

Vultures show Argentina no mercy

By Sabri Ben-Achour

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"Vulture funds" earned their nickname because they are, in a sense, scavengers.

They go after the debt of dying firms or crisis-addled countries, buying it on the cheap when nobody thinks it'll get paid back and many other creditors have given up and agreed to accept pennies on the dollar. Then, they sue to get it paid back in full. This can result in a situation where a vast majority of original creditors have agreed to accept a fraction of their original debt, leaving the vulture minority to win big. For example, in the current dispute between a group of investors and Argentina, a firm called Elliott Capital Management purchased Argentine debt for \$48.7 million and is now seeking payment of \$832 million.

"These firms profit from the backs of poor people," says Eric LeCompte, executive director of Jubilee USA, a religious organization that lobbies for debt relief for poor countries and international financial reform. "One of the most tragic recent examples is money from debt relief was sent to Zambia, but that money for schools and hospitals was collected by vulture funds."

Funds have been aggressive in using whatever legal means they can to ensure full repayment of sometimes decades old debt. In 2010, Elliott Capital Management convinced a court in Ghana to bar an Argentine navy ship from leaving that country as a way to extract the money it says it is owed. Such examples are extreme and give a bad name to what is otherwise a simple case of enforcing commitments, argues Edward Altman, professor of finance at New York University's Stern School of Business.

"Asking for full payment is totally appropriate," he says. The original owners of a country's securities are ill-equipped to negotiate when those countries renege on their commitments, and the vultures have the appetite and ability to play hardball.

Like vultures in the wild, vulture funds may serve an important ecological purpose.

"They provide in the case of distressed assets a liquidity that simply wouldn't be there," he says. (In other words, it's helpful to have somebody out there who will buy bad debt.)

There's a hole in international law

Whether morally bankrupt or legally secure, the reason why vulture funds can operate in the first place and why there is such controversy around them boils down to a hole in international law: There is no bankruptcy court for countries.

"When you, or I, or General Motors runs out of money, we can file for bankruptcy and there's somebody to oversee that process," explains Anna Gelpern, professor of law at Georgetown University and a senior fellow at the Peterson Institute for International Economics. "When a government runs out of money there is no such process, all you have are a bunch of contracts and it's every person and fund for themselves."

Theoretically, it's possible to write contracts when bonds are issued that lay out what happens in the case of a default. For example, to set out in the contract that if 90 percent of creditors agree to accepting 30 cents on the dollar, it applies to all creditors. The problem, of course, is that nobody wants to talk about default when they issue a bond. Bankruptcy laws get around this problem by laying out rules in law. No such luck for countries.

Over the years, an informal system developed whereby countries would get a majority of creditors on board with restructured debt when defaults occur. But the Argentina case, the firms who sued "have thrown a big wrench in the process of coming up with a methodology for an orderly resolution of countries with debt problems," says Barry Bosworth, senior fellow at the Brookings Institution. Gelpern points out that as firms and countries fight through international legal and financial systems, it's banks and financial institutions that suffer jabs and bruises along the way.

"You can't make Argentina do anything, but by golly, you can threaten anyone who has anything to do with Argentina," she says. "Going forward, countries will find it harder to restructure their debts, creditors will have to think about risk more carefully when getting involved with countries that are in trouble."