Two centuries of Latin American external debts, 1822-2010: loan booms, debt crises, normal bankers and vultures.

A long term historical perspective

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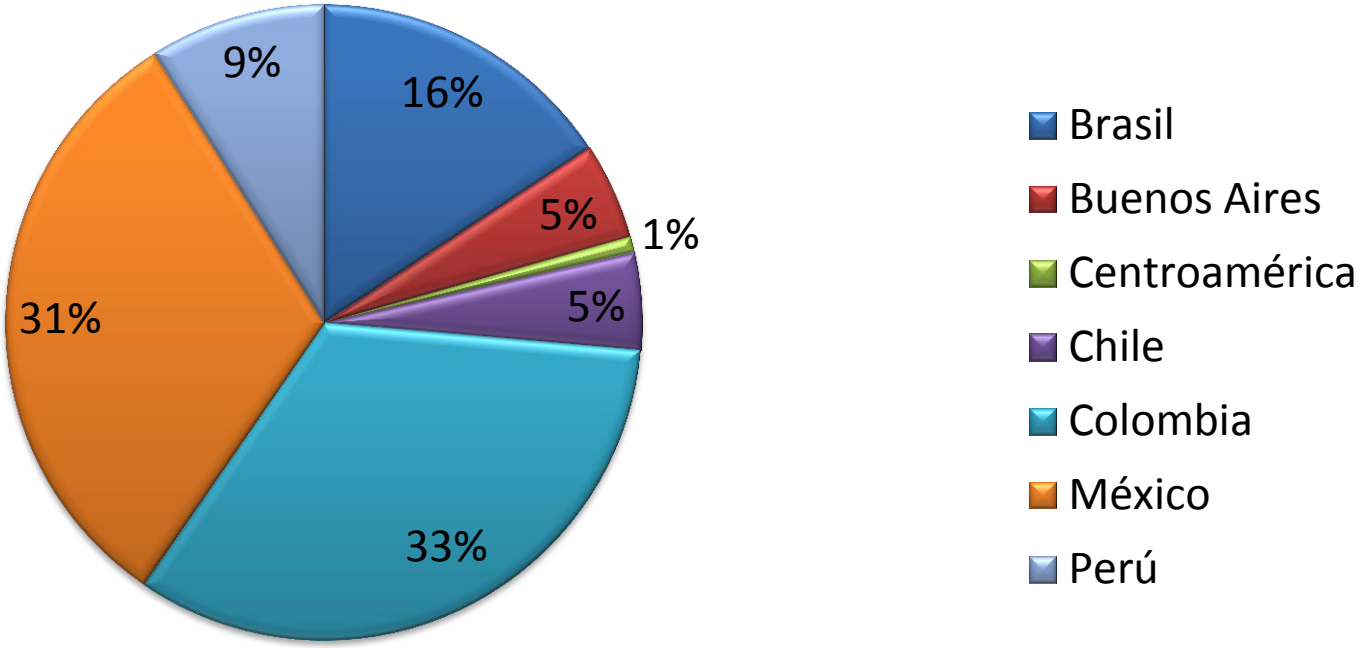
The origins of external sovereign debts, 1822-1825

- **When did external sovereign debts originate?**

- European merchant bankers in the eighteenth century provided some loans to monarchies. But modern external sovereign debts really came to the fore in the years 1822-1825.
- Most of these loans to the new Latin American republics, to the emerging Greek nation state, as well as to Spain, Denmark and Russia, were issued in London in pounds sterling.
- **The early loan contracts and bonds set the pattern for *two hundred years* of sovereign debt issues.**

Issue of sovereign external bonds in London by newly independent Latin American governments, 1822 - 1825



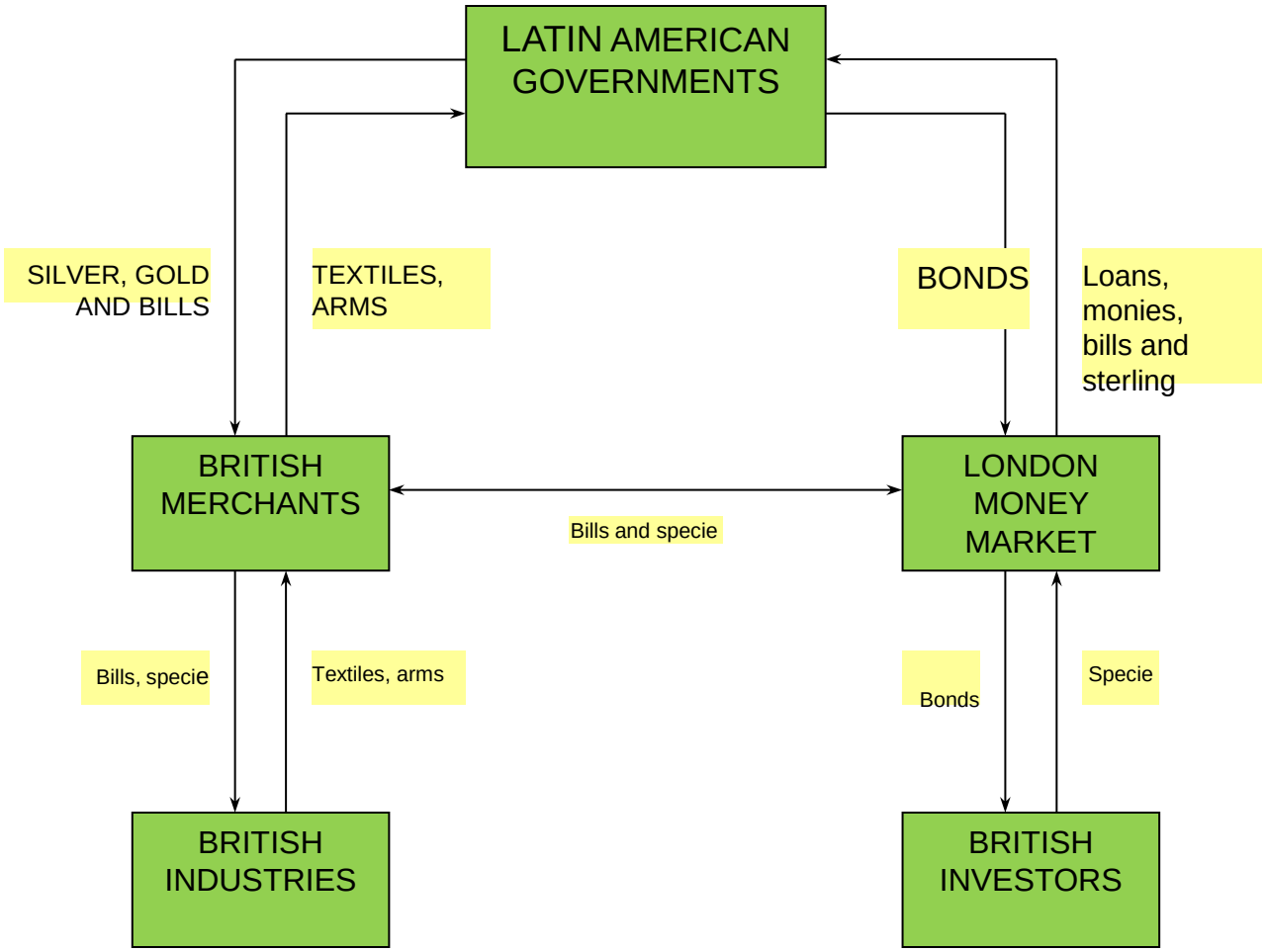
Monto total = 20,329,300 £

London Bridge, 1825,

(engraving in the library of Bryn Mawr College)

MERCANTILE AND FINANCIAL RELATIONS BETWEEN GREAT BRITAIN AND LATIN AMERICA IN THE EARLY 1820'S

Pattern of flows of Specie, Bills, Loans and Merchandise



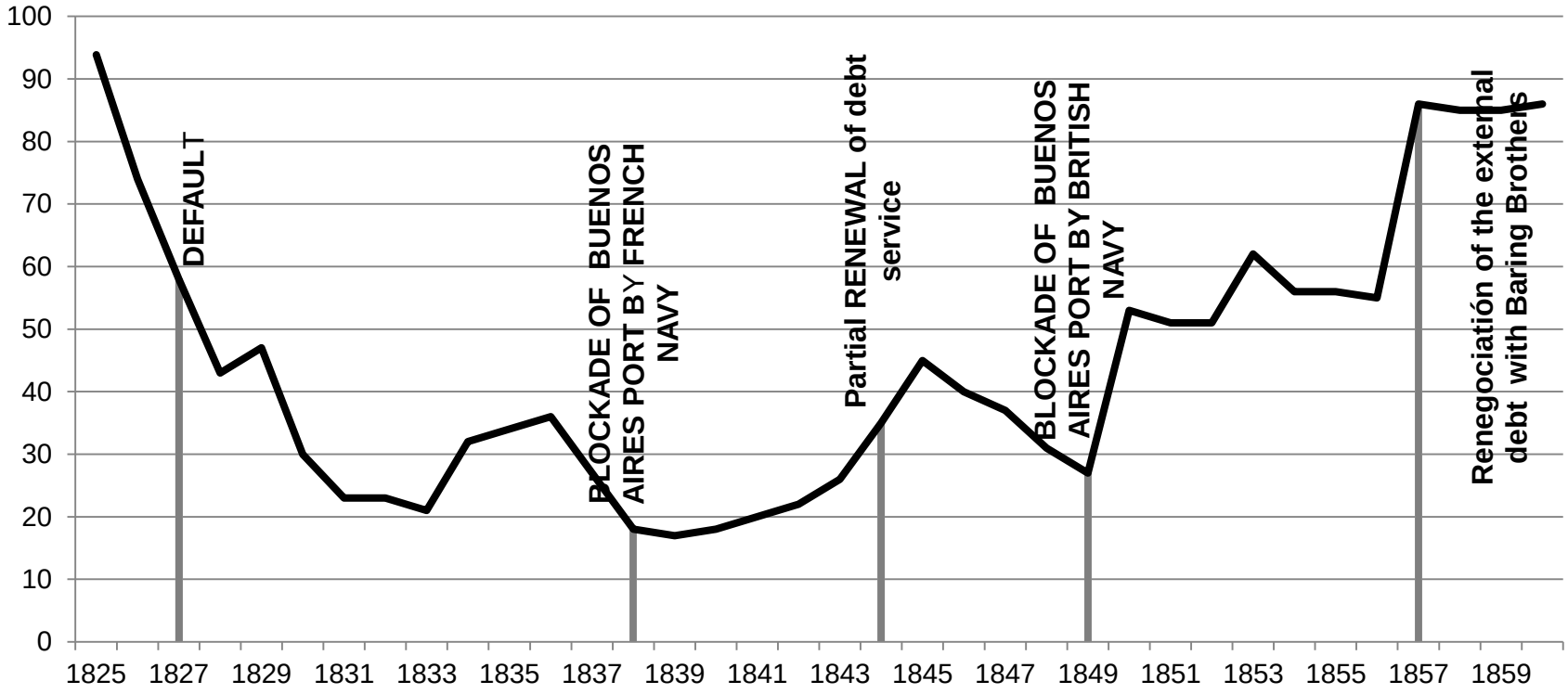
The origins of debt defaults

- In the *ancien regime, some* absolutist monarchies suspended payments on their debts to private bankers.

- But the first suspensions of payments on external sovereign bonds came after Latin American independence in the years 1826/1827 **as a result of the financial and trade crisis that broke in London in January 1826 and spread internationally.**

- **Spanish American governments had insufficient fiscal resources to cover payments and practically defaulted, and remained in default for decades**.

Argentina external bonds quotations on the London Stock Exchange, 1825-1860



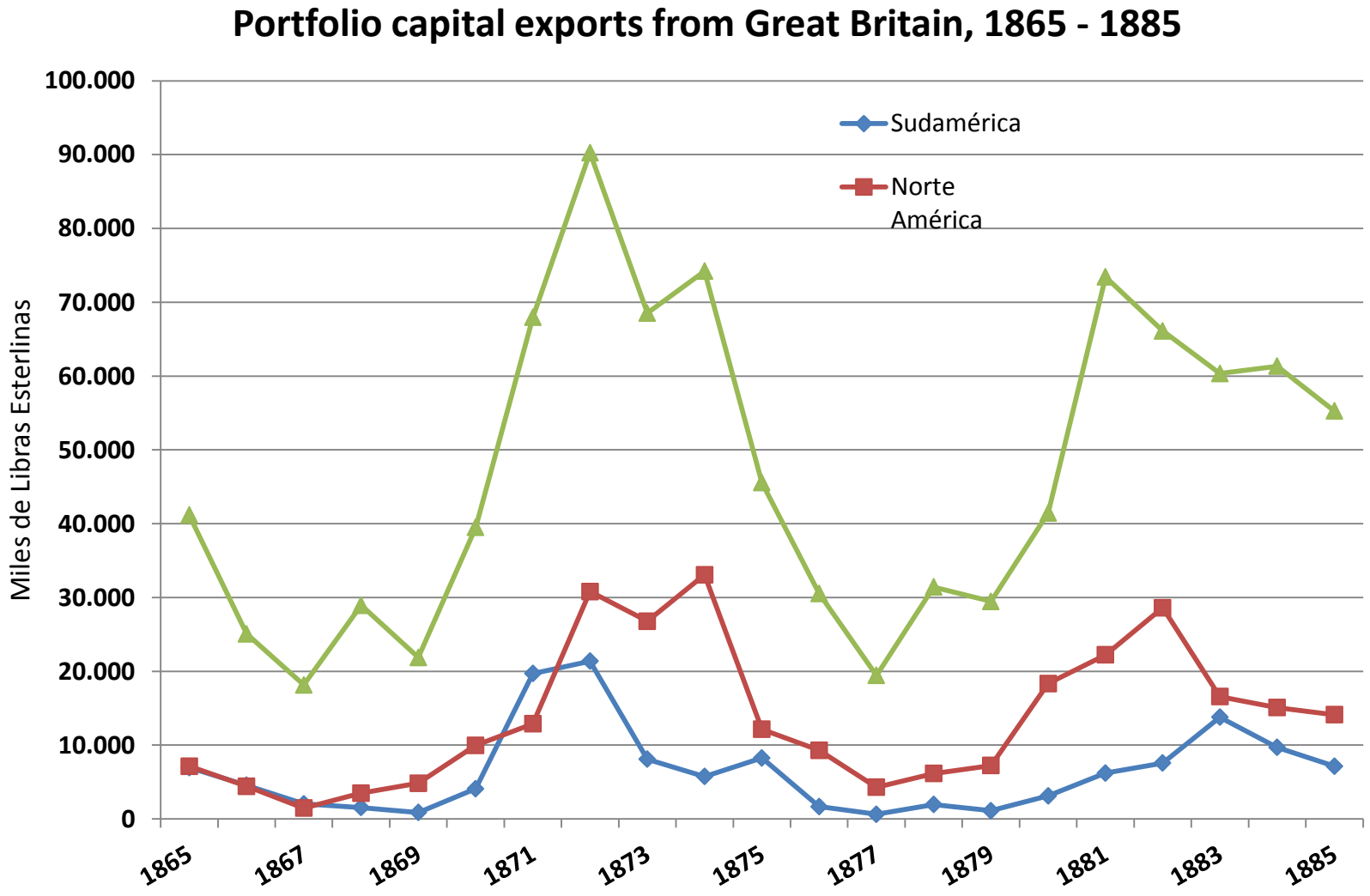
Fuente: Pedro Argote, *Informe del Presidente del Crédito Público...*, vol. IV, pp. 96-98, Buenos Aires, 1887

The origins of financial “vultures” and Latin American sovereign debt defaults in the 19th century

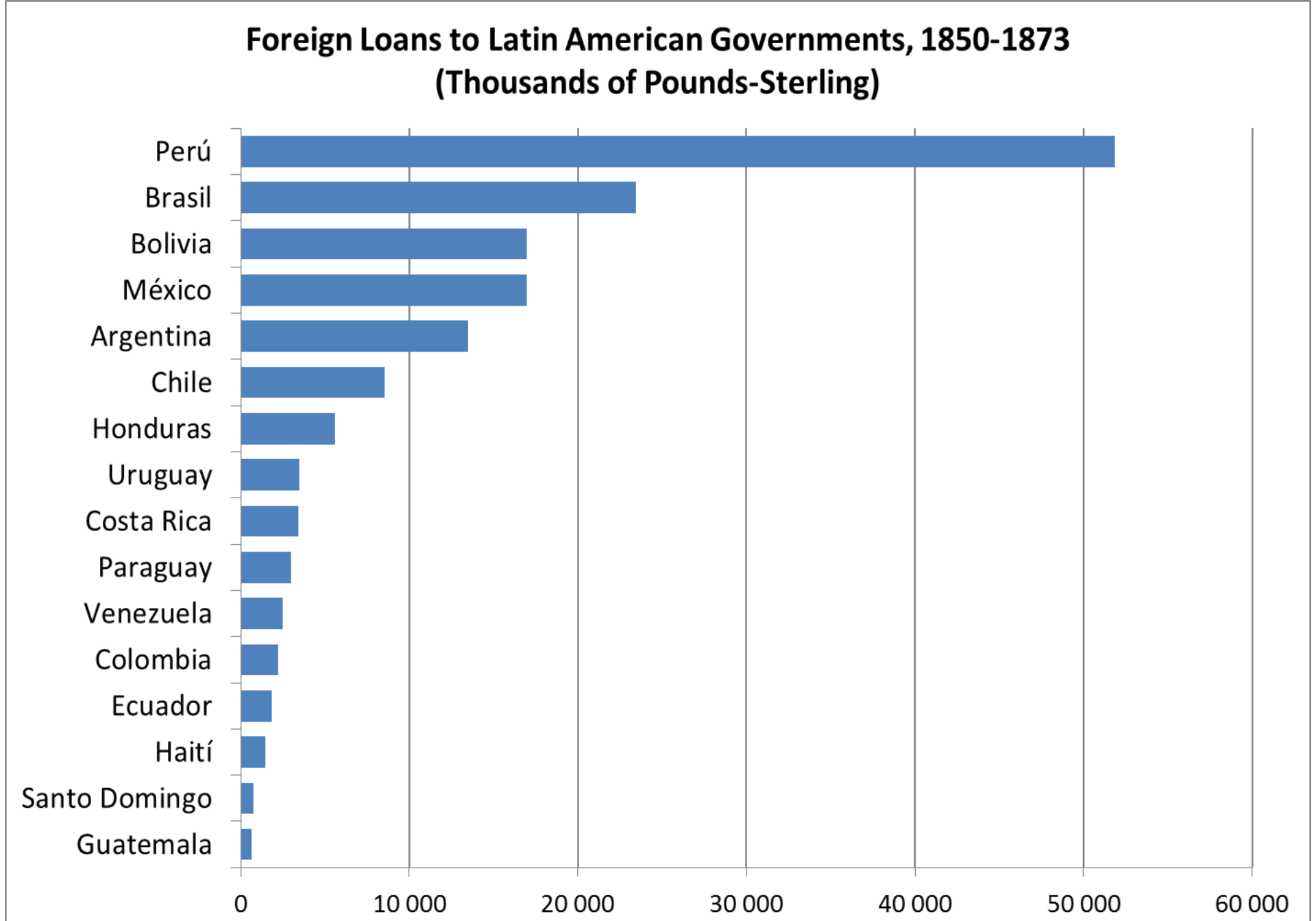
- The first instance of financial “vultures” can be found in the 1830s in the period that followed the first defaults.
- Who were the vultures?
- Basically unscrupulous London financial firms that wished to buy Latin bonds on the cheap and then resell much higher if renegotiations played out to their advantage.
- The bondholders sold a great part of their bonds in the 1830s and 1840s when they saw that it would be difficult to get their money back. Here the vultures entered the scene!

The loan boom of 1850-1873: *the birth of financial globalization*

- The trade boom of the 1850s in the Atlantic world, North and South, as well in the Pacific, led to an international loan boom, which marked the first sustained flows of international capital flows.
- The largest receptors of portfolio flows in North America were the US railroads, and in South America, domestic governments which took loans for wars, public works, state railroads and refinance.
- This great loan boom came to a halt as a result of the
- International crisis of 1873.

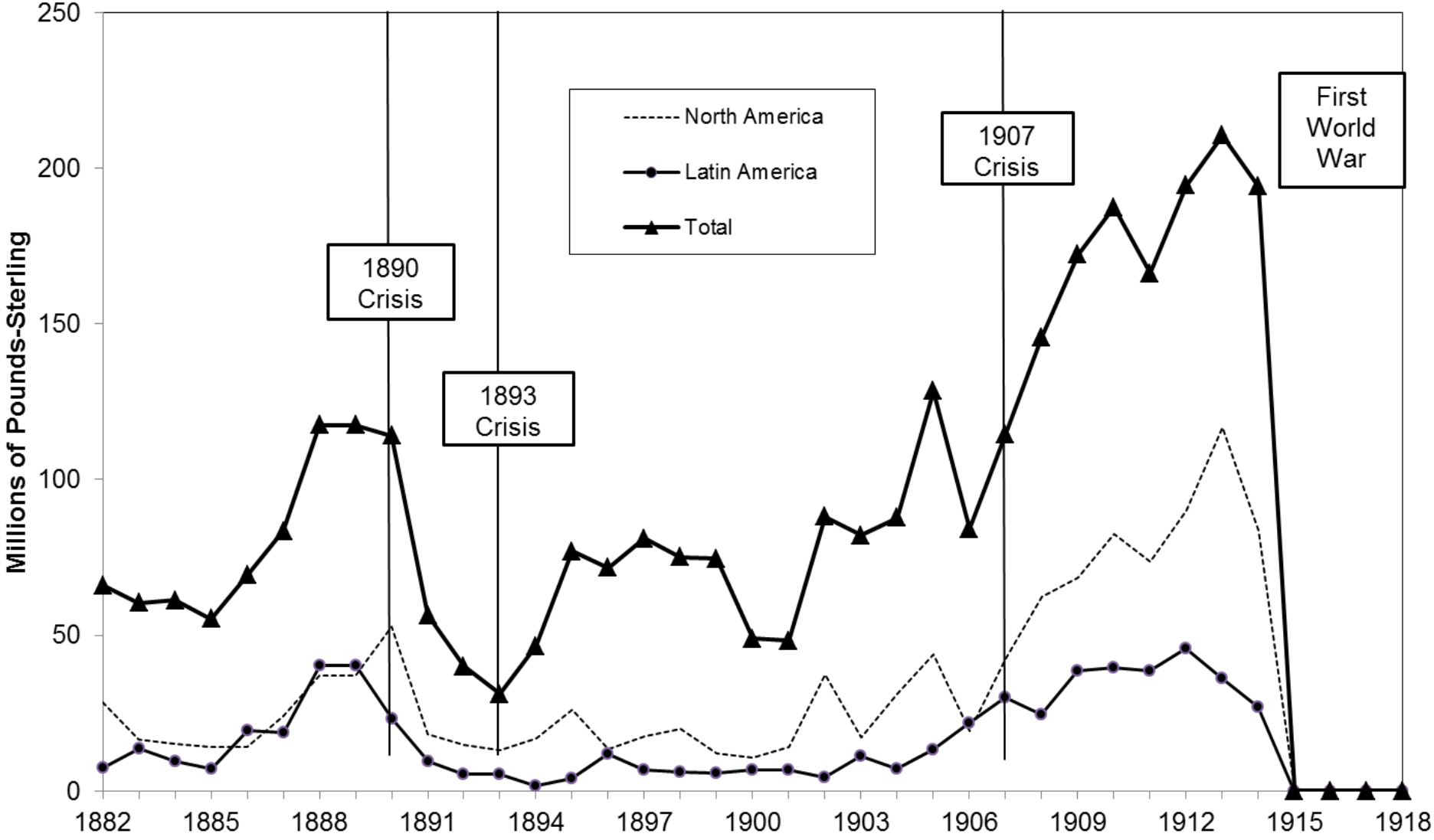


Fuente: Stone, Irving (1999) The Global Export of Capital from Great Britain, 1865-1914. A Statistical Survey, New York, Macmillan/St. Martin´s Press



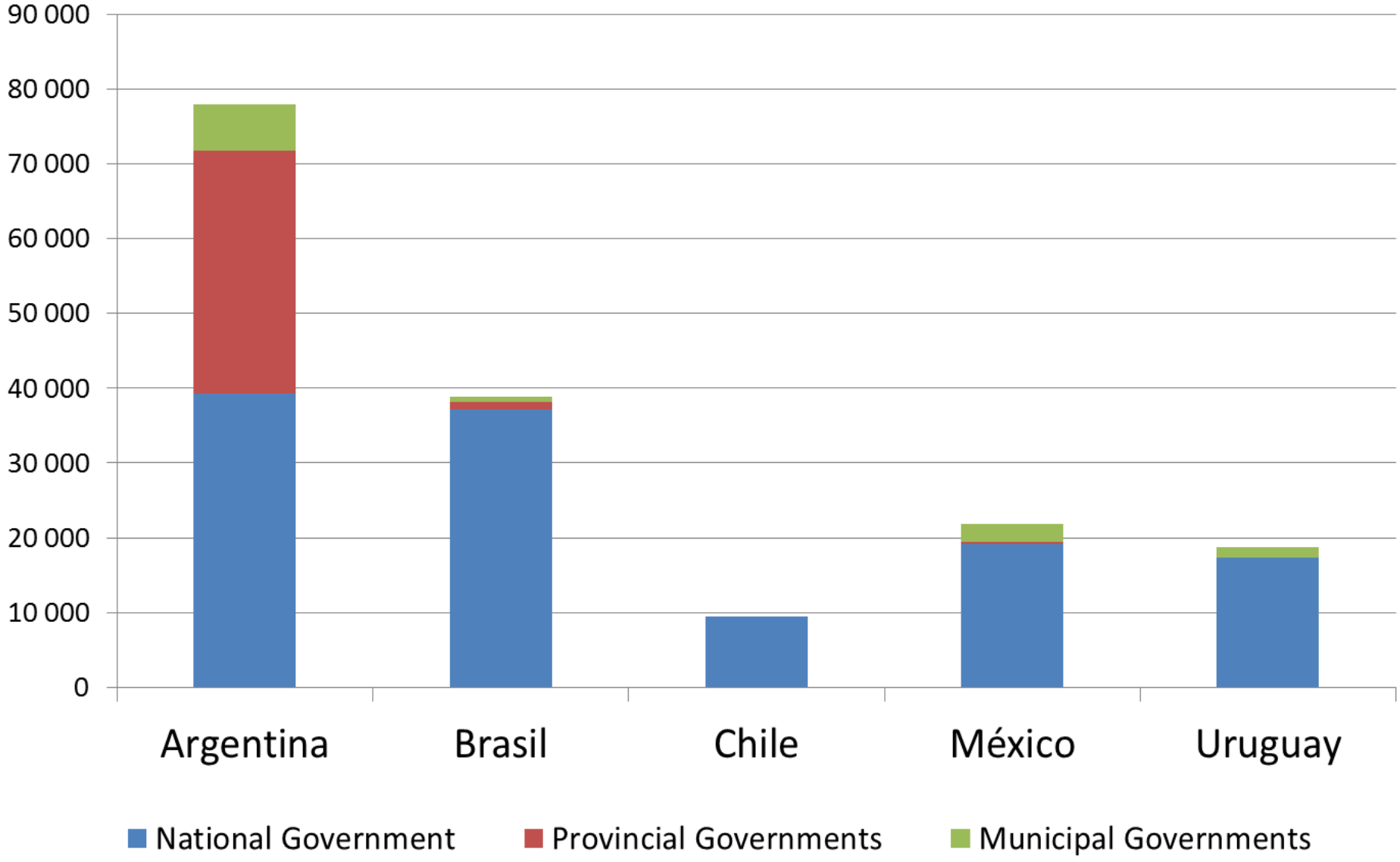
Source: Corporation of Foreign Bondholders, Annual Reports, 1873-1880; C. Fenn, A Compendium of the English and Foreign Funds; Irving Stone, "The composition and distribution of British Investments in Latin America, 1865-1913".

Capital Exports from Britain, 1882-1918



Note: North America refers to Canada & the USA. **Latin America** includes México, Central America, the Caribbean, and South America. **Total** includes British capital exports to North America, Latin America, Europe, Asia, and other regions.
Source: Irving Stone. *The Global Export of Capital from Great Britain, 1865-1914: a Statistical Survey*.

Foreign Loans to Five Latin American Countries, 1880-1890. Thousands of £.



The Baring Crisis of 1890 and Argentina

- In 1890 Argentina suffered a severe financial collapse, that included a banking collapse, a stock market panic, and a debt crisis.
- Baring Brothers, a leading London merchant bank, was menaced and had to be rescued by a syndicate of banks, supported by the Bank of England.

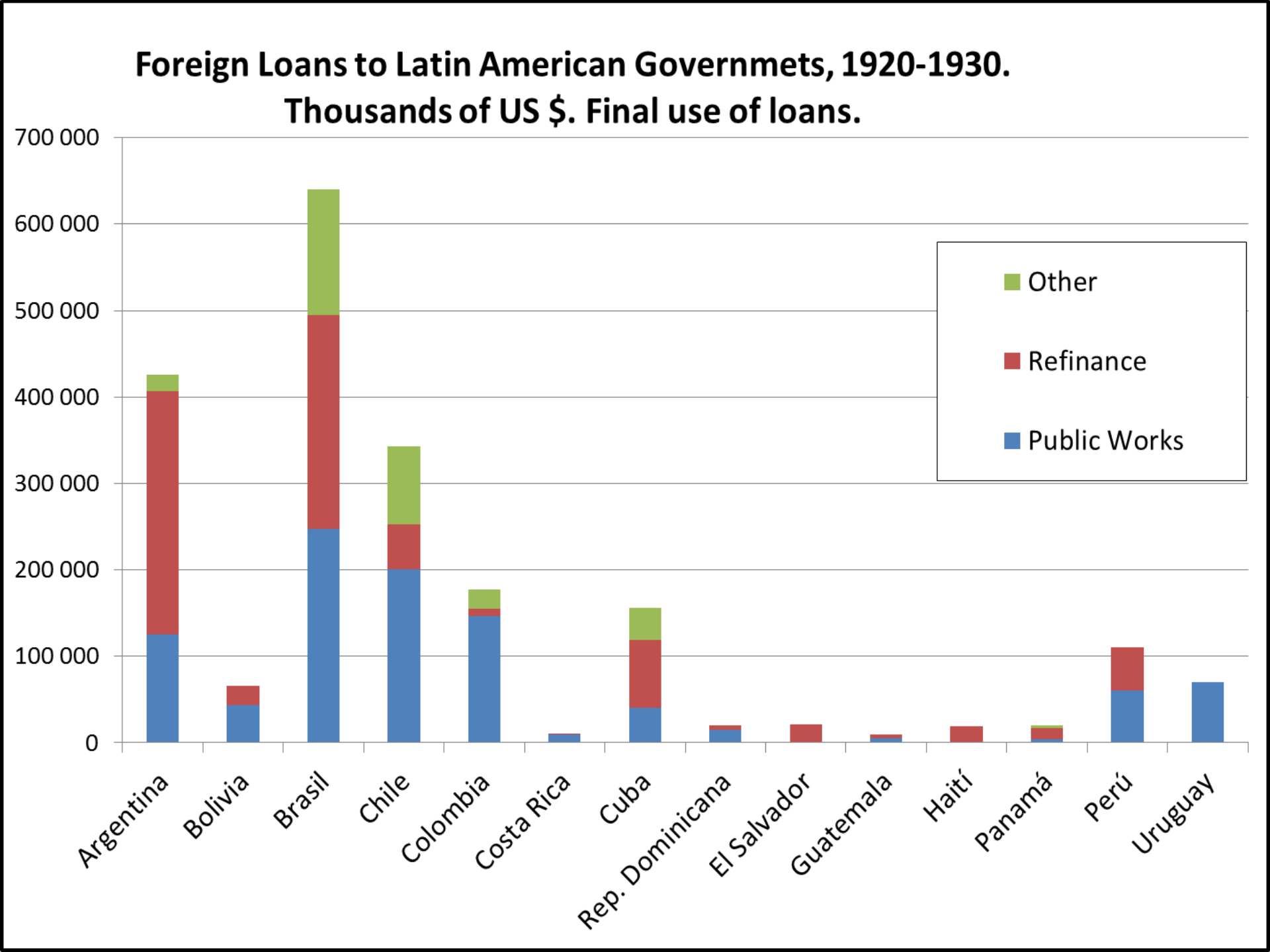
- In recent years, Eichengreen and others have rebatized this as an early “emerging makerts crisis”

- The volatility was contagious and also spread to Brazil where there was a grave financial crisis in 1891.
- Vultures, however, did not proliferate, and the complex rescues were handled by the leading international banks.

The loan boom of the 1920s

- After the First World War there was a new loan boom, mainly of placement of sovereign bonds of Germany and of Latin American governments by New York banks.

- Why virtually all Latin American governments participated in the loan boom at the same time is an open question, which should also be asked when analyzing later loan booms such as that of the 1970s


Foreign Loans to Latin American Governmets, 1920-1930.
Thousands of US $. Final use of loans.
700 000
600 000
500 000
400 000
300 000
200 000
100 000
0
Other
Refinance
Public Works
Argentina
Bolivia
Brasil
Chile
Colombia
Costa Rica
Cuba
Rep. Dominicana
El Salvador
Guatemala
Haití
Panamá
Perú
Uruguay

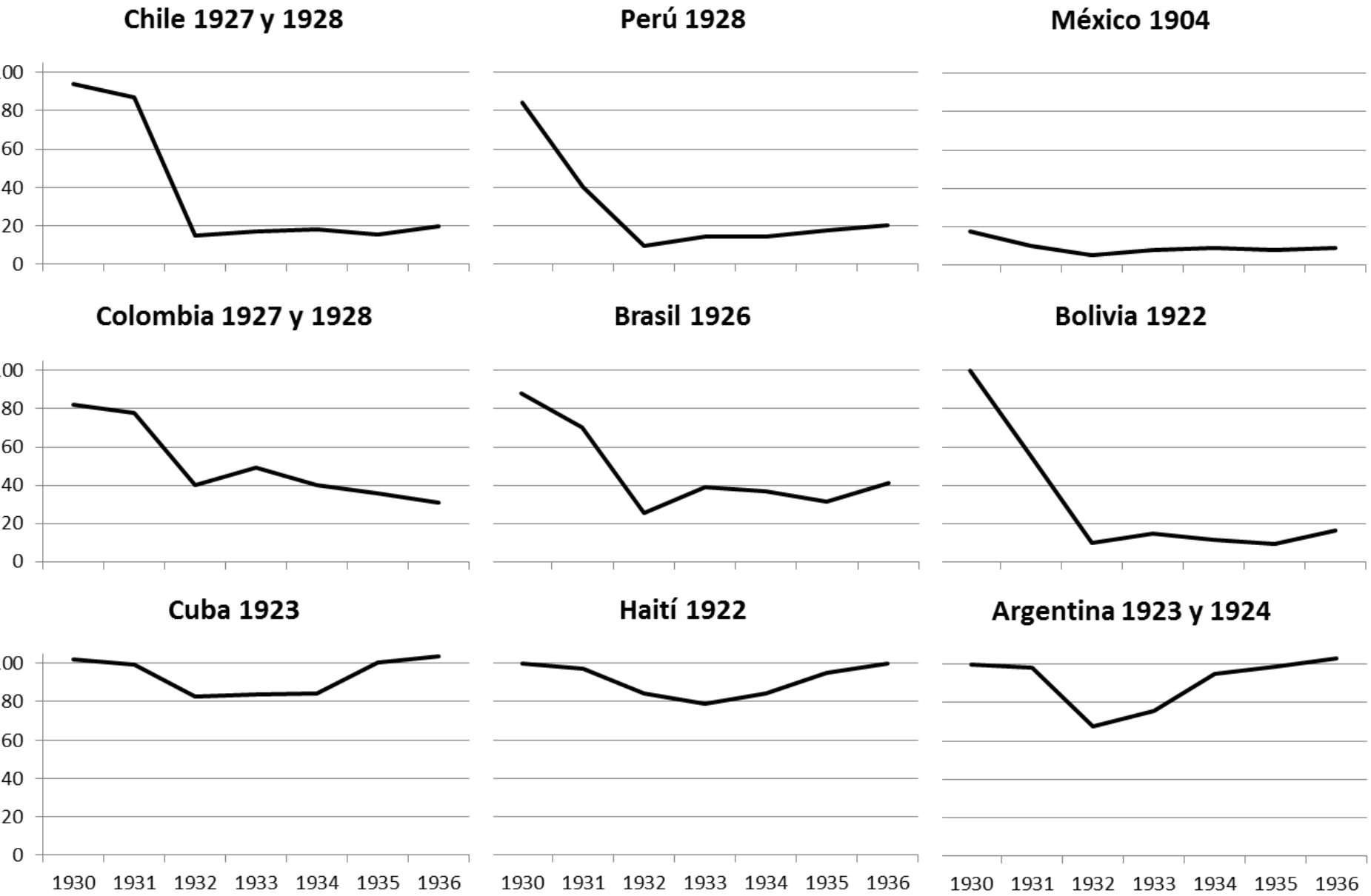
The crash of 1929 and the Great Depression of the 1930s

- As a result of the stock market crash in New York in 1929,, other markets also began to confront problems, which however took longer in becoming critical.

- Many countries, including Great Britain went off the gold standard and thus ended the era of iberal capitalism. **Most Latin American governments suspended payments on their debts in 1931-1933, except – curiously enough- Argentina, Cuba, Haiti and Santo Domingo which did not.**

- Renegotiations were prolonged on most sovereign debts and did not end until after Bretton Woods, usually with direct financial diplomacy between the United States and Latin American governments.

Market Prices of Latin American Gold Bonds on the New York Stock Exchange, 1930-1936*



*Based on highest prices of the year.

Source: Foreign Bondholders Protective Council, *Annual Report 1936* (Nueva York, 1937)

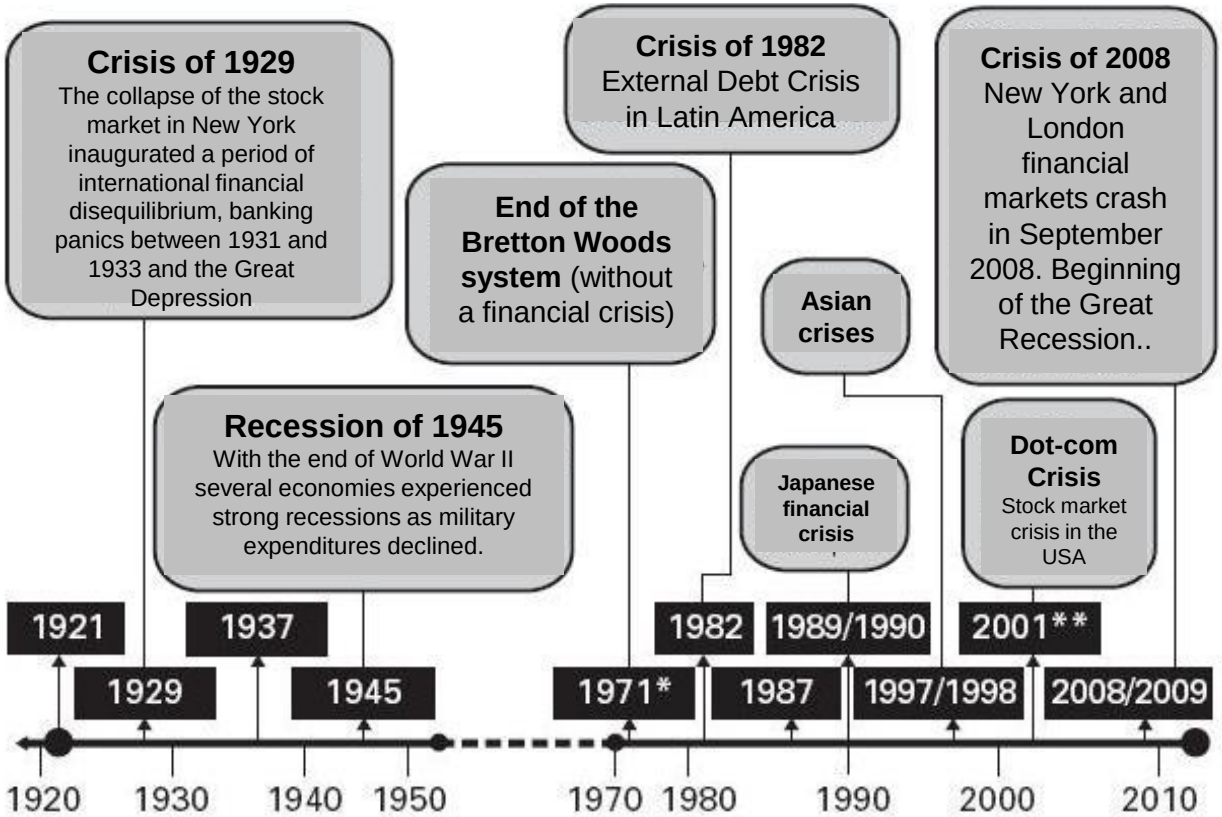
Nueva historia de

LAS GRANDES CRISIS FINANCIERAS

Una perspectiva global 1873-2008

Diagram 2

Financial Crises of the 20th and 21st Centuries



Source: Author's own elaboration based on Carlos Marichal, *Nueva historia de las grandes crisis financieras. Una perspectiva global, 1873-2008* (Madrid/Buenos Aires/México: Debate, 2010): 35, available at http://www.historiadelascrisis.com.mx/attachments/DIAGRAMA2.JPG (accesed on April 26th, 2012)

LONG-TERM LATIN AMERICAN EXTERNAL DEBT
1945-1970
(Millions of Dollars)

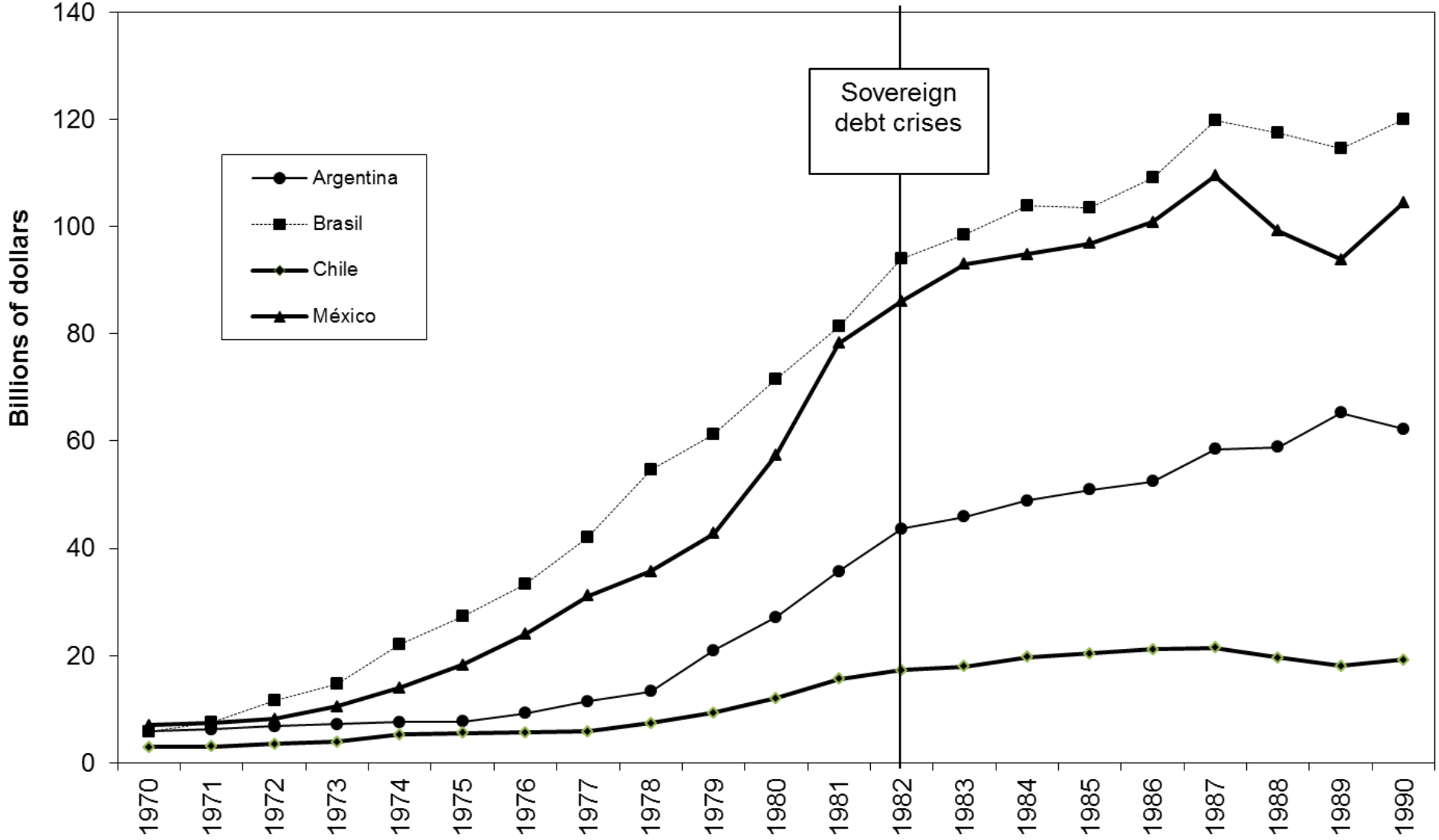
Country	1945	1950	1955	1960	1970
Argentina	900.	400.	600.	1 478.1	1 880
Bolivia	61.	50.	93.1	199.8	480
Brazil	432.7	409.4	1 380.3	1 823.9	3 421
Chile	425.9	355.4	350.7	565.9	2 067
Colombia	171.4	157.5	276.2	376.8	1 297
Costa Rica	14.	12.	36.	56.1	134
República Dominicana	12.	10.	-	5.7	212
Ecuador	24.2	31.9	67.6	100.8	193
El Salvador	13.4	22.4	28.4	33.3	88
Guatemala	.9	.4	22.2	53.5	106
Haiti	15.2	8.3	39.6	39.7	40
Honduras	5.4	1.3	4.7	23.6	90
México	540.	509.1	478.9	1 038.4	3 196
Nicaragua	5.8	4.6	23.1	41.1	147
Panamá	15.6	13.	18.1	58.4	194
Paraguay	15.8	15.3	22.1	22.3	112
Perú	104.8	107.2	229.1	268.1	856
Uruguay	153.4	105.5	126.6	131.8	269
Venezuela	-	-	249.8	314.1	728
Total	**2 911.5**	**2 213.3**	**4 046.5**	**6 631.4**	**15 510**

Source: M. Avella, "El acceso de Colombia al financiamiento externo durante el siglo XX. Una sintesis.", Bogotá, Banco de la República, Subgerencia de Estudios Económicos, *Borradores de Economía*, no. 387, 2006.

The loan boom of 1970s and debt crises of 1980s

- The international loan boom of the 1970s in Latin America, marked a first phase of the new financial globalization, led by big international banks.
- The loan boom was based on state-led capitalism models impelled by alliances of international banks and local technocrats and generals, all blessed by the IMF.
- The oil export boom impelled the portfolio flows. Also important was reluctance of elites to carry out tax reforms and preference to rely on foreign loans to cover both revenue and development needs.
- IA very large proportion of loans were taken by state enterprises, while others were loans for arms acquisitions, all financed by international private banks and investor groups.

Total External Debt of Argentina, Brasil, Mexico, and Chile. 1970-1990 (Billions of dollars)



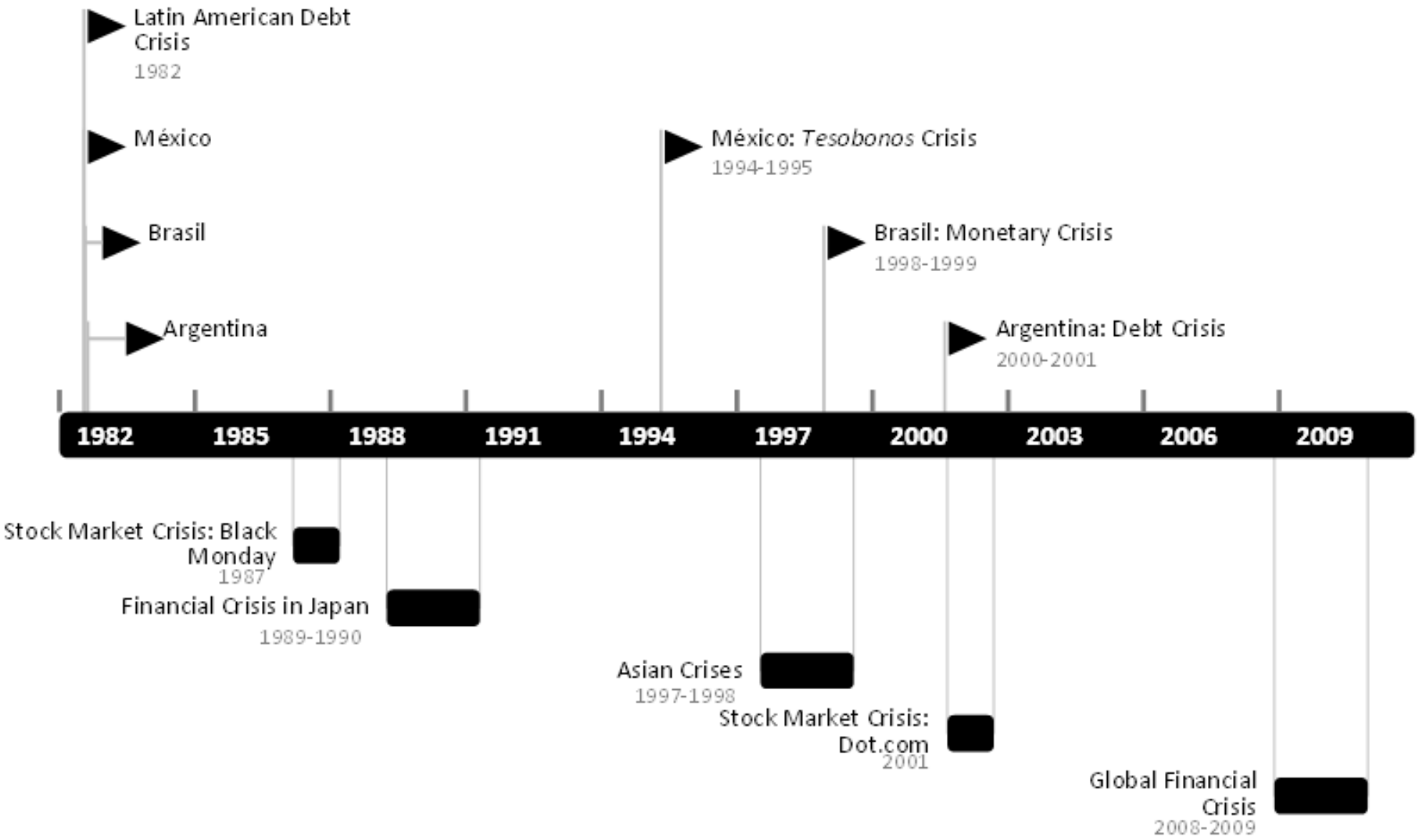
Source: World Bank, *Global Development Finance*, several years.

The explosion of literature on global finance since the debt crises of the 1980s in Latin America: some issues debated

It is worth noting that the finances of Latin America were not a major subject for economists round the world until the debt crises of the 1980s, but after became fundamental subject.

1. Analysts were initially concerned with practical problems of how to deal with the debt crises that began in 1982. The principal debate was on whether the crisis was the result of illiquidity or insolvency.
2. A further area of analysis and debate in the mid 1980s focused on possible solutions to the crisis:
   - fiscal adjustment and policies to "grow out of the crisis" by promotion of exports
   - partial debt forgiveness
   - debt moratoriums and/or outright repudiation

Main Latin American and International Financial Crises 1982-2009



Source: Carlos Marichal, *Nueva historia de las grandes crisis financieras*, p. 35.

LATIN AMERICAN EXTERNAL DEBT, 1980-2010

End of year balances. Millions of Dollars

Country	1980	1990	2000	2010
Argentina	27 162	62 233	146 200	128 618
Bolivia	2 340	3 768	4 461	5 875
Brasil	64 000	123 439	236 157	256 804
Chile	11 207	18 576	36 849	73 578
Colombia	6 805	17 993	35 851	64 723
Costa Rica	2 209	3 924	4 050	9 123
Ecuador	4 167	12 222	13 564	13 895
El Salvador	1 176	2 076	2 795	9 698
Guatemala	1 053	2 387	3 929	5 562
Guyana	449	1 812	1 250	1 043
Haití	290	841	1 170	353
Honduras	1 388	3 588	4 685	3 773
Jamaica	1 734	4 152	3 200	8 390
México	50 700	106 700	149 300	196 702
Nicaragua	1 825	10 715	6 660	3 876
Panamá	2 271	3 795	5 604	10 439
Paraguay	861	1 670	2 491	3 718
Perú	9 595	22 856	28 353	43 674
República Dominicana	2 173	4 499	3 676	9 947
Trinidad y Tobago	911	2 520	1 550	1 561
Uruguay	977	2 937	5 492	14 468
Venezuela	26 963	35 528	31 545	80 831
Total	**220 256**	**448 231**	**728 832**	**946 651**

Sources: CEPAL, Anuario Estadístico de América Latina y el Caribe, 2002 y 2012.

Final Comments

- **The history of the cycles of lending booms and debt crises in the Latin America over two centuries indicates that it is necessary to break this vicious and perverse circle in the future.**
- Acumulating reserves on a huge scale, as has been done since 2002, is a costly but necesaary solution to counter speculative attacks. However central banks need to rethink how they can use the reserves as guarantees for financing economic and social development.
- **The weaknes of domestic financial and capital markets has been the Achilles talon of Latin American finance since independence**. Recently some countries have developed deeper capital markets but they remain fragile.
- Economists and historians need to dialogue in order to find new solutions to a complex and historical problem that continues to affect Latin American development.