overthrown in 1979, Iran refused to accept debts incurred by the former regime. Eritrea, upon gaining independence from Ethiopia in 1993, refused to take on the debts that Ethiopia sought to transfer to it.[12] On its independence in 2002, East Timor, a former Portuguese colony that was annexed by Indonesia in 1975 under Suharto's dictatorship, refused to inherit any debts.[13] In 2005, Paraguay successfully repudiated debts claimed by Swiss banks.[14]

In 2008, Ecuador unilaterally suspended payments on a debt which had been found to be illegitimate by an audit commission and obliged its creditors to agree to the cancellation of two-thirds of the debt in suspension of payment.[15]

In all these examples, the countries that took these decisions came out stronger, with the exception of Congo-Leopoldville, whose Prime Minister, Lumumba, was overthrown and subsequently assassinated. Resisting may not guarantee victory, but submitting to creditors does guarantee defeat.

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11 Carton, Anaïs (2022). A sovereign State can refuse the transfer of debts that were contracted in times of subjection. *Committee for the Abolition of Illegitimate Debt* (CADTM), published 23 June 2022. Accessible at: https://www.cadtm.org/A-sovereign-State-can-refuse-the-transfer-of-debts-that-were-contracted-in.

12 King (2016), op. cit., 104–106.

13 Toussaint, Éric (2023). The World Bank A Critical History. London: Pluto

14 Presidencia de la Republica de Paraguay (2005). *Decreto n°6295*, 26 August 2005.

15 Toussaint (2024), Ecuador: Resistance against the policies imposed by the World Bank, the IMF and other creditors between 2007 and 2011, *Committee for the Abolition of Illegitimate Debt* (CADTM), published 16 August 2024, https://www.cadtm.org/Ecuador-Resistance-against-the-policies-imposed-by-the-World-Bank-the-IMF-and. See also: International Monetary Fund (2012). Sovereign Debt Restructurings 1950–2010: Literature Survey, Data and Stylized Facts. *IMF Working Paper*, 78. Accessible at: Sovereign Debt Restructurings 1950–2010: Literature Survey, Data, and Stylized Facts; by Udaibir S. Das, Michael G. Papaioannou, and Christoph Trebesch; IMF Working Paper 12/203; August 1, 2012.

The Arguments of Opponents of Debt Repudiation or Suspension of Debt Payments Are Contradicted by the Facts

Let us consider the arguments of detractors of debt repudiation or suspension of debt payments. According to traditional economic theory, breach of contract has certain negative consequences for debtors. After reneging on their promises and imposing losses on investors, debtors are supposed to find it very difficult to access capital markets and generate new debts. The cost of new borrowing is expected to rise significantly, with a 'stigma effect' on new debt issuance. Some go so far as to say that such debtors will be completely excluded from the debt market, at least for some time. A country that repudiates or suspends payment of its debts will be sanctioned, its rating by international agencies will be deeply downgraded, there will be a reduction in investments and, consequently, a lower growth rate.

These assertions are contradicted by the facts, as shown by renowned economist Joseph Stiglitz. Joseph Stiglitz was awarded the Nobel Prize in Economics in 2001 and chaired President Bill Clinton's Council of Economic Advisers from 1995 to 1997 before becoming Chief Economist and Vice-President of the World Bank from 1997 to 2000. Stiglitz makes a strong case for suspending public debt repayments. In a collective work published in 2010 by Oxford University Press, he argues that Russia in 1998 and Argentina in the 2000s prove that unilateral suspension of debt repayments can be beneficial to countries that implement the measure: 'Both theory and evidence suggest that the threat of a cut-off of credit has probably been exaggerated.'[16]

When a country succeeds in imposing a debt reduction on its creditors and recycles the funds previously earmarked for debt repayment to finance an expansionary fiscal policy, positive results are achieved:

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16 Herman, Barry; Ocampo, José A. & Spiegel, Shari (2019). *Overcoming Developing Country Debt Crises.* Oxford: Oxford University Press. Chapter 2 was written by Stiglitz, Joseph (2019). Sovereign Debt: Notes on Theoretical Frameworks and Policy Analyses, 35–66; quotation from p. 48.

> Under this scenario, the number of local firms that are forced into bankruptcy is lowered, both because of the lower interest rates than if the country had continued to pay its debt[17] and because of the improved overall economic performance of the economy. As the economy strengthens, government tax revenues are increased – again improving the fiscal position of the government. […] All of this means that the government's financial position is stronger going forward, making it more (not less) likely that creditors will be willing to provide finance. […] Empirically, there is little evidence in support of the position that a default leads to an extended period of exclusion from the financial market. Russia was able to borrow again on the financial markets two years after defaulting, based on a unilateral decision without prior consultation with its creditors. […] Thus, in practice, it is apparent that the threat of credit being cutting off appears not to be effective.[18]

According to Joseph Stiglitz, some people believe that one of the central roles of the IMF is to impose the highest possible price on countries that are planning to default, and many countries behave as if they believe in that threat. He believes they are wrong: 'The fact that Argentina did so well after defaulting, even without IMF support (or perhaps because it did not have IMF support), could lead to a change in this belief.'[19]

Stiglitz also clearly blames bankers and other lenders who grant massive loans without seriously checking the creditworthiness of the borrowing countries or, worse, who lend in full knowledge that the risk of default is very high. He adds that since lenders charge high rates to certain countries in light of the risks they take, it is only natural that they should face losses due to debt write-offs. The lenders should use the high interest rates they charge as provisions for potential losses.

17 One of the conditions set by the IMF when it assists a country on the verge of defaulting is to raise local interest rates. If a country escapes the conditions set by the IMF, it can instead lower interest rates to avoid business failures as much as possible.

18 Stiglitz (2019), op. cit., 48–49.

19 Ibid., 49.

He further denounces indiscriminate, 'predatory' lending to debtor countries by bankers. In short, Stiglitz argues that lenders should take responsibility for the risks they take. At the end of his contribution, he considers that countries that are preparing to default or renegotiate for debt relief will need to impose temporary capital controls/exit taxes to discourage capital outflows. He embraces the doctrine of odious debt and argues that it should be cancelled.[20]

The Case of Argentina in the 2010s–2020s

A final thought on the case of Argentina. In his book on the repudiation of the gold clause by the Roosevelt administration and Congress, Sebastian Edwards[21] explains that he decided to study that period of 20th century history when he realised that the Argentine government had justified its attitude towards its creditors in the 2010s by referring to the actions of the United States in 1933–1935.[22] Edwards himself states that he was on the side of the creditors when the US courts ruled in their favour and ordered Argentina to compensate them. What Edwards fails to mention is that Argentina also managed, as Stiglitz points out, to come out ahead by standing up to its private creditors. Its annual growth rate between 2003 and 2008, in the midst of its suspension of payments, was remarkably high despite the fact that the country no longer had access to the financial markets. Although the New York State Court ruled against Argentina in 2013, the Argentine authorities initially resisted the injunction

20 Ibid., 55, 60–61. Joseph Stiglitz has argued in favour of this position on numerous occasions over the past decade. See, in particular, his book Stiglitz, Joseph (2002). *Globalization and Its Discontents*. New York: W.W. Norton.

21 Edwards, Sebastian (2018). *American Default. The Untold Story of FDR, the Supreme Court, and the Battle over Gold*. Princeton, NJ: Princeton University Press.

22 Toussaint, Éric (2023). Debt ceiling: Radio Silence Concerning United States President Franklin Roosevelt's Repudiation of Debts. *Committee for the Abolition of Illegitimate Debt* (CADTM) published 28 May 2023. Accessible at: https://www.cadtm.org/Debt-celling-Radio-Silence-Concerning-United-States-President-Franklin.

of Judge Griesa. It took the election of neoliberal Mauricio Macri to the presidency of Argentina for the country to misguidedly agree to compensate the vulture funds favoured by Judge Griesa. Macri's debt management was disastrous and brought the country to the brink of bankruptcy in 2018.[23] The IMF had to grant Argentina an emergency loan of $45 billion, the largest amount granted by the institution in its history. The loan and Macri's management of the crisis caused him to lose the elections in 2019 and sparked the need for an additional IMF loan of $45 billion in 2022, which was used to pay off the previous loan.[24] This clearly shows that subservience to the markets and the IMF does no good and that it is better to resist creditors while pursuing a different kind of policy.

23 Toussaint, Éric (2019). Argentina: facing another debt crisis. *Committee for the Abolition of Illegitimate Debt* (CADTM), published 18 December 2019. Accessible at: https://www.cadtm.org/Argentina-facing-another-debt-crisis.

24 Toussaint, Éric (2022). The IMF agreement with Argentina is perversely sophisticated. *Committee for the Abolition of Illegitimate Debt* (CADTM), published 15 June 2022. Accessible at: https://www.cadtm.org/Eric-Toussaint-The-IMF-agreement-with-Argentina-is-perversely-sophisticated.