

# EMTA's 20<sup>th</sup> Year—A Look Back to:

## EMTA 1999 to 2007: The EM Debt Trading and Investment Market Matures and Mainstreams

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*[EMTA was formally incorporated in December 1990, in the wake of the so-called LDC Debt Crisis and the pioneering Brady bond debt restructurings by Mexico and Venezuela. To help mark EMTA's 20<sup>th</sup> Anniversary, EMTA's Bulletin this year has featured a series of articles on EMTA's history.*

*The 1<sup>st</sup> Quarter Bulletin reprinted Bruce Wolfson's recollections of the informal meetings of LDC debt traders beginning in 1989 that, with some 'encouragement' from then-FRBNY President Gerald Corrigan, eventually led to EMTA's formation in 1990 as the LDC Debt Traders Association. The 2<sup>nd</sup> Quarter Bulletin reprinted Tom Winslade's article on EMTA's Early Years (1992 and 1993), when it emerged as an independent trade association with a growing agenda of activities. The 3<sup>rd</sup> Quarter Bulletin reprinted Michael Chamberlin's perspective on the evolution of the EM debt trading and investment markets and the growth and diversification of EMTA's activities during the period 1994 through the auspicious year of 1998.*

*This series continues in this 4<sup>th</sup> Quarter with Michael Chamberlin's reflections on the development of EMTA, and the market that it represents, following the Asian crisis and Russian debacle of 1997/98 up until the first signs of the mortgage crisis and global market slowdown in 2007. Formerly a Partner at Shearman & Sterling with a law practice split between public and private sector debt restructurings and capital market transactions in Latin America, Michael Chamberlin led Shearman & Sterling's representation of the international banking community in Mexico's Brady bond debt restructuring and worked on many financings, refinancings and debt swaps in the 1980's and early 1990's, before becoming EMTA's Executive Director at the beginning of 1994.]*

*The views expressed in this series of articles are personal views only, and do not represent official EMTA views or necessarily reflect the views of any of its member firms.*

At the time, the Asian financial crisis and Russian meltdown in August 1998 resulted in a big setback for the EM debt trading and investment industry. Asset values and debt trading volumes plummeted, and investor confidence in the Emerging Markets fell considerably. Among other things, these events changed EMTA's priorities, resulting in several important new projects, greater emphasis on certain existing ones, and the postponement of several others. As always, however, setbacks lead to new opportunities, and from these events soon came a gradual and strong recovery of the EM debt markets that, supported by a long period of low interest rates and continuing economic and financial reforms and reserves accumulation in many EM countries, continued for nearly a decade. The EM debt markets grew, matured and prospered, and the overall period from 1999 through 2007, despite a shock or two, was generally characterized by a strengthening of many EM economies and a steady mainstreaming of the EM debt markets into the broader capital marketplace. With this mainstreaming came a much broader class of new investors in the EM debt markets and debate about the adequacy of the architecture for resolving financial crises in the Emerging Markets.

During this time, EMTA diversified its activities to keep pace with the evolution of the marketplace, incorporated a new class of market participants into its membership—the EM buy-side—and added a variety of investor-oriented activities to its more traditional sell-side agenda.

Asia's Financial Crisis, Russia's Devaluation and Default and their Aftermath. The 1997 Asian financial crisis, which was largely a local markets crisis that was fairly quickly resolved, pointed out the need for the EM financial community to pay more attention to potential disruptions in the foreign exchange markets. Shortly thereafter, EMTA began collaborating with the Foreign Exchange Committee of the FRBNY (the FXC) and the International Swaps & Derivatives Association (ISDA), initially to set priorities and undertake specific FX-related projects in several Latin American and Eastern European currencies, with one goal being to improve the local legal environments for netting. An early project to develop standard definitions and confirmation forms for documenting non-deliverable forward transactions (NDF's) in various EM currencies evolved into a broader effort to revise ISDA's 1992 FX and Currency Option Definitions. The most significant new concepts in the revision were the inclusion of Disruption Events and Disruption Fallbacks, which permitted counterparties to allocate certain event risks on the trade date by providing alternative means of settling transactions in the event of a market disruption, such as occurred in various Asian countries in 1997. These revisions eventually became the 1998 FX and Currency Option Definitions, which provided the market with an architecture for documenting various transactions in EM currencies. Among other things, the 1998 Definitions, which were finalized and published late in the first quarter of 1998, created a common vocabulary for addressing market disruptions, which later enabled market participants to begin standardizing documentation for, and

reduce a growing backlog in the settlement of, forward trading in various non-deliverable currencies.

In the second half of 1998, the markets (and EMTA) were forced to focus a lot of attention on Russia, which had only recently (in December 1997) succeeded in completing a massive restructuring of US\$ 28 billion in defaulted VEB loans. Speaking at EMTA's 1997 Annual Meeting just a week after the closing, Mikhail Kasyanov, Russia's Deputy Finance Minister, noted that it would put Russia's relationship with the international financial community "on a new footing" and "pave the way for investor confidence" in Russia.

As it turned out, the new footing lasted only a few months, until August 1998, when Russia was forced to devalue the Ruble and declare a 90-day moratorium on its indebtedness. Responding to the crisis, EMTA's experience in standardizing NDF language for market disruptions led to a joint project with the Chicago Mercantile Exchange (CME) to develop a back-up survey mechanism for valuing the Ruble/USD FX rate (the CME/EMTA Rate), which soon became the primary settlement rate for the market and provided a model for similar back-up mechanisms for other EM currencies.

On August 28, shortly after the suspension of spot auction currency trading on the Moscow Interbank Currency Exchange (MICEX), EMTA and CME began publishing the daily CME/EMTA Rate as a back-up valuation for the settlement of the CME's Ruble futures contract and for use by market participants as the basis for valuing their NDF's. Developing this new rate required extensive consultation with and among market participants, as well as daily surveys of major international and Russian banks active in the Russian interbank currency market. EMTA provided the forum for these consultations, and the resulting CME/EMTA Rate was quickly built into the 1998 Definitions and became widely used.

Aside from contagion that resulted in freefalling asset prices for most EM debt assets, the most immediate effect of the 1997/98 crises was a sharp fall in EM debt trading volumes, which had peaked in the first and fourth quarters of 1997. After increasing rapidly to US\$ 5.3 trillion in 1996 (up from US\$ 2.378 trillion in 1995!), trading volumes topped off at nearly US\$ 6 trillion in 1998. Trading activity then dipped somewhat in the first three quarters of 1998, before sharply falling in the fourth quarter to levels not seen since 1994 and early 1995. Overall trading volumes for 1998 dropped to US\$ 4.2 trillion, and eventually fell much further in 1999 to US\$ 2.185 trillion, before recovering somewhat in 2000 to nearly US\$ 2.9 trillion.

The Russian default also called into question, as if the Asian debt crisis had not already, the assumption that local market instruments issued by sovereigns were somehow immune from default and restructuring because they were not subject to transfer risk.

In addition to the obvious market disruptions, which spread from Asia and Russia into LatAm and other EM assets, the Russian meltdown directly led to the postponement or curtailment of a number of EMTA projects, particularly those relating to making the trading of Restructured VEB Loans, so-called Min-Fin Bonds, and Russian equities more efficient. In addition, the resulting decline in overall trading activity, and contraction in the size and scope of the EM trading industry, led eventually to EMTA's scaling back its local markets agenda and staffing considerably.

EMCC. Most of EMTA's projects throughout the early to mid-1990's were oriented toward building EM debt trading infrastructure, in the form of standardized documentation, market practices and systems designed to make the global EM debt trading markets more efficient or more secure. These projects were normally initiated at the request of the larger sellside firms, and included the Match-EM automated trade confirmation and matching system, as well as the Emerging Markets Clearing Corporation (EMCC), which was launched in April 1998 and whose origins and early history were described in "EMTA 1994-98: The Golden Age of EM Debt Trading?".

As originally conceived and operated, EMCC was, in effect, a joint venture among EMTA, the National Securities Clearing Corporation (NSCC, a predecessor to the Depository Trust & Clearing Corporation (DTCC)) and the International Securities Market Association (ISMA, predecessor to the International Capital Market Association—ICMA). EMCC was developed by the EM debt trading industry and formed as a stand-alone clearing corporation, subject to regulation by the US Securities and Exchange Commission, and owned primarily by leading market participants and with its own board of directors, while operated and managed as part of the NSCC (later DTCC) family of clearing corporations. In forming EMCC, the EM debt trading industry's principal goal was to support screen-based trading by reducing counterparty and settlement risk and improving certain operating efficiencies.

From the outset, EMCC's trade matching and settlement rates were consistently high, with over 90% of trades successfully matched and assumed by EMCC on trade date and settled on T+3 (in addition, individual firm positions were netted, with the resulting net positions collateralized). Beginning with ten market participants, and clearing only Brady bonds, by 2000 EMCC had grown to include 21 market participants clearing 319 eligible securities, including both Brady bonds and a wide range of EM sovereign Eurobonds. During this time, EMCC established a pair-off capability and a Y2K contingency plan and helped the industry to navigate through the temporary surge in trading volumes (accompanied by extreme price volatility) that occurred in the late Summer of 1998 and Daiwa's 1999 exit from the EM debt clearing business.

Although EMCC reached critical mass in 1999, served most of the major dealer firms and was profitable as a stand-alone affiliated clearing corporation, DTCC concluded by

2001 that it was necessary to start integrating its operations and management more closely with DTCC's other fixed-income clearing corporations as part of a broader consolidation of DTCC's family of clearing corporations intended to take better advantage of economies of scale and other synergies. Despite some misgivings within EMTA about the wisdom of this based upon the loss of independence and EM industry ownership and control, this consolidation was approved by the EMCC and DTCC Boards and became effective at the end of 2001. Concerned about losing EM focus and momentum, as a member of the EMCC Board of Directors I spoke out against including EMCC in the overall consolidation and ultimately abstained from the final vote to proceed.

DTCC continued to own and operate EMCC for another several years before deciding that EMCC was not financially viable, due in large part by the failure to expand its membership beyond the core group of major dealers. One of the problems faced by DTCC in maintaining EMCC's viability was the lack of EM input into EMCC's decision-making process, natural fall-out from DTCC's decision to take over EMCC and disband its Board and EM advisory bodies. Intensive efforts by an EMTA working group to persuade DTCC to keep EMCC operating (or, alternatively, to locate another EM clearing provider) were ultimately not successful, and EMCC was shut down by DTCC effective March 31, 2005. Thereafter, trades have been submitted for bilateral settlement by individual dealers, normally against a private clearing firm acting on behalf of one or more of the interdealer brokers (IDB's) who operate the screens through which most of the interdealer market trading is conducted.

When it became clear that EMCC would inevitably be shut down by DTCC, the EMTA working group concentrated its efforts on finding a replacement provider of EM clearing services. Following an extensive beauty contest, LCH.Clearnet was selected to build and operate the replacement clearing facility offshore, but due to a combination of circumstances, the replacement was never implemented.

At the time (early to mid-2005), most of the IDB screens were cleared by an affiliate of REFCO, and LCH.Clearnet's efforts to develop its EM clearing product were delayed, in part as a result of its inability to reach satisfactory collateral arrangements with REFCO. Due to subsequent credit problems at REFCO, the IDB's replaced REFCO as their clearing firm later that Fall with more creditworthy firms. The effect of the REFCO situation on the business case for the LCH.Clearnet EM clearing entity presented an interesting question. Although REFCO's credit difficulties tended to support the need for mutualizing and collateralizing EM clearing risk through an industry utility (such as an EMCC or the proposed LCH.Clearnet entity), rather than concentrating risk in a private entity, the substantially improved creditworthiness of the new private clearing arrangements, and the speed and ease with which they were implemented, ultimately persuaded many dealer firms that the industry utility was no longer worth its expense

and effort. As a result, the LCH.Clearnet proposal eventually lost industry support and was abandoned.

To this day, the vast majority of interdealer trading in EM fixed income instruments is conducted through the interdealer broker screens, and trades are matched and settled through Euroclear, Clearstream or DTC against one or more private clearing firms acting on behalf of the IDB's as aforesaid. Although this process has worked well enough, obviously there is no assurance that some market or credit events will not occur in the future that could affect the private clearing firms or otherwise disrupt the normal settlement process. With the demise of EMCC, the dealer community assumed a permanent short-term (one or two days) increase in broker counterparty risk, as well as greater eventual clearing risk in private clearing firms.

During its short life, EMCC served the EM debt trading community well by bringing much greater administrative efficiency to the settlement of interdealer bond trades and by reducing counterparty and related systemic risk, particularly during times of real and potential market crisis (notably, August 1998). Perhaps even more importantly, EMCC brought cohesion to the discussions and arrangements between the dealers, the IDB's and the private clearing firms. Unfortunately, some of the expected benefits of EMCC (as well as anticipated economies) were never fully realized, and ultimately EMCC was not successful or long-lived because of participation by less than all of the major dealer firms and a perception that its benefits, while real, could not be amortized over a sufficiently high volume of trading and therefore were simply not worth their out-of-pocket running costs.

Ecuador Brady Bonds, the Burdensharing Debate, and Investor Rights and a Changing EMTA Agenda. Inherent in the mainstreaming of the EM trading markets and asset class was a broader distribution of EM debt instruments throughout the investment community, which had some policy implications for the industry and for EMTA.

One of the policy goals of the Brady plan was to take the concentration of EM credit risk within the banking system and distribute it more broadly throughout the financial system. The various Brady restructurings largely accomplished this goal by the mid-1990's, creating a new class of EM creditors, the EM buy-side, and giving EM countries greater access to new sources of capital. Despite the maturing and mainstreaming of the EM asset class, occasional financial crises continued to occur (notably in Russia in 1998, Ecuador in 1999 and Argentina in 2001), and the broader distribution of EM credit risk, coupled with a reduced official sector appetite for offering bail-out packages to EM countries in economic and financial distress, led policymakers to conclude that they had no alternative but to "bail-in" the private sector by encouraging EM debt issuers to get the EM buy-side to participate in crisis resolution by restructuring their bonds. As one can imagine, this was not necessarily what the EM buy-side expected from their EM

bond investments, and it led to considerable discussions about the adequacy of the EM bond restructuring “architecture”.

Key to the implementation of the Brady plan’s exchange of bank loans for more marketable Brady bonds was that the new Brady bond instruments would represent a permanent reduction in the debt and debt service levels for the issuing debtor countries. As a result, the two most prevalent forms of Brady bonds were Discount bonds issued in a face amount substantially discounted from the principal amount of the loans exchanged therefor (and bearing interest at a floating market rate, usually of 13/16ths over LIBOR) and Par bonds issued without such a discount but bearing interest at a concessionary fixed rate. These discount rates for Discount bonds and concessionary fixed interest rates for Par bonds were heavily negotiated with the bank advisory committees in part in reliance upon an “exit undertaking” included in the bond documentation stating to the effect that the Discount and Par bonds would never be subject to restructuring. As a practical matter, of course, these exit undertakings added little to the explicit promise to pay already included in the bonds, but they nevertheless were intended to represent a moral undertaking on the part of the obligor that it would meet its payment obligations under the Brady bonds as they became due.

Throughout the 1980’s and early 1990’s, bonds were traditionally considered ‘excluded debt’ for purposes of the many country debt restructurings, along with many other debt categories (such as project financings, other secured financings, interbank lines and trade debt) that were considered de minimis, too important to discourage or too difficult to restructure. In some cases, categories of debt were excluded from restructuring for the simple reason that there was a consensus among debtors, creditors and the official sector that the providers of such debt should not be ‘punished’, but rather encouraged to continue providing such credits—in short, that it would be counter-productive to try to restructure them because the inevitable result would be for countries to lose access to them as a source of financing.

As bond indebtedness replaced bank loans as the leading source of country financing for many countries, and creditor governments felt (or manufactured) greater taxpayer pressure to avoid moral hazard and “bailing out” private creditors, the official sector began to emphasize (in what appeared to be a coordinated series of IMF, G7, G10, G22 and US Treasury statements and reports) the need for private sector bondholders to share the burden for resolving sovereign financial crises in the Emerging Markets. Concerns in the bond marketplace about this change in official sector policy increased in early 1999 following various official sector statements about the need for holders of Russian, Romanian and Pakistani bonds to grant debt relief. In response to concerns that debtor countries were being pressured to restructure their outstanding bonds, EMTA issued a position paper in April 1999 that emphasized the following points:

- (1) Greater effort should be made by the official sector to encourage more market-oriented approaches to private sector burden-sharing, as forced rescheduling of Eurobonds was likely to make it all the more difficult for the private sector to contribute resources in support of EM countries.
- (2) Forcing Eurobond investors into involuntary rescheduling would raise legal and practical difficulties that would likely lead to litigation and the loss of access to the bond markets, as well as to increased borrowing costs for all EM countries.
- (3) The treatment of sovereign Eurobonds should be left for countries to determine on a case-by-basis and the doctrine of comparable treatment should not be applied rigidly.
- (4) Radical changes in bond documentation (such as the inclusion of sharing clauses or substantial reductions in voting requirements) would lead to higher borrowing costs and possible tiering of the bond markets, while more modest changes (such as reducing voting requirements to 95% or so) might be perceived as having advantages for both issuers and investors.

While there were indications that this message (as well as similar ones from other trade groups) was helpful in moderating some official sector policies, these and similar issues regarding creditor's rights and the restructuring of bonds continued to feature prominently in EMTA's agenda for much of the following decade.

More tangible and immediate concerns about official sector policies toward bondholders surfaced in August 1999 when Ecuador announced that it would be deferring \$96 million in interest payments on its \$6 billion outstanding face amount of Brady bonds, which had been issued in 1994 in a debt exchange that had granted Ecuador debt relief of about 45%. At the same time, Ecuador announced that it would be proposing a restructuring of its Brady bonds using 'market mechanisms' (so much for Ecuador's exit undertaking, and it is important to note that at the same time Brazil and Mexico were in the process of retiring their Brady bonds). In addition to triggering a lengthy discussion about how these bonds would trade and settle, Ecuador's announcement suggested to some market commentators that burden-sharing was being unfairly targeted at Brady bondholders, and not spread across all classes of Ecuador's creditors. In a notable research note, Michael Gavin of UBS Warburg referred to this as "burden-shifting", noting that what was most significant was not the default itself (which had long since been anticipated by the market), but how it was being handled. Among other things, Gavin expressed concerns about the implications of a seemingly arbitrary situation where Brady bondholders were apparently being asked to restructure, with little or no bondholder input, outside of a comprehensive restructuring plan supported by official sector debt relief and an IMF-approved reform program.

In view of the importance of Brady bonds to the overall EM debt trading and investment marketplace, Ecuador's announcement pushed EMTA's agenda further into advocating



policies on behalf of creditor's rights. In late September, EMTA released a position paper (reinforced by a speech given at the Council of the Americas on December 7, 1999 entitled "Ecuador's Default: Burden-Sharing and the Future of Brady Bonds") on the Ecuador restructure asking whether burden-sharing was being pushed too far, and making the following points:

- (1) Dishonoring the exit undertaking in the bonds and requiring holders to give debt relief beyond the 45-55% previously granted, on top of the market losses already incurred, would create a precedent that would make future debt restructurings for Ecuador and other countries more difficult.
- (2) Targeting the Brady bonds violated sound work-out principles inasmuch as the lack of a comprehensive plan to address Ecuador's entire debt profile represented a piecemeal approach that was likely to jeopardize the prospects for Ecuador's eventual financial recovery.
- (3) Targeting the Brady bonds did not address moral hazard because the Brady bonds represented previously restructured bank loans and not new extensions of credit.
- (4) Targeting the Brady bonds was not comparable treatment to any debt relief granted or to be granted by official creditors.

In addition, EMTA's paper articulated principles for clarifying and legitimizing the concept of burden-sharing, including

- (1) The official sector should make greater efforts to hold debtor countries accountable for steadfastly pursuing economic reform programs and policies that enable them to meet their payment obligations.
- (2) The specifics of burden-sharing should only be developed and applied to the circumstances of individual debtor countries on a case-by-case basis, but such case-by-case approach must be guided by clearer and more consistent principles, including that all financial instruments and sources of financing should be considered subject to burden-sharing, though possibly on differing bases, depending on consideration of the importance of that funding source and the likely effect that burden-sharing would have on future access.
- (3) Proposals to make bonds easier to restructure must not undermine the legal responsibility of debtors to meet their payment obligations or unduly interfere with the delicate balance that exists between the mutual rights and responsibilities of sovereign debtors and their creditors.

These principles have now guided EMTA's agenda to advocate policies on behalf of the EM asset class for over a decade. EMTA consistently counseled that the value of bonds in the market depended on a perception shared among the issuer and investors that the bonds would be performed in accordance with their terms, and warned of the moral

hazard that making bonds too easy to restructure would make it more likely that payment obligations would not be met, but instead would be restructured. On the contrary, bond restructurings should be viewed as a last resort only, because the likely consequence, loss of market access, was so severe.

The Keynote Address at EMTA's 1998 Annual Meeting had been given by former US Secretary of the Treasury Nicholas F. Brady, who noted that there had been "too much talk about financial architecture" and that what was needed was "somebody becoming operational". In October 1999, Ecuador asked EMTA to sponsor a series of meetings (not as a negotiator, but to facilitate and provide logistical support for them) between representatives of the government and a group of its bondholders to discuss Ecuador's economic and financial situation and to obtain bondholder input on the possible terms of an exchange offer to restructure Ecuador's debt profile. Referring to Mr Brady's remarks, I opened the first meeting by noting that it was encouraging to see that Ecuador and its bondholders were getting "operational". Although EMTA hosted and distributed materials in connection with several of such meetings, the sessions proved contentious and not particularly fruitful, and by year-end the effort was postponed (and eventually abandoned) after Ecuador's economic and political situation worsened and its discussions with the IMF stalled.

To promote further dialogue between the official and private sectors, EMTA's 1999 Annual Meeting featured keynote remarks by Stanley Fischer, First Deputy Managing Director of the IMF, and Timothy Geithner, then Under Secretary for International Affairs at the US Treasury. Mr Fischer's remarks specifically addressed EMTA's policy paper (Is Burden-Sharing Being Pushed Too Far?), reviewing the Romania, Ukraine, Ecuador and Pakistan case histories, and noting that the official sector was "in the process of drawing lessons from the experience" and that the official and private sectors "surely have a common interest in many aspects of reform ... of the international financial architecture". Speaking of Russia (where a far larger amount of debt was in default), he noted that "moral hazard exists, and for a clear example of the dangers that it poses, look no further than Russia". Many investors had thought that Russia was "too big to fail", and "the IMF does not have enough money to ensure that countries can always service their debts". Mr Geithner's remarks focused on three major challenges for the international financial community: (1) how to reduce the vulnerability of EM economies to risks, (2) how to create a system of more stable flows to the Emerging Markets and (3) how to strengthen the capacity to catalyze market-based solutions to financial crises. He ended with the prescient observation that "Probably the most important lesson of the last decade [ie, 1990-99] is that governments, in Emerging Market economies in particular, need to plan for the worst...".

Of course, as much later events demonstrated, many Emerging Markets countries took this lesson to heart, and their continued reform efforts, and reserves accumulation (as

well as, in some cases, the attainment of investment grade debt ratings), through the succeeding years 1999-2007 enabled them to weather the global recession of 2008-09 surprisingly well.

If the years 1997 and 1998 were filled with pessimism, crises and default, things started looking up in 2000, as several debtor countries were able to start putting their defaults behind them, Brazil successfully completed a large voluntary exchange offer (retiring many of its Brady bonds) and investors previously discouraged by the Asian and Russian debacles were slowly attracted back into the EM asset class. Early in the year 2000, Russia and its London Club Advisory Committee pleasantly surprised most market participants by announcing proposed terms for restructuring US\$ 31.8 billion principal amount of its defaulted Restructured Prin and IAN debt. The restructuring was successfully completed in the third quarter in what was largely heralded as a major step in the normalization of Russia's relations with the global financial community. Shortly after Russia's restructuring terms were announced, Moody's gave the markets another piece of good news by upgrading Mexico's foreign currency debt to investment-grade status (ten years after its historic Brady plan restructuring and only five years after the so-called Tequila crisis and subsequent rescue package).

Of somewhat lesser importance, but nevertheless significant in several respects, at mid-year Ecuador also announced, and later completed, its exchange offer to restructure its Brady bonds and Eurobonds. As in the case of Russia, EMTA prepared when-issued confirmation forms and recommended market practices in connection with the new bonds issued, but Ecuador's restructuring was not as successful as Russia's in normalizing its relations with the international financial community. To paraphrase an EMTA buy-side director, the result wasn't too bad (the incremental debt relief was about 30%), but the "process stunk".

In a development that seemed relatively minor at the time, but which had lasting significance, Peru delayed an interest payment due on its Brady bonds in early September 2000 as a result of enforcement actions brought against it in multiple jurisdictions by a prominent non-bank creditor that had opted not to participate in Peru's 1996-97 Brady plan restructuring and instead had obtained federal court judgments in the Southern District of New York (Elliott Associates v Peru). After a delay of nearly a month (during which EMTA issued a somewhat long-winded explanation of why it was not recommending that trading of Peru's Brady bonds be taken "flat" unless the non-payment continued beyond a 30-day grace period), Peru and its "hold-out" creditor settled their dispute with a reported payment of US\$ 58 million, thus enabling the interest payment on the Brady bonds to be made. The dispute, and particularly its resolution, was highly controversial at the time, and later became somewhat of a cause célèbre used by many in the official sector, and by the debt forgiveness lobby, as

justification for pursuing changes in the international financial architecture to make EM debt easier to restructure.

Largely as a result of these developments (and also due to industry consolidation and declining trading volumes caused by the Asian, Russian and related debt crises that led to a decrease in EMTA's sellside membership), EMTA re-examined its mission and agenda in 1999 and early 2000, and at mid-year 2000 added five new buy-side directors to EMTA's Board of Directors (bringing the total number of buy-side firms represented on EMTA's Board to seven (out of 24)). An additional two buy-side directors were added to EMTA's Board in early 2001. In addition, investor frustration with Ecuador's restructuring process also led to the formation in late 2000 of the Emerging Markets Creditors Association by eight large EM buy-side firms (who, among other things, apparently believed that EMTA's traditional sellside orientation precluded it from putting bondholder interests first).

The addition of these new buy-side directors to EMTA's Board was soon accompanied by changes in EMTA's official name (from the Emerging Markets Traders Association to simply EMTA), and in EMTA's mission statement and agenda. Added to EMTA's traditional mission of working to make the trading markets more fair, efficient and transparent, was the effort to build greater confidence in the EM asset class by promoting investor rights, and much of EMTA's work over the next few years was focused on this new, more buy-side-oriented mission, including a partially successful effort in late 2000 and early 2001 to make the workings of the Paris Club more transparent, an analysis of the permissible scope of exit consents (At the Frontier of Exit Consents) and repeated efforts (alone and in collaboration with other trade groups) to influence and moderate the official sector's proposals to reform the sovereign debt restructuring process.

As a practical matter, these changes reflected a realization that, with Eurobonds (and then local instruments) rapidly replacing Brady bonds as the most heavily traded debt instruments and EMTA's involvement with EMCC decreasing, much of EMTA's sellside work in the fixed income area had been more or less successfully completed, the investment community had diversified, matured and grown well beyond EMTA's traditional sellside constituency, that the Board needed to be opened up to a wider group of market participants, and that more staff time needed to be dedicated to investor interests. While the name change was largely symbolic, what it symbolized was significant—an EM debt marketplace dominated by traders and their interests was well on its way to developing into a broader trading and investment community. EMTA needed to evolve with its marketplace, and fortunately we recognized that and started the necessary process in motion.

Not that the process was linear, or without some challenges. At the time, re-orienting EMTA and its Board from representing almost solely sellside interests to representing both sellside and buy-side interests encountered some initial resistance from several sellside firms, who felt that the potential conflicts would be too great. After all, recent experience in the derivatives area tended to suggest that very significant issues separating the sellside and the buy-side might be too contentious and difficult to bridge. At the time, I felt that the consensus approach that had consistently guided EMTA, as well as the constant and ongoing experiences in handling trading issues involving the sometimes conflicting interests of buyers and sellers, would give us the tools to navigate through the potential conflicts that representing both the sellside and buy-side might raise. In addition, I was confident that my various experiences as a lawyer representing investment banks, commercial bank lenders and bank advisory committees were good background for this kind of challenging work.

Over the intervening years, various conflicts did arise from time to time, and it was clear that EMTA could not be all things to all market participants, but such conflicts were not limited to those between the sellside and the buy-side. Because of sellside business relationships with debtor countries, EMTA was able to promote the principle of creditor rights effectively, but not as aggressively in the context of specific credits as some investors would have liked. And as the Elliott v Peru case amply demonstrated, with some investors supporting Elliott's assertion of creditor rights, while others preferred to take advantage of the market opportunities that the aggressive assertion of individual rights would have prevented, investors were more than capable of having their own conflicting interests or holding inconsistent views on matters of principle or practice. The one factor that enabled EMTA to retain credibility, and to avoid fracturing on a faultline of such conflicts, was that rather than necessarily coming to and expressing a single position on many issues, EMTA more often provided a forum to enable market participants to exchange (and clarify) views, much as a market provides a forum to enable them to buy and sell.

The EM Debt Market Mourns and Responds to the 9/11 Tragedy. Against a backdrop of cautious optimism as inflows into the EM asset class replaced improving fundamentals as the main market driver in the Summer of 2001 (along with concerns about a teetering Argentina), the EM marketplace demonstrated great resiliency in the face of the horrible tragedy of 9/11. Several interdealer brokers located in the World Trade Center suffered devastating personal losses, and EMTA in particular mourned the loss of its director from Cantor Fitzgerald, Frank McGuinn.

In addition to the personal losses, which obviously caused unimaginable shock and mourning throughout the financial community, the terrorist attack created widespread dislocations for firms located in lower Manhattan, and as a result EM debt trading was severely disrupted. Along with the fixed income markets generally, the EM debt trading

markets in NYC were effectively closed on the following Wednesday, but reopened on Thursday, September 13. The NYC market observed early closings until the middle of the following week, and during this time much trading activity and processing was redirected to London, thus taking some pressure off of New York's capacity to handle transaction flows. Back-up systems and locations generally worked well, and the industry's seemingly superfluous preparations for Y2K in the run-up to January 1, 2000 were helpful in enabling the financial markets to cope with the dislocations. In varying degrees, communications disruptions and office dislocations lasted for most of September, but mourning continued.

Along with much of lower Manhattan, EMTA's offices at 63 Wall Street (with those inviting terraces) were evacuated on Tuesday afternoon, following a feverish period of locating, circulating and downloading contingency plans and lists of home contact information. EMTA's offices were reopened on the following Monday, again along with a large part of lower Manhattan, and access into the Wall Street area was for a time only available through a limited number of checkpoints. In the days immediately following the attack, EMTA worked in collaboration with The Bond Market Association and other industry trade groups to review systems availability and readiness, to advise market participants daily of the status of the market and to ensure that temporary contact information was available throughout the marketplace. EMTA staff participated in daily conference calls and communicated information to the marketplace by email, telephone and through the EMTA website daily for nearly two weeks following the attack.

As might have been expected, due to the concentration of offices in lower Manhattan, the weakest link in the New York EM trading infrastructure was the availability of broker screens and the processing of screen trades. It became apparent early on that, despite sharply reduced screen capacity in NYC and occasional outages in London, most dealer firms no longer considered "face-to-face" trading to be a viable alternative. Remarkable efforts by dealers, brokers and clearing firms substantially restored screen availability and processing capacity in New York by late September.

The next few months were a bleak time that no one working in lower Manhattan is likely to forget.

Argentina, the SDRM and Collective Action Clauses. A looming Argentina default increasingly hung over the marketplace over the course of 2001, and an increase in EM debt trading volumes was fueled by speculation over what was described by one analyst as Argentina's "roller coaster ride" and another as a "slow-moving trainwreck". Just before Christmas 2001, Argentina's FX markets became erratic and the government declared a moratorium on its bond payments. Shortly thereafter, EMTA issued recommendations to the effect that all Brady bonds and other global Eurobonds issued by the Republic of Argentina, unless otherwise agreed, be traded "flat" and

invoking back-up valuation and deferred settlement procedures for Argentina Peso NDF's.

A month earlier, on the Monday after Thanksgiving, the IMF's First Deputy Managing Director Anne Krueger proposed that sovereign financial crises be subject to a Sovereign Debt Restructuring Mechanism (SDRM). Shockwaves reverberated throughout the EM trading and investment community, and the private sector (and especially the EM investor community) began to mobilize against the proposal. Within days, for delivery at EMTA's 2001 Annual Meeting, I published a paper (entitled The IMF's Sovereign Bankruptcy Proposal and the Quest for More Orderly Sovereign Work-Outs) criticizing the SDRM proposal and suggesting a more practical approach.

Against the backdrop of the massive rescue packages for Mexico in 1995 and South Korea in 1997-98, Elliott Associates' enforcement action against Peru had combined with Ecuador and Argentina's defaults to ignite a small powder keg of policy turbulence for Emerging Markets investors that has abated, but in some respects continues to this day.

Ostensibly intended by policymakers to make sovereign debt restructuring more 'orderly', the SDRM proposal had a number of fundamental flaws that were quickly pointed out.

- (1) Among others, the SDRM proposal appeared to be based upon the dubious assumption that the existing mechanisms for resolving sovereign financial crises in the Emerging Markets did not work (or did not work well enough) because sovereign debt restructurings were too prone to disruption by hold-out bondholders or so-called 'rogue' creditors, an assumption largely contradicted by the recent experience of Ecuador, Pakistan, Russia and Ukraine in restructuring their bond debt (even in Peru, the Elliott enforcement actions had minimal effects on Peru's Brady plan restructuring and were successful in obtaining payment from Peru only several years later, at a time when Peru had accumulated ample reserves from which to make payment). In short, the perceived threat that a small minority of creditors would prevent a debtor country from restructuring was highly exaggerated, and much more theoretical than real.
- (2) The second basic flaw in the SDRM proposal was that it would have severely compromised the legitimate right of creditors to enforce their claims and thereby upset the delicate balance between the rights of sovereign debtors and their creditors. The fundamental types of creditor protections present in workable insolvency regimes (sales of non-strategic assets, changes in management and/or business and comprehensive treatment of all classes of debt) were lacking, in part because they simply cannot be enforced against a sovereign.

Such protections are a part of the necessary checks and balances that legitimize and make a bankruptcy regime fair and effective. When such key elements are missing, the appropriate balance between debtor and creditor rights is upset, and credit would stop flowing as a result.

- (3) Third, the legitimacy of a bankruptcy regime also depends upon there being an impartial arbiter whose judgments of fairness and efficacy strongly influence the reorganization process. The IMF's status as a creditor owned and controlled by debtor and creditor countries would inevitably create conflicts of interest and a resulting perception of bias (if not outright impartiality) that would damage the regime's legitimacy.
- (4) Finally, the proposed solution, a bankruptcy procedure, did not address the real problem, which was the failure of some sovereign debtors to develop the institutions and systems (and discipline), and to pursue the policies, that could provide greater protection over the long-term from severe economic and financial difficulties. A crisis prevented is one that never needs to be resolved. A sovereign bankruptcy mechanism would not have helped to address the problems that led to Argentina's crisis. Other policy measures and incentives applied much earlier might have. The 'gaping hole' in the current financial architecture was the apparent lack of effective policy measures and incentives to prevent sovereign financial crises, not the lack of mandatory mechanisms to ensure orderly debt work-outs.

For these reasons, the IMF's SDRM proposal seemed a serious step in the wrong direction. Instead, my paper, which was presented at a variety of forums in late 2001 and early 2002, argued in favor of a more market-oriented and case-by-case approach to resolving sovereign debt crises.

Galvanizing the private sector into an unprecedented (in my experience) degree of cooperation, by early February 2002, the SDRM proposal resulted in five financial trade associations (SIA, EMTA, IPMA, ISMA and TBMA) writing the Managing Director of the IMF a joint letter criticizing the proposal for these and other reasons. Shortly thereafter, John Taylor, Under Secretary of the US Treasury for International Affairs, without explicitly commenting on the IMF's SDRM proposal itself, encouraged the private sector to develop a market-based alternative pursuant to which debtor countries and their bondholders would insert into their bond contracts a new package of provisions known as 'collective action' clauses. In his view, these CAC's would provide for (a) majority-action voting to change payment terms (his suggestion was 75% instead of the 100% required in most bonds governed by NY law), (b) an 'engagement' clause describing the process for restructuring (including how the creditors would be represented during restructuring negotiations) and (c) an 'initiation' clause specifying how the sovereign



would initiate a restructuring (including a temporary standstill or suspension of payments while the restructuring discussions were being organized).

Despite the Taylor proposal, the SDRM proposal was not withdrawn, and it soon became clear that the official sector was directly or indirectly pursuing a two-track approach that involved simultaneously pressing ahead with the SDRM proposal and also promoting the more voluntary development and adoption of bond contract clauses along the lines of the Taylor proposal. Faced with this choice of alternatives, the Taylor proposal almost immediately received qualified support from the private sector, and various groups began the process of preparing a formal response.

Despite widespread agreement that the Taylor proposal was preferable to the SDRM (at least one very senior executive at a major sellside firm strongly disagreed, stating privately that the Taylor proposal should be resisted in its entirety because it was “proposed by people with no understanding of markets and is merely the first step in an effort to control them”), several months passed without any sign that a unified private sector position on the Taylor position would coalesce. The IMF floated a revised SDRM proposal, putting increased pressure on the private sector to respond. Working together with a group of five other leading financial trade associations (SIA, TBMA, IIF, EMCA and IPMA), EMTA was in a nearly unique position to assist in a constructive effort to develop specific clauses (or principles) that reconciled differing private sector interests and views. Other groups tended to represent sellside or buy-side views only, or had much less experience and expertise in the area of EM bond financing altogether.

On April 23, 2002, the Emerging Markets Creditors Association (EMCA) released their draft of Model Covenants for New Sovereign Debt Issues (a revised draft was released in May and posted on EMTA’s website). While apparently not developed in specific response to the Taylor proposal, these Model Covenants nevertheless contained a number of provisions that did respond to the three concerns expressed by Mr Taylor and others in the official sector. My Commentary on the Taylor Proposal and the EMCA Model Covenants reviewed both in detail, concluding that “bondholders would consider it a fair trade if EM sovereign bonds were made easier to restructure so long as, at the same time, greater efforts were made, contractually and otherwise, to ensure that making them easier to restructure would not simply result in their default and/restructuring becoming more likely”. To this end, the Model Covenants (as revised) responded to the Taylor proposal by supporting a form of majority-action clause (with a suggested voting level of 90-95% for amending payment and other key legal terms) and prescribing procedures to facilitate a better dialogue between sovereign debtors and their bondholders in times of financial difficulty. Responding also to the Taylor proposal in its broader context, the Model Covenants also invited a dialogue about contractual provisions (and other mechanisms) designed to provide greater assurance that debtor

countries would remain more creditworthy and, when confronted with financial problems, that they treated their bondholders more fairly.

On June 3, 2002, EMTA and the five other trade associations sent to the G10 finance ministers a joint letter that articulated a set of general principles for private sector involvement in resolving financial crises in the Emerging Markets. Among other things, the letter emphasized that any such involvement must be market-oriented to ensure the best chance of maintaining market access and restoring private sector credit flows. Specifically, the joint letter expressed support for limited collective action clauses (including super-majority provisions (at 90-95%) to amend payment and other key terms) in the context of other mechanisms (including greater transparency as well as enhanced financial covenants) intended to reinforce a higher level of financial discipline. Following on from their letter, the six trade associations continued their collaboration by working together to develop a private sector consensus regarding specific, marketable bond contract language that balanced the Taylor proposal with the legitimate concerns of bondholders that bonds be made more creditworthy at the same time that they be made easier to restructure.

The consensus represented by this joint letter, and the collaboration that resulted in it, was remarkable in that almost the entire private sector financial community was able to “get on the same page” and agree on a single approach; what it took was a general recognition that bond contracts had to include stronger creditor protections. It was not obvious that IIF would support this principle, or that EMCA would support the collective action clauses at all, and EMTA took the leading role in brokering the consensus, both by revising EMCA’s Model Covenants to make them more feasible, and by persuading IIF that increased creditor protections were necessary to make bonds with collective action clauses more marketable. EMTA’s specific contribution was to provide technical, legal and market input into the policy debate, to help find common ground for market participants and thus to form a more effective working coalition among the financial trade associations.

Despite increased private sector support for the Taylor proposal for CAC’s, many in the G10 preferred the SDRM, and as a result the official sector continued to pursue the ‘two-track’ approach through the Summer and the Fall of 2002. It was unclear whether or not the SDRM, or a UST-driven effort to draft specific bond language, could be pre-empted. Representatives of the six trade associations met with the G10 in the Fall and both reaffirmed their opposition to the SDRM and announced that they were developing model collective action clauses for marketable bonds under both NY and English law (including a summary of their terms). In support of the collaborative private sector effort to steer the official sector away from the SDRM and toward marketable CAC’s, EMTA published a position paper entitled *The Quest for More Orderly Sovereign Work-Outs* that summarized the flaws in the SDRM and the advantages of Marketable CAC’s.

Speaking at EMTA's 2002 Annual Meeting, UnderSecretary Taylor praised EMTA's position paper, noting that it fleshed out many of the details of how collective action clauses should be developed. Taylor affirmed that he agreed "wholeheartedly" with the two main principles of EMTA's paper: that CAC's must be acceptable to both debtors and investors, and that the new clauses must not increase the likelihood of a sovereign's decision to seek a restructuring. "Conditions now appear ripe" for the actual writing of the new clauses, he said, and, echoing the sentiments of former Secretary Brady spoken at a previous EMTA Annual Meeting, he termed 2003 the time for market participants and sovereign issuers to "roll up their sleeves and get to work".

In January 2003, the group of financial trade associations (now expanded with the addition of ISMA to a group of seven) released its Marketable Bond Package, which included specific bond language for bonds under NY and English law, as well as a Code of Conduct for resolving financial crises in the Emerging Markets and a form of Bond Documentation Chart to be used in summarizing and publicizing the key terms of EM bond issues.

Within several months, Mexico surprised the markets by becoming the first EM country to include CAC's in its bond documentation. Mexico's initiative was strongly supported by the US Treasury but given only qualified support by EMCA, which noted that the Mexico's CAC's would permit the amendment of payment terms by a 75% vote of bondholders and that the CAC's seemed to lack some of the creditor protections that had been recommended by the group of seven trade associations. Not wanting to interfere with a market transaction, EMTA declined comment on Mexico's CAC's, other than to say that this aspect of bond documentation and crisis resolution had now moved "out of the hands of government policymakers, and trade associations, where it never really belonged, and into the marketplace, where it properly does." Soon after Mexico's pioneering bond issue was successfully completed, other debtor countries followed (including Uruguay, Brazil, South Africa, Korea and the Ukraine), for the most part following the example of Mexico's clauses (with some variations in super-majority voting percentages), and to enable the marketplace to compare them more easily, EMTA began preparing and publishing summaries of their terms with its Bond Documentation Charts. Little further was heard of the IMF's SDRM proposal, which was quietly withdrawn by the IMF and G7 in the Spring of 2003.

The IMF's SDRM proposal and the EM industry's effort to oppose it, and to influence the official sector toward a more market-oriented approach toward involving the private sector in the resolution of financial crises in the Emerging Markets, was a long, drawn out affair, marked by intensive collaboration among a broad spectrum of trade associations against a backdrop of considerable industry concern that Argentina's economic crisis and default were not being adequately addressed. Although the rest of the market decoupled from Argentina soon after its default, there was much at stake for

Argentina's bondholders, and the memory of Ecuador was fresh in the collective mind of EM investors. Many EM investors were clearly uncomfortable with the general lack of credit protections built into bond documentation, and unhappily surprised by the way they were treated by Ecuador and later Argentina, and by the apparent indifference of the IMF and other official sector bodies and lack of remedies they had in response.

Although the Taylor proposal itself, and perhaps the trade association effort in support of it, took much of the wind out of the SDRM's sails, what ultimately seemed to tip the balance against the SDRM and in favor of marketable CAC's was that major debtor countries were strongly, but quietly, against the SDRM proposal, out of a concern that it would drive up borrowing costs and limit the control that they had over their own debt strategies. Mexico's adoption of CAC's largely settled the matter, although for a time there were variations in the voting levels included in the CAC's of different countries, variations that indicated a continuing conflict between the interest of debtors and investors, as well as some unresolved tension between the somewhat conflicting goals of standardizing bond documentation and the traditional case-by-case approach toward resolving financial crises in the Emerging Markets.

EMTA's efforts to forge a consensus between the EM sellside and buy-side were important in catalyzing an effective industry response to the SDRM. Although CAC's were not a perfect solution to the problem of how to resolve financial crises in the Emerging Markets, they did help preserve a more market-oriented, case-by-case approach to future crises than would otherwise have been the case under the SDRM. At least for the time being, the Argentina default notwithstanding, the policy debate about this aspect of resolving financial crises in the Emerging Markets, and how to involve the private sector in it, and the resulting distractions, seemed at last to have ended. More importantly, the markets moved on.

The confluence of Ecuador, Argentina and the SDRM brought the EM trading and investment community, and even the broader financial community, together to an unusual degree. Most importantly, the trade association collaboration, and particularly the cooperation between EMTA and EMCA, demonstrated that the two organizations, and the EM sellside and buy-side generally, could work together toward common goals. This common undertaking laid a good foundation for future cooperation between the EM sellside and buy-side, and that it had occurred within EMTA meant that EMTA was likely to be a forum shared by the sellside and buy-side going forward. In addition, the working relationship with ISMA, IPMA, TBMA, SIA and EMTA showed that the organizations all shared common interests and goals, albeit each within its separate spheres of expertise and influence.

Industry and Trade Association Convergence/EMTA's Office Move to 360 Madison Avenue. EMTA's increasing visibility on buy-side issues was accompanied by a steady

increase in buy-side membership. By mid-2003, ten of EMTA's 22 directors were representatives of buy-side firms, and for several years nearly half of EMTA's agenda had been focused on issues that could be said to be mostly buy-side in nature. Among other things, the collaboration among financial trade associations to oppose the SDRM and to shape the evolution of CAC's, as well as the continued Argentina default, eventually led to discussions between EMTA and EMCA regarding a possible combination between the two organizations. The direct impetus for the possible combination probably came from a joint EMTA/EMCA effort to oppose certification of a class action against Argentina (including the imposition of a formal stay that would in effect have reversed the Allied decision) and instead suggest ways in an amicus curiae brief that the federal district court might help guide Argentina toward as constructive a restructuring process as possible. Argentina generally was in favor of the brief, in part because a class action would have subjected the restructuring process to the untoward influence of class action plaintiff's counsel (the court eventually ruled against both the class action and the stay). Throughout the process of developing the legal brief (which was never finalized), it became increasingly clear that EMCA's substance lay in its membership and Board leadership, but that it did not have sufficient staff resources to follow-up on its Board's policies.

Early discussions quickly led to the shared conclusion that EMTA and EMCA should affiliate as sister organizations under a new umbrella organization (tentatively called EMA) with three semi-autonomous organizations representing the sellside (EMTA), buy-side (EMCA) and FX derivatives (EMDA) businesses. In general, all trade associations serving the financial sector had been under considerable pressure to improve their efficiency and reduce their cost structures. The trend toward consolidation that had existed generally in the financial industry for several years had clearly reached the financial trade associations. The proposed affiliation of EMTA with EMCA could be seen as part of this trend, as well as evidence of the continued maturing of the EM trading and investment businesses. In addition to a fairly obvious overlap of membership interests, the proposed affiliation was driven by a mutual need for a better economy of scale—EMCA had suffered from an apparent under-capacity of staffing and other resources, while EMTA had somewhat of an over-capacity. The proposed affiliation was intended in part to provide a more efficient (and effective) matching of resources against services needed. Unfortunately, the discussions with EMCA first lagged, and then stalled in 2004, mostly as a result of difficulties that EMCA had in focusing its attention on the proposed affiliation. One conclusion that could be drawn from this was that it demonstrated EMCA's need for the affiliation as clearly as EMTA's eroding finances showed EMTA's need for it.

Meanwhile, the industry drive toward greater efficiency ( the trend that had become known as 'convergence') continued, as did the trend of EMTA's increasing work on behalf of buy-side interests.

Dating back to its formation in late 1990, EMTA's offices had always been in the Wall Street area, first within JP Morgan's complex at 23/37 Wall Street and 15 Broad Street, and later in the Brown Brothers Harriman building at 63 Wall Street. EMTA's lease at 63 Wall was due to expire early in 2003, and EMTA began searching for new space in 2001. On the assumption that midtown rent levels were prohibitively expensive, the search focused on the Wall Street area.

In August 2001, the heads of fixed income at 21 major financial institutions (including 11 EMTA Board firms) wrote a letter to their financial trade associations (specifically, SIA, TBMA, ISMA, ISDA, IPMA, LSTA, FIA and EMTA) asking for greater organizational and operating efficiency among industry trade associations in view of the increasing integration of financial products within individual firms. The associations were asked to meet to review alternatives that would achieve these objectives. This letter, and the obvious trend toward industry convergence that was behind it, precipitated discussions among all of the associations, but particularly between TBMA and EMTA regarding how the two organizations could work together more effectively (after several months, the group of trade associations responded with a joint letter summarizing some of their current efforts to work together more efficiently, at the same time stating some concerns about organizational integration and requesting further guidance from the fixed income heads). At about the same time, EMTA was offered the opportunity to join TBMA in a real estate parcel that it was assembling midtown for a possible group of financial trade associations.

TBMA soon proposed, in a draft letter, a combination in which EMTA would become a semi-autonomous affiliate of TBMA, maintaining its own Board of Directors, staff and agenda for an indefinite period, while working toward a closer integration in the future. My initial reaction to this proposal was colored by issues that had arisen in connection with the more or less contemporaneous integration of EMCC into DTCC and with our prior experience with TBMA's predecessor, PSA (a prior effort in 1997 by PSA to take over EMTA had ended when key EMTA Board members thought the idea premature). From EMTA's side, the most obvious concerns involved the reactions of EMTA's non-US and buy-side members (at the time, TBMA did not permit buy-side members and was generally perceived outside the US as an almost exclusively domestic US organization) and about the potential weakening of EM decision-making and 'voice' within a broader, integrated organization (the same thing that had happened to EMCC).

Of three possible alternative ways of structuring a closer relationship between EMTA and TBMA (EMTA as an integrated Division, EMTA as an affiliated Forum or EMTA as a

tenant with some sharing of administrative staff), I recommended that we work with TBMA staff to explore the middle alternative. Under this alternative, EMTA would become a 'forum' of TBMA on terms that addressed EMTA's basic concerns about TBMA's mainly domestic US and sellside orientation. EMTA would retain its separate corporate identity, Board, membership, finances and senior staff. Certain administrative staff would be transferred to TBMA and 'leased back' on an as-needed basis, thus (A) giving EMTA greater access to TBMA resources in areas such as IT, communications and advocacy and (B) enabling EMTA to shed about enough in annual administrative expenses to offset the increased expense for midtown office space. Future steps toward further integration of the two organizations would be reviewed over a two-year period, based on such factors as how well the affiliation was working and what further progress TBMA made toward becoming a more globally-oriented and buy-side-oriented organization. This type of arrangement was discussed at several EMTA Board meetings over the course of the first half of 2002, and the negotiation of a formal memorandum of understanding to implement the affiliation of EMTA as a TBMA forum was approved. Throughout the negotiation, TBMA's CEO Micah Green was extremely reasonable in resolving issues that arose, and during this time, EMTA and TBMA were working in close collaboration to put together the private sector alternative to the IMF's SDRM proposal.

I recommended the resulting MOU essentially because I thought that the affiliation would put EMTA on a somewhat sounder financial and institutional footing without sacrificing its credibility or effectiveness. In my view (the rest of EMTA staff did not necessarily agree), the MOU, as negotiated, adequately balanced a number of considerations: EMTA would have greater access to some key resources, better technology and better opportunity to coordinate policies with other associations, without losing the independence it needed to set and execute its agenda and serve its membership. EMTA's affiliation with TBMA was supported by the representatives on EMTA's Board of several US investment banks, but viewed somewhat skeptically or opposed by most other Board members.

Following a lengthy discussion at a Board meeting in the Summer of 2002, a strong consensus of EMTA's Board welcomed EMTA's relocation into the TBMA premises at 360 Madison Avenue, as well as the related resource-sharing arrangements, as a substantial step toward greater efficiency, coordination and cost-savings, but decided that any further integration of EMTA with TBMA (as a forum, affiliate or otherwise) might adversely affect EMTA's credibility and status as a global organization with significant buy-side orientation and extensive activities outside the fixed income area (notably, FX derivatives). This decision was strongly supported by EMTA's Co-Chairs, Juan del Azar (Merrill Lynch), George Grunebaum (JP Morgan Chase) and Mark Coombs (Ashmore).

Accordingly, in November 2002, EMTA relocated from 63 Wall Street to 360 Madison Avenue, and within several years, ISMA and IPMA in London had merged to form ICMA (2005), and TBMA and SIA (located primarily in NYC and Washington, DC) had merged to form SIFMA (2006), which has subsequently worked to develop a more global presence. EMTA, LSTA and ISDA remain independent trade associations. In the final analysis, the combination of the lease and resource-sharing arrangements with TBMA effectively decreased EMTA's overall annual expenses by about \$170,000 (increased occupancy expense of \$50,000 offset by a decrease in staffing costs of \$220,000), thus relieving EMTA of some of the financial pressure that it had been under since the contraction of the EM trading industry after the Asian and Russian debt crises.

The Continuing Warrant Debacle. As recounted in EMTA 1994-98: The Golden Era of EM Debt Trading?, there have been longstanding difficulties in the settlement of trading in the commodity-based warrants that originally accompanied the issuance of certain Brady bonds (most notably, Mexico's Value Recovery Rights, Venezuela's Oil Obligations and Nigeria's Payment Adjustment Rights). Though initially attached to the underlying Brady bonds, these warrants became detachable, with their own ISIN codes, and therefore settlement of trading in them required submission of a separate instruction to the settlement systems (Euroclear, Cedel (later Clearstream) or DTCC). Unfortunately, this separate settlement instruction was often forgotten or disregarded, the result being a long chain of failed or non-settlements, which only became a practical problem years later when the warrants came into the money. In 1997, EMTA adopted a new set of market practices for Mexico's Value Recovery Rights that were designed to simplify warrant settlement (by bundling them with their underlying Brady bonds into units with a single ISIN code so that only a single settlement instruction was required to effect settlement of the unit). Unfortunately, by then, sufficient seeds of confusion had been sown to create reconciliation and settlement problems that continued for many years.

After nearly a year of consideration, a new market practice for trading Mexico Value Recovery Rights became effective on February 1, 2001, providing that VRR's would trade separately from their related Discount and Par Bonds (and vice versa) (a comparable revision in market practice was recommended for Venezuela Oil Obligations effective early in 2002 and for Nigeria's Rights effective late in 2002). Previous market practice, dating back to 1991, had been that a trade of such bonds was assumed, unless otherwise agreed, to include the related VRR's (the previous market practice being justified by the fact that, historically, the VRR's had only occasionally been in the money (and then not substantially so) and therefore were generally perceived as having little or no market value).

The change in market practice was largely driven by a sharp increase in global oil prices during 2000 that put the VRR's in the money and increased their market value.



Providing for separate trading of VRR's from their related bonds was perceived as offering several advantages to the marketplace: (1) separate trading would create a market for the VRR's, thereby enhancing and "unlocking" their market value that, under the former market practice, was embedded in the price of the related bond and (2) separate trading would permit Discount and Par Bonds to settle without the need for separately transferring the related VRR's, a transfer that, unfortunately under the former market practice, was not always (perhaps rarely) done, thus creating over the years the massive accumulation of failed VRR transfers. To assist the marketplace in better understanding Mexico VRR's and their trading characteristics, EMTA prepared and published "EMTA's Primer on Mexico Value Recovery Rights".

Eventually, the new market practice was enthusiastically received by the marketplace, but the process of developing and implementing it was convoluted and slow-moving. Many market participants had wanted the new practice to become effective in mid-year 2000, before payments on the VRR's began to become due, but its implementation was delayed by six months when the fragile consensus in its favor broke down in the late Spring of 2000 over concerns about several potential disadvantages. While ultimately successful, EMTA's experience in connection with adopting this new market practice illustrated both the pros and cons of EMTA's consensus-oriented decision-making process.

From the outset, the marketplace seemed in uniform agreement on the two advantages of the new market practice described above. Many market participants also believed that, in addition to halting the increase of failed VRR transfers ("stopping the bleeding"), the new practice would actually help reduce the outstanding backlog by creating a supply of VRR's in the market for use in settling old fails and by establishing a VRR market value that would quantify the potential risks associated with the backlog. Several other major market participants disagreed, however, arguing that, while trades in the Discount and Par Bonds would settle without problems under the new market practice, any separate trades of VRR's would likely fail, thus aggravating the existing backlog; moreover, the change in market practice, they felt, would increase the likelihood of disruptive buy-ins and potentially contentious claiming for VRR payments. In effect, these market participants strongly believed that the new market practice should not be adopted until further progress had been made in the reconciliation and clean-up of the accumulated backlog of failed or otherwise unsettled VRR trades.

In the absence of clear consensus, EMTA reluctantly decided to defer the new market practice until later in the year 2000 (and then later into early 2001) and in the interim to concentrate on the reconciliation and clean-up process. This decision was not uniformly popular, particularly with buy-side firms that understandably wanted to recognize the embedded value of the VRR's as early as possible.

A Digression on Market Practices and EMTA's Decisionmaking Process. For an organization that works to promote greater transparency in the marketplace, it is perhaps odd that EMTA's own decision-making process is somewhat opaque. But making decisions for a marketplace that is composed of buyers and sellers with diverse and often-opposing interests is hardly simple or straightforward. Despite by-laws that provide, in most cases, for decision by majority voting of the Board of Directors, by long-standing custom, most EMTA decisions, and certainly those involving market practices, are made by consensus, a process that has been worked out over time but may not always be self-apparent.

Market practices are proposed by EMTA members. These proposals are typically developed and circulated by EMTA's staff in consultation with (mostly) ad hoc working groups as draft recommendations for review by market participants, often with the reasoning for the proposed recommendation as articulated by its leading proponents. If consensus is not reached in the first instance, the draft recommendations are revised and recirculated to the market for further review and comment. When consensus is reached, the recommendations are republished prior to their becoming effective. Occasionally, so-called 'final' recommendations are revised before their effective date. Following their formal recommendation, market practices are subject to further review and may be revised from time to time. In general, EMTA's market practices are recommendations only, and as such, are not binding on market participants except to the extent that they agree, explicitly or implicitly, to be bound by them in the context of specific transactions. I cannot think of a market practice recommendation that did not contain the phrase "unless otherwise agreed".

How well have these informal procedures served the marketplace? And what constitutes a "consensus"?

For two decades, EMTA's decision-making procedures have enabled the industry to address many of its most pressing problems with a minimum of controversy or acrimony. While they have sometimes slowed down market-wide decision-making, they have never resulted in stalemate. For the most part, in an environment of volatile uncertainty, they have worked well to allow market participants with diverse, and often strongly-held, views to resolve their differences and make progress on complex issues. While mistakes are sometimes made, serious ones have been avoided.

As it has evolved, EMTA's consensus approach clearly requires more than a majority and somewhat less than unanimity. Above all, reaching consensus requires a balancing of interests. The majority implicitly agrees not to override a reasonable objection from a significant minority, and the minority agrees not to raise unreasonable objections and to graciously drop their objections when (and if) it becomes clear that they have been raised and fairly considered. All commit in good faith to work to resolve differences and

reach an acceptable consensus view as soon as practicable. This approach seems to balance the interests of all market participants, whether they are in the majority or the minority. Speed is sometimes sacrificed for the greater certainty and legitimacy that usually comes from considering all views seriously. Weighing factors such as the influence of a market participant and the strength of its conviction or the reasonableness of its views requires considerable subjective judgment, and determining when consensus has been reached (and sometimes where it can be reached) may be more art than science.

This consensus approach has generally served the marketplace well. Did it work perfectly in the case of the 2001-02 market practice for VRR's (or necessarily in later efforts to resolve the continuing warrant settlement problem)? Perhaps not quickly enough in 2000-2001, but well enough considering the serious concerns that were raised. Although the 2001-02 market practice was delayed for over six months, during the delay sufficient progress was made in reconciling old trades and cleaning up the existing backlog to allay previous concerns and enable a stronger consensus to form. As it turned out, the new market practice worked reasonably well (certainly in terms of "stopping the bleeding" and allowing bond trades to settle), and the buy-ins and claiming that some had feared did not materialize. While the market practice was undoubtedly successful, its benefits came later than some market participants would have wanted.

Venezuela's Warrants Come into the Money. Unfortunately, "stopping the bleeding" was not enough to save the patient. Once the warrants came into the money, the somewhat theoretical problem of not being able to reconcile and settle warrant positions became the more practical and immediate one of warrant payments not ending up in the hands of the right counterparties.

Although the difficulties in reconciling warrant positions was common to Mexican, Venezuelan, Nigerian and, to a lesser extent, Uruguayan instruments, various circumstances (including their issuance in series and Mexico's retirement of its bonds by 2003) limited the worst of the problem to Venezuela's Oil Obligations, which came into the money for the first time in the last quarter of 2004. This payment was not made when due, and its delay until March 2005 raised many trading questions. The EMTA Warrant working group immediately began an intensive effort to focus on the reconciliation of the Venezuela Oil Obligations, and in June 2005 EMTA released a communication to the marketplace in support of this effort, advising that "In the interests of an orderly market, EMTA wishes to remind all market participants that, although progress has been made toward the industry goal of resolving this settlement backlog satisfactorily, until this reconciliation is substantially completed, and a strategy to address the current problem comprehensively (such as a global multilateral netting facility) can be developed and implemented, a certain amount of patience and forbearance in dealing with counterparties is likely to contribute a great deal more to the

overall resolution of the settlement backlog than the aggressive pursuit of individual payment and settlement claims”.

The reconciliation effort focused initially on an internal reconciliation (particularly important for those dealer firms that had participated in mergers), and then proceeded in the Fall to reconciliation among dealers and between dealers and the settlement systems, and finally between dealers and custodians for buy-side firms. EMTA assisted in this reconciliation effort by collecting and disseminating contact information and by hosting monthly conference calls to review reconciliation progress. During the course of this work, it became apparent that poor recordkeeping and the lack of cooperation from many custodians were significant hurdles to addressing the overall settlement backlog, as were a number of legal issues relating to the considerable length of time that the backlog had existed (in particular, the length of time that settlement fails had existed and related issues involving statutes of limitations and measurement of damages). Legal uncertainty and complex and differing factual circumstances combined to help frustrate the development of a comprehensive solution. In mid-Summer 2005, the EMTA Board was informed that “Realistically, beyond facilitating reconciliation through better information-sharing and some nudging, reducing agreed positions through bilateral and/or multilateral netting and facilitating cash settlement, there may be little that EMTA can do to help address the overall settlement backlog.”

By late in 2005, sufficient progress had been made by the dealer community in reconciling their positions internally, and with the settlement systems and with each other, to enable JP Morgan Chase to propose a large multilateral netting facility as an effort to provide a comprehensive solution to the longstanding problem. As proposed, positions would be netted multilaterally among a critical mass of market participants and the resulting net positions would be cash-settled at a price determined by a market mechanism. The facility was authorized by EMTA’s Board in early 2006, and work began on its construction, with a view to completing it by the Summer of 2006. The facility was publicly announced in February 2006 and it remained clear that reconciliation with custodians and legal issues bearing on the appropriate pricing of the cash-settlement mechanism would be the main hurdles to the completion of the facility. Regulatory pressure was applied by the New York Stock Exchange in the Spring of 2006, and operations personnel worked intensively to complete the necessary reconciliation. At its October 2006 meeting, EMTA’s Board recognized that the earliest possible date for completing the facility was some time early in 2007 and that very significant issues would need to be worked out before any such facility would be feasible, including much more reconciliation work (especially with customers and their custodians) and consensus on the structure and pricing methodology (which were, as noted above, dependent on a combination of uncertain legal and factual issues).

During the course of collecting data for the proposed multilateral facilities, EMTA became aware of many opportunities for firms to reduce risk and facilitate settlement by entering into trilateral netting and other arrangements that would prove much more

feasible due to their relative simplicity and lesser vulnerability to the non-participation or withdrawal of counterparties. By the Spring of 2007, it had become apparent that the barriers to completing a multilateral netting as a comprehensive solution were insuperable, both for Venezuela and for Nigeria, and EMTA shifted its attention to attacking the overall problem in a series of smaller steps by preparing documentation for and encouraging a series of these trilateral arrangements among interested market participants. Often, these transactions were structured as trilateral “step outs” or “offsets” without settlement to avoid pricing and delivery problems and thereby ensure their completion.

With the onset of the subprime mortgage crisis in the third quarter of 2007, the EM industry’s effort to resolve the warrant settlement backlog, particularly with the elusive industry-wide comprehensive solution, gradually lost steam. Much progress had been made in reconciling positions among market participants (especially on the sellside), but several factors (and particularly differing perceptions of the value and enforceability of warrant claims, and the relative lack of progress in engaging cooperation from buy-side firms that were net sellers of the warrants) combined to prevent a comprehensive solution. With the exception of a netting facility for Nigeria’s warrants, completed in the run-up to a Nigerian exchange offer for them, the effort to arrange a multilateral netting facility proved to be impossible. An unknown number of smaller trilateral and bilateral facilities were successfully completed, however, which makes it possible to say that although we were not aware of any large-scale break-throughs in resolving the overall situation, the problem was pecked away at, and that may have been the best that could have been hoped for under the circumstances.

More on Argentina and the ‘Unfinished Business’ of the Burden-Sharing Debate. At a time when many Emerging Markets countries truly emerged, the Argentina default continued to have market and policy implications throughout the decade of the 2000’s, long after the implementation of CAC’s had taken the wind out of the SDRM’s sails.

The keynote speaker at EMTA’s 2003 Annual Meeting was Argentina’s Finance Secretary Guillermo Nielsen, a somewhat controversial choice especially in the view of a number of EMTA’s buy-side members, who felt that permitting him to give the keynote was, because of Argentina’s recalcitrance in dealing with its bondholders, giving Argentina a platform that it did not deserve. Officially, EMTA remained neutral in the obvious dispute between Argentina and its bondholders, though some private efforts were quietly made to encourage Argentina to recognize a negotiating committee, a process that Argentina firmly rejected as against its interests. In response to the objections of some EMTA buy-side members, I tried to ensure that Mr Nielsen’s remarks were placed in an appropriate context, by making sure that his address was preceded by panel presentations that would highlight market concerns, as well as a special briefing by members of the Argentina Bondholders Committee on their recent counterproposal to Argentina’s initial restructuring offer, and by inviting him to respond. During the meeting, I noted that Mr Nielsen, and also the ABC, had been invited to speak as part of EMTA’s role to provide a forum for the discussion of important market issues, and to promote the dialogue between Argentina and its bondholders. Mr

Nielsen's remarks were comprehensive, and delivered graciously, though his description of the restructuring process that Argentina intended to follow was more inclusive, and less recalcitrant, than most investors, then or now, would be willing to give Argentina credit for.

Within a year or so of Mexico's pioneering inclusion in March 2003 of CAC's in its bond issues, nearly 30 other EM sovereigns brought to market bonds with CAC's under either NY or English law aggregating over US\$47 billion in face amount. During this time, general market conditions were very favorable for issuing EM bonds, and, regardless of how investors may have felt about CAC's generally, these various CAC bond issuances were generally well-received. EMTA's bond chart summaries of the terms of these bonds showed that there were significant variations among them. Of course, none of this affected Argentina, but the Argentine default, and its difficult restructuring process, continued to have its effect on the burden-sharing debate.

While all of these bond issues included provisions to permit payment and other key terms to be changed by majority action (thus responding to what had been perceived as a potential holdout or 'rogue' creditor problem), with the exception of two issues (one by Hungary and the other by Latvia), they failed to address concerns (expressed by Mr Taylor in his original proposal, and also expressed by many investors frustrated by Argentina's restructuring process) that EM sovereign bonds lacked adequate mechanisms to facilitate the constructive 'engagement' of sovereign debtors and their creditors in times of financial distress. To some (including me), the lack of such engagement mechanisms (which include the formation of negotiating committees and reimbursement of their reasonable legal and financial advisory expenses) seemed a remaining 'hole' in the existing architecture for resolving financial crises in the Emerging Markets that permitted 'rogue debtors' to avoid negotiating their way out of default.

Argentina's relationship with its creditors remained polarized throughout 2004, and the burden-sharing issue was increasingly seen through an Argentine prism. IIF pushed hard for a set of Principles that would articulate guidelines for the conduct of debtors, creditors and the official sector in the context of EM sovereign financial crises. Over the Summer of 2004, EMTA worked intensively with a group of five other major financial associations (SIA, TBMA, ISMA, IPMA and EMCA) in an effort to improve the IIF's draft Principles. The effort was only partly successful, as IIF broke off the collaboration after refusing a final set of comments that the group felt was necessary to ensure that the Principles would be supported by a sufficiently broad spectrum of the marketplace (and particularly, investors) to validate them and make them successful.

While the IIF Principles appropriately emphasized that debt restructurings should be voluntary and as market-oriented as possible, they failed to provide useful guidance on two areas that many investors considered important to the integrity of the restructuring process, constructive engagement with creditors and the aggressive use of exit consents. The final version of the Principles was silent on the issue of exit consents (rather than, as was suggested, discouraging their aggressive use), and did not support the inclusion of engagement provisions as a part of CAC's (which would have included

the recommendation that debtor countries reimburse creditor committee expenses). By not dealing with these two issues adequately, the IIF Principles did not add much, if anything, to the then-existing framework for resolving crises, and as a result, investors did not support them, and despite considerable pressure from IIF, EMTA declined to take a formal position on them (I had to remind IIF that EMTA could recognize market consensus, but could not manufacture it). Ultimately, IIF's goal was to submit their Principles to the G-20 countries at their Fall Summit; the G-20 issued a statement welcoming the Principles, but tellingly declined to endorse them.

Argentina's long-awaited exchange offer to restructure its bonds was finally launched in January 2005, and following several delays due to pending litigation that threatened to attach tendered bonds, the exchange offer was completed in early June, restructuring about 76% of Argentina's bond debt. In connection with the restructuring, EMTA recommended forms for trading the various instruments issued pursuant to the exchange offer on a when/issued basis. Legal actions by non-tendering bondholders against Argentina to enforce their judgment claims continued, however, though without a great deal of success, and EMTA continued to monitor the situation closely.

There is little that can be said about Argentina's economic difficulties, default and 2005 restructuring that all market participants would agree with, other than that the whole situation was deeply unfortunate and that it highlighted the lack of consensus about country debt restructurings. Many investors, for example, sharply criticized Argentina's restructuring tactics, which involved what can fairly be described as a "take-it-or-leave-it" offer, at a time when many believed (particularly with the benefit of hindsight) that Argentina could have offered its creditors more generous restructuring terms. Other investors (some pointing to the subsequent performance of Argentina's innovative GDP instruments and other assets offered in the restructuring) have criticized the so-called 'hold-out' investors for not participating and, in effect, for not simply 'moving on'. Similarly, the resulting legal actions against Argentina have been criticized by some (as disruptive, unsuccessful and, in effect, shortsighted), and applauded by others (for defending the interests of creditor's rights and pressuring Argentina to reopen its 2005 offer). A clear example of the differing opinions that together make markets.

Beginning with the Mexican 'Tequila' crisis in 1994, there was much debate about international financial architecture, whether or not there are 'holes' in it, and if so, how to fill them (the debate was continuing in mid-2010, particularly with the Euro-Zone crisis). Much of this debate was overblown, and focused on perceived demons such as 'rogue' creditors, 'rogue' debtors and even 'rogue' international financial institutions.

Lessons Learned. After some of this dust had settled, over the course of 2006, EMTA presented four panel discussions relating to various aspects of what we called "Partial Sovereign Restructurings". The purpose of these discussions was not to take sides in the debate about Argentina's default and restructuring, or necessarily to develop any sort of consensus position on any of the questions raised by it or other recent restructurings, but simply to explore the lessons, if any, that could be learned from recent experience, an experience that was difficult for all concerned, and for the market

in general. Panelists included a range of lawyers (for both debtors and creditors), representatives of the official sector, rating agencies, investors and the sellside. Various observations can be drawn from these presentations.

- (1) Rating agencies may have quite different policies on how to treat sovereign debtors that are in, or emerging from, default scenarios, and in particular, they may have differing views on the relative importance of capacity and willingness to pay. These discrepancies are probably mirrored in a certain inconsistency of investor views regarding the significance of a debtor country's track record in servicing its debt. This inconsistency certainly can be seen if one looks at the differing investor attitudes regarding Argentina.
- (2) Creditor participation levels in sovereign restructurings may or may not have declined from the 95%+ critical mass levels of the Brady and pre-Brady era, but it seems clear that the diversification of bondholders, low carrying costs, debtor country populism and the trend toward CAC's at the 75% level put some downward pressure on future participation levels, with one implication being greater potential for litigation. Regardless of the factors that led G-8 governments to encourage the market to adopt the 75% CAC's that are now standard, the many prior bond issues without CAC's will probably require that most country debt rescheduling will continue to be structured in the form of exchange offers. Despite some signs of a trend toward greater populism (eg, Ecuador), each country that determines that a restructuring is necessary will likely do so in the context of its own facts and circumstances. Belize, which completed the restructuring of its debt in 2007 with a participation rate of 98%, signaled early on that its restructuring would be market-friendly (other examples of market-friendly deals would include Uruguay and the Dominican Republic). Compared with Argentina, that establishes a wide bid/offer in restructuring approaches and participation levels, and at this point, there is no more reason to assume that other debtor countries will follow the Argentine model than the Belizean one. Presumably, future restructurings will be guided less by populism than by a practical balancing of the degree of debt relief needed with the benefits of early return to the normally functioning voluntary markets, and it seems clear enough that the main factors in determining the level of creditor participation are the nature of the debtor's engagement with its creditors and whether or not the restructuring process is considered market-oriented.
- (3) Predictably, there is a significant split in perceptions between investors and debtor countries regarding whether or not the US Foreign Sovereign Immunities Act is working properly, or as originally intended, with debtors and many in the official sector pointing to the somewhat greater prevalence of creditor litigation, and investors emphasizing the surprising few instances where creditor litigation has actually resulted in any recovery. Despite the fact that one of the fundamental purposes of the FSIA was to 'de-politicize' the granting of sovereign immunity and to make the judicial process more transparent and objective, it seems that the question of litigation against sovereigns has become more political than ever before.



- (4) At the same time, there is a significant spectrum of private sector attitudes, and even split views within the investor community, regarding whether or not the existing financial architecture is adequate in balancing the interests of debtor countries and their creditors. Some investors seem much more inclined than others to approve of aggressive actions taken by some creditors that could interfere with the flexibility of other investors to enter into restructurings or other financings with debtors. In fact, the divide between investors seems to extend almost to the point where some investors care passionately about the enforceability of their rights under bond legal documentation, while others seems almost not to care whether or not their bonds are enforceable. If one can generalize, EMTA members seem to believe that while the enforceability of bonds generally underpins the market, thus establishing a bedrock of value, actual enforcement by a single creditor can have the potential to reduce value for other investors. The beauty of bond enforceability is very much in the eye of the bondholder.
- (5) The prevailing view among investors, despite their differences, is that G-7 (or in these days, G-20) policies are significantly more in favor of debtor countries, and less in favor of creditor interests, than they were a decade or more ago. This trend probably traces back to the mid-1990's, when with the increasing securitization of EM debt into bonds, came a growing sense in the official sector that their traditional approach toward supporting EM debt restructurings needed to be reviewed. Before Argentina, there was a widespread sense throughout the official sector that the presumed 'hole' in the international financial architecture was the potential that a 'hold-out', or 'rogue', creditor might disrupt a restructuring. This perception was generally consistent with the prevailing official sector philosophy of 'burden-sharing', but largely seemed to stem from the relatively isolated experience of Elliott v. Peru, where a creditor who had bought its debt at a discount in the secondary market succeeded in collecting a substantial claim, but only several years after Peru's restructuring was successfully completed. The 'disruption' was more theoretical than real, but it ultimately led to a series of official sector proposals designed to fill the perceived 'hole'. One of the more enduring legacies of the Argentine default and restructuring may be that the official sector has gained a greater appreciation of the appropriate balance between debtors and creditors, as well as of its limitations to influence outcomes, that may lead it to be more modest about what it can or should do to help resolve future sovereign financial crises.
- (6) Finally, the ability to make accurate judgments about the efficacy of the international financial architecture is affected by the prevailing economic and investment climate, which in the period 2000-2007 was characterized by high commodity prices, low interest rates, substantial accumulation of reserves and reduction of debt levels by many debtors, substitution of local currency financing for financing in external currencies and generally high levels of liquidity. During EMTA's 2006 presentation series, several speakers noted the inability of market forces to impose much in the way of discipline on sovereign debtors under then-current market conditions, in the absence of stronger

enforcement rights. Just as the favorable economic environment bolstered the performance of Argentina's economy, it may also have made investors generally less risk averse and more tolerant of the apparent erosion of creditor rights represented by such things as the market's adoption of collective action clauses and recent developments in the interpretation of the FSIA by US courts. It would be a mistake automatically to assume that either the particular economic and market environment, or the investor or debtor behavior that it encouraged, would remain constant. Perhaps with the passing of time, and changes in market conditions to a less favorable environment, EM investors will become more discriminating and inclined to impose more in the way of market discipline on debtors, and debtors may become subject to different influences as they form and implement their economic and financial plans and, if need be, their restructuring strategies. Similarly, changing circumstances may affect judgments about how well the international financial architecture works or how it should be changed.

- (7) Because creditor reactions to a debt restructuring are strongly influenced by how effectively the debtor engages with its creditors, process does matter, though how much it matters may vary depending upon prevailing economic and market circumstances. Clearly, one way to make the restructuring process more 'orderly' (to the extent that is necessary or desirable) is to find mechanisms that encourage such engagement to be as constructive as possible. Because country debt restructurings must be approached on a case-by-case basis, their modalities and outcomes cannot be standardized. This almost inherent lack of uniformity is inevitable and may result in a somewhat ad hoc process that has sometimes seemed unpredictable and therefore disorderly. The starting point in determining how to make the restructuring process more 'orderly' is in recognizing that even countries in financial crisis nevertheless retain considerable power (they are sovereign, after all) to determine how that crisis will be resolved. Because of the limited remedies available, and the tendency of courts to proceed cautiously, even legal actions that may be brought by some creditors against the debtor country seem likely to prove more of a nuisance than a serious disruption. Whether or not a country's policies and actions can effectively prevent an economic crisis, the timing and manner of a restructuring are in many respects within the debtor country's control. While a debtor country may not, under the prevailing architecture, be able to control creditor reactions to its financial crisis and restructuring proposals, such reactions can generally be anticipated and influenced by the debtor country's conduct. This influence over creditor reactions is in part exerted through the debtor country's engagement with its creditors. If there has been a 'hole' in the financial architecture, it was that how (or in some cases, whether!) a debtor country chose to engage with its creditors was too uncertain, and that uncertainty had the potential for resulting in an unconstructive engagement or, even worse, a perceived lack of it at all, as was the case in Argentina.

Frankly, it is hard to evaluate how effective EMTA's efforts were to influence policy in the area of sovereign default, its resolution and burden-sharing. In general, during the period 1999-2007 there was considerable official sector interest in these issues, which resulted in numerous proposals that, without good private sector input, would certainly have created a less favourable legal and contractual environment. Direct input from individual firms from the private sector, invaluable when given, is not always provided (or may not be provided as effectively) for a variety of reasons. Clearly, EMTA played a useful role as an industry resource in soliciting and marshalling industry input, as well as in providing some protection for firms that did not wish to be seen, for whatever reason, to be directly participating in the advocacy process. Equally clearly, EMTA's size, while probably contributing to the nimbleness of some of our responses, put pretty severe constraints on the resources that it was able to devote to this work. It is probably fair to say that, over the years, EMTA developed a certain amount of experience and expertise in this area and with that came some capability as well as credibility. EMTA's views are now widely cited, and sought by members, official sector groups and the media. There are other advocacy organizations, of course, but probably none that was as focused on EM or as responsive to the specific and immediate concerns of EMTA's constituency.

Laying specifics aside, the main lessons that I took away from these aspects of the burden-sharing debate was that the markets work remarkably well to price in risks, and that bond documentation, while important, must be understood in its context—ultimately, documentation is less important than process, and documentation and process together are less important than basic factors such as yields, fundamentals and the overall investment, financial and economic environment. Clearly, CAC's or their specific terms, or other aspects of the broader burden-sharing debate, were simply not to be the tail that wagged the dog, particularly at a time when interest rate levels were at historic lows and many EM countries were earning investment-grade debt ratings.

EMTA's Activities in the FX Derivatives Area date back to late 1995, when an FX working group was formed, initially to look into the standardization of trading forms and market practices for Mexico and Brazil FX transactions, as part of an effort initiated by JP Morgan to reduce a tremendous settlement backlog. Shortly thereafter, EMTA began soliciting opinions of local counsel in Argentina, Brazil and Mexico regarding such matters as onshore and offshore trading restrictions and the extent to which netting was enforceable under local law. As noted above, and in EMTA 1994-98: The Golden Age of EM Debt Trading, the Asian and Russian financial crises established EMTA over the next several years as the forum for developing mechanisms to permit counterparties to allocate Emerging Markets FX risks and settle transactions in the event of market disruptions and for managing the resolution of the crises that resulted when such disruptions occurred. This work created within EMTA great expertise in developing spot and back-up survey rates and procedures that EMTA later used in addressing market closings and other events that arose in Brazil (1999), Taiwan (1999), Venezuela (1999 and 2003), Argentina (2001-02) and elsewhere. Meanwhile, several regional EMTA NDF working groups led by Starla Griffin (nee Cohen) worked for several years on

developing standard templates, market practices and rate-source definitions for NDF's in a number of EM currencies in the LatAm, Eastern Europe and Asian regions (including the Brazilian Real, Hungarian Forint, Taiwan Dollar, Chinese Renminbi, Indian Rupee, Korean Won, Philippine Peso, Argentine Peso and Indonesian Rupiah). When Starla Griffin left EMTA at the end of 2001 (to write a children's book—she later returned to focus mostly on policy issues), EMTA's work in the FX derivatives area became the responsibility of Leslie Payton Jacobs.

In the next five years, the marketplace for Emerging Markets FX products grew rapidly, and by 2005 EMTA had essentially completed developing an architecture (including standard documentation, market practices and user's guides) for trading NDF's and NDO's throughout Latin America (specifically, Brazil, Argentina, Colombia, Chile, Peru and Venezuela) and Asia (South Korea, China, Taiwan, India, Indonesia, the Philippines, Malaysia, Vietnam and Pakistan (though notably not the Thai Baht)), as well as Russia. Primary or back-up FX rate determination mechanisms were developed and implemented for Argentina and Brazil (the mechanism for Russia was revised), many rate definitions were revised and EMTA was employed as the principal forum for addressing unscheduled market closings and other disruptions in numerous countries.

This work was developed organically, as EMTA and its FX derivatives working groups responded to specific market needs as they arose, often in collaboration with other trade groups or service providers (such as the Foreign Exchange Committee in New York, other foreign exchange committees in Singapore, Hong Kong and Tokyo (for the various Asian currencies), the Chicago Mercantile Exchange (mainly in Russia and Brazil) and ISDA). While EMTA developed considerable expertise in the FX area, industry decision-making was spread across various industry bodies and was not particularly transparent, and EMTA, and the industry generally, probably devoted insufficient resources to ensuring that its infrastructure (such as rate determination mechanisms) was adequately automated (or 'fail-safe') to meet best industry standards. Fortunately, during the period in question, none of these rate determination mechanisms, though perhaps vulnerable, was ever tested by a market crisis.

Market Trends Generally; Development of the Local Currency Market. Though much of this description of EMTA's activities during the period 1999-2007 dwells on various market problems, these years were generally prosperous ones for the EM debt trading and investment industry. Investment opportunities abounded, and surging commodity prices and historically low interest rate levels combined to result in rising reserve levels and strong investment flows into the Emerging Markets and generally tightening spreads for many EM debt instruments.

In response to this favorable environment, trading volumes in Emerging Markets fixed instruments generally grew throughout the early 2000's, from a 1999 bottom of US\$ 2.2 trillion to a high of US\$ 6.5 trillion in 2006 and 2007 (before falling off substantially in

2008). More specific information evident from successive EMTA volume surveys showed a steadily declining importance of Brady bonds (Mexico retired its pioneering Brady bonds in 2003, followed by Brazil, Nigeria, Panama, Philippines, Uruguay and Venezuela—even Argentina retired a large percentage of its Brady's as part of its 2005 exchange offer). Increasingly, external currency borrowings were comprised of Eurobonds (whose annual trading volumes peaked at US\$ 2.675 trillion (41% of total trading volumes) in 2006), but the most significant trend was the rapid development of investment interest and trading in local market instruments, as the prevailing economic environment enabled many debtor countries to overcome the “original sin” of borrowing in foreign currency and investors sought yield and became more comfortable with EM policy reforms and fundamentals, local currency FX risks and the enhanced liquidity that accompanied greater investor interest and higher trading volumes. For many EM countries and their investors, it was an era marked by a virtuous cycle. Trading in local market instruments surged from US\$ 1.54 trillion in 2001 (44% of 2001's overall trading volume of US\$ 3.5 trillion) to US\$ 4.264 trillion in 2007 (66% of 2007's overall trading volume of US\$ 6.5 trillion), and many debtor countries generally continued to accumulate reserves that eventually prepared them better than many so-called ‘more developed’ countries for the eventual economic downturn that began in mid-2007 as a result of the subprime mortgage crisis and bursting of the US residential housing bubble. EMTA's volume survey for the fourth quarter of 2007 showed a sharp drop-off in trading volumes (that continued throughout 2008).

During this time, some instruments declined in importance or disappeared almost entirely (loans gave way to Brady bonds and Warrants by the mid-1990's, with sovereign Eurobonds gradually replacing the Brady's by the mid-2000's), while others once seen as novel or problematic became much more prominent or popular (local market instruments generally, as well as corporate bonds and GDP-type instruments). At the same time, investment ratings climbed throughout this period, with a number of countries (such as Mexico (2000-2002), Russia (2003-2005), Brazil (2008) and Peru (2008)) reaching investment grade (though not entirely graduating from EM), while others (such as Argentina, Ecuador and Venezuela) seemed mired in credit doldrums mostly of their own making.

With this evolution of the market came significant changes in EMTA's work (particularly as it involved the sellside). Some problems were solved or just went away; others emerged. In their day, EM loans and Brady bonds (with their related Warrants) generated the need for a lot of documentation and market practices, which over the years required considerable follow-up attention (mostly provided by Aviva Werner). Local Markets instruments and corporate bonds tended to develop with less need for this type of standardization. An important outgrowth of this evolution was the extensive work that EMTA took on in the general area of investor rights (as discussed above), and, to a lesser extent, in the so-called Frontier Markets that were developing in Africa and around the periphery of the relatively well-developed Emerging Markets. EMTA's work in the FX area, on the other hand, has tended more to follow the Brady bond

model of requiring extensive standardization of legal documentation and development of market practices and infrastructure.

One area in which EMTA's activities grew substantially was in the presentation of events designed to provide a forum for the discussion either of country developments and prospects or of specific topics thought to be of particular interest to EM market participants. Of course, EMTA's annual meeting in NYC dated back almost to its earliest years, and various programs relating to EMTA projects (the so-called open meetings) occurred regularly, particularly in EMTA's early years. In 1998, EMTA launched its Summer Forum in London, an effort to respond to the needs of London market participants for a forum similar to that provided by the annual meeting, as well as to address uniquely London-oriented investment opportunities. A London Winter Forum was added in 2004, giving EMTA an annual line-up of seasonal forums, which included Spring and Fall Forums in NYC. Responding to regional interest, two Asian forums (Singapore and Hong Kong) were launched in 2006 and two LatAm forums (Sao Paulo and Buenos Aires) were initiated in 2008. A special effort was made throughout this period to present topical presentations of particular interest to investors, and after years of insisting that EMTA was not in the business either of giving parties or promoting charities, EMTA (largely through Jonathan Murno) began to sponsor EM industry benefits in both NYC and London.

In mid-2003 EMTA initiated a short-lived effort to collect and publish CDS and NDF volume information, comparable to its traditional survey of fixed income trading volumes that dates back to 1992. By year-end, however, the effort was suspended, and then abandoned in late 2005, when it became apparent that EMTA was not receiving sufficient reports from market participants to produce credible industrywide CDS and NDF volume surveys. Feedback from several major market participants among EMTA's membership indicated that, at the time, the potential results did not justify the dedication of the necessary resources to collect and report the data to EMTA. We continued, however, to believe that this data was valuable in the interest of promoting market transparency, and the effort was put on the back burner for later development (ultimately the EM CDS survey was restarted in 2010, with hopes that the NDF survey would follow shortly).

EMTA's Leaders from 1999 through 2007. Of course, there have always been great traditions of leadership (and change) in the Emerging Markets trading and investment community, and this period was no exception. Many of EMTA's founding Directors stepped down from EMTA's Board during the mid-1990's (notably, several others continued to serve for a few more years or longer, as noted below), but their successors were in many cases already industry leaders in their own right, having played prominent roles on early EMTA committees and working groups, and in the marketplace, in helping to establish market practices and standard documentation during EMTA's formative and

early years. EMTA and the EM trading and investment industry owe a great debt of gratitude to them for their leadership, wisdom and hard work on EMTA's behalf.

Leaders on EMTA's Board of Directors during the period 1999-2007 included the following, many of whom are still active in the markets today (though in many cases, not at their original sellside firms):

Guido Mosca (JPM) assumed the Board seat originally held by EMTA founding Director Nicolas Rohatyn and served on the Board from 1996-2000 (and as Co-Chair in 1999 and before that, as a vigilant Board Treasurer for several years). Among other things, Guido was always a forceful advocate for the high road (as well as principal advocate of the school of thought that EMTA should not be in the business of throwing parties) .

Paul Masco (Salomon Brothers) replaced Mark Franklin and served on EMTA's Board from 1994-2000 (and as Co-Chair in 1999). Paul also served on the Board of Directors of the Emerging Markets Clearing Corporation. Among other things, it was Paul who most impressed on EMTA staff the need for EMTA to always strive to represent both sellers and buyers in the marketplace.

Modesto Gomez (Chase/JPM Chase) assumed the Board seat held by Jorge Jasson and served as EMTA Co-Chair from 1999-01, and encouraged the development of many of EMTA's local markets activities.

Juan del Azar (Merrill Lynch), who managed Merrill's global EM trading and sales business for many years, served on EMTA's Board of Directors from 1998-2007 (and as Co-Chair from 2000-06). During times of market convergence, Juan was a consistent and forceful advocate for EMTA and the EM trading and investment industry.

Mark Coombs (Ashmore), EMTA's longest-serving Director, has served on EMTA's Board of Directors from 1994-2010 (from 1994-99 on behalf of the sellside firm ANZ and since then, on behalf of his buy-side firm Ashmore). Since 2001, Mark has been an EMTA Co-Chair, providing much of the continuity that has characterized EMTA's philosophy and activities over the years.

George Grunebaum (JPM Chase), a trader's trader, served as an EMTA Co-Chair from 2002-05.

Steve Kenny (UBS) served as a Co-Chair from 2004-06.

Bo Bazylevsky (JPM Chase) served as a Co-Chair from 2005-06.

Martin Marron (JPM Chase) joined EMTA's Board in 2007 and served as Co-Chair from 2007-2010.

Matt Clinton (Lehman) served as Co-Chair (and also Board Treasurer) from 2007-09.

Among others, the following Directors also served notable terms on EMTA's Board of Directors during this time:

Peter Geraghty, an EMTA founding Director (then from NMB), also served as a Director from 2005-08 from Dresdner Kleinwort, 2000-03 from Darby and 1994-97 from ING and ING/Barings, and from 1994-97 was an EMTA Co-Chair or Vice-Chair. Among other things, it was Peter who first articulated the EMTA mantra that the Emerging Markets were a "state of mind."

Bruce Wolfson has served as an EMTA Director since 1995 (1995-2004 from Bear Stearns and 2005-10 from The Rohatyn Group). One of EMTA's longest-serving Directors (along with Mark Coombs and Peter Geraghty), Bruce's legal judgment was a guiding force in the development of EM standard documentation and market practices.

Ruth Laslo (UBS) served on EMTA's Board of Directors from 2003-04 and 2006-07. She also has served as Board Treasurer and as a long-time alternate Director who has played a leading role in the development of EMTA's FX and derivatives activities.

Dean Menegas (Spinnaker) replaced Alexis Habib and has served on the Board of Directors from 2002-2010 (and as a Vice-Chair from 2005-10). Dean has been instrumental in providing EMTA with expert legal advice and European market perspective.

Manuel Mejia-Aoun, also a founding EMTA Director, served on EMTA's Board of Directors from 1999-2000 while he was at Deutsche Bank and before that, from 1990-95 while he was at Merrill Lynch.

Gail Segal replaced Alex McLeod on EMTA's Board on behalf of Bank of America and served from 1997-2000.

Abigail McKenna (Morgan Stanley Investment Management) served on EMTA's Board of Directors from 2001-04. Abby is well-known for her leadership of the EM investment community.

Keith Gardner (Western Asset Management) has served on EMTA's Board of Directors from 2001-10, and, with Abby, was a leader in EMCA's efforts to promote investor rights.

Mohamed el-Erian (PIMCO) served on EMTA's Board of Directors in 2001.

Mike Gagliardi served on EMTA's Board of Directors from 2002-09 on behalf of TC Atlantic and Halbis, and before that in 1999 on behalf of Wasserstein Perella. Mike participated in many EMTA Forum panels, always preceding his accurate market



predictions with the phrase “I could be wrong, and a lot of you are a lot smarter than I am, but...”

Fran Bermonzohn (Goldman Sachs), a former general counsel of the Public Securities Association (a predecessor of TBMA and SIFMA), served on EMTA’s Board of Directors from 1999-2002.

Brian Lazell (BNP Paribas), for many years a leader of ISMA and ICMA market practice committees, served on EMTA’s Board of Directors from 2000-2002.

Alexis Habib served on EMTA’s Board of Directors from 1995-2002 on behalf of Indosuez Capital, Credit Agricole and Spinnaker Capital.

Richie Prager served on EMTA’s Board of Directors from 2000-03 on behalf of Bank of America.

Diego Ferro (Morgan Stanley) served on EMTA’s Board of Directors from 2003-07.

Diego Gradowczyk (Barclays Capital) joined EMTA’s Board of Directors in 2004 (eventually becoming Co-Chair from 2009-10).

Last, but not least, Francis McGuinn served on EMTA’s Board of Directors in 2000 and 2001 on behalf of Canter Fitzgerald (tragically passing away at their offices on September 11, 2001).

Other Directors who served on behalf of their firms as EMTA Vice-Chairs during this time included Andy Alter (2000-05 from Salomon Smith Barney and Citigroup), Gaby Szpigiel (2001-03 from Deutsche Bank), Kay Haigh (2004-09 from Deutsche), John Cleary (2001-03 from INVESCO and 2004-06 from Standard Asset Management), and Mohammed Grimeh (2004-06 from Lehman Brothers).

In Conclusion. As noted above, the growth of Local Markets investment interest and trading activity has not been accompanied by the same degree of need for standardization that typified the development of the market for Brady bonds (and that characterizes the EM FX derivatives market), so there has been some shift in the orientation of EMTA’s work, at least in the fixed income area, away from the development of documentation and market practices and toward more general policy issues (such as maintaining a level playing field for foreign investors). Whether this continues to be the case is probably anybody’s guess.

Despite the change in the nature of EMTA’s workload, what has tended to stay more or less the same over the years is that (1) EM itself has remained somewhat separate from other business areas (despite some mainstreaming of EM into the broader investment business, EM continues to require some skills, attitudes and attention distinct from the

mainstream), (2) buy-side issues involving credit and investor rights seem to transcend the ebb and flow of differing instrument types and (3) there is a continuing need for institutional memory, expertise and coordination that cannot be met entirely from within the industry itself.

When asked what EMTA does, my typical response (based on the diversity of market circumstances and their effect on EMTA's activities) is to say that EMTA is the EM debt community's "clubhouse" and "firehouse". Clubhouse in the sense that EMTA provides the main forum for members of the industry to gather, sometimes just to socialize but most often to discuss and debate industry developments and prospects, and firehouse in the sense that, though the Emerging Markets and the EM debt trading markets have prospered in ways that the LDC debt traders of the late 1980's could scarcely have imagined, there are still occasional market events or "situations" that require the industry to mobilize a response. In many cases, EMTA provides the 'first responders' to such market situations.