Why Not Default?

The Structural Power of Finance in Sovereign Debt Crises

Jerome Roos

Thesis submitted for assessment with a view to
obtaining the degree of Doctor of Political and Social Sciences
of the European University Institute

Florence, 19 May 2016

European University Institute
Department of Political and Social Sciences

Why Not Default?

The Structural Power of Finance in Sovereign Debt Crises

Jerome Roos

Thesis submitted for assessment with a view to
obtaining the degree of Doctor of Political and Social Sciences
of the European University Institute

Examining Board
Prof. Pepper D. Culpepper, European University Institute (supervisor)
Prof. László Bruszt, European University Institute
Prof. Robert H. Wade, London School of Economics
Prof. Daniel Mügge, University of Amsterdam

© Jerome Roos, 2016

No part of this thesis may be copied, reproduced or transmitted without prior
permission of the author

Researcher declaration to accompany the submission of written work
Department of Political and Social Sciences - Doctoral Programme

I , Jerome Roos, certify that I am the author of the work Why Not Default? The Structural Power of Finance in Sovereign Debt Crises, which I have presented for examination for the Ph.D. at the European University Institute. I also certify that this is solely my own original work, other than where I have clearly indicated, in this declaration and in the thesis, that it is the work of others.

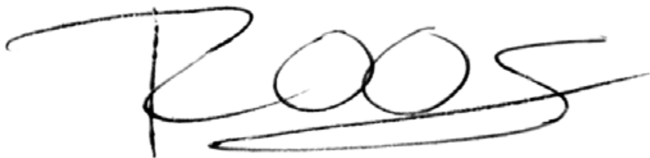
I warrant that I have obtained all the permissions required for using any material from other copyrighted publications.

I certify that this work complies with the Code of Ethics in Academic Research issued by the European University Institute (IUE 332/2/10 (CA 297).

The copyright of this work rests with its author. Quotation from it is permitted, provided that full acknowledgement is made. This work may not be reproduced without my prior written consent. This authorisation does not, to the best of my knowledge, infringe the rights of any third party.

I declare that this work consists of 98,087 (109,119 incl. bibliography) words.

Signature and date:



2nd May 2016

Acknowledgments:

Some debts can neither be repaid nor repudiated – only acknowledged. Unlike the liabilities piling up in the financial system, what makes these obligations so special is that, instead of leaving us individually poorer, they tend make us collectively stronger. Notwithstanding the neoliberalization of our societies and universities, personal and scholarly debts often remain of this "virtuous" kind. I know because I have incurred many in writing this thesis.

Academically, I am above all indebted to my supervisor, Pepper D. Culpepper, whose sharp eye, straight-shooting style and balanced approach to supervising – always there to help yet allowing the necessary space for independent research – is the best thing a graduate student could wish for. I am also profoundly obliged to the members of the jury, and not just for their close reading of and helpful feedback on the thesis. To Robert Wade I actually owe the original inspiration for this research, which properly began with his thrilling IPE course at the London School of Economics in late 2008, as financial panic raged through the City. Daniel Mügge's excellent comments, both on the thesis and on an earlier paper presented in Berlin in 2013, have been of great help in making sense of some of my own remaining questions and concerns. Lászlo Brúszt's course on capitalism and crisis during my first year at EUI helped provide some of the early theoretical foundations.

Intellectually, I have been very lucky to have benefited from conversations with and comments by some of the greatest living theorists of capitalism and the state: David Harvey, John Holloway (who kindly hosted us at the Institute in Puebla), Wolfgang Streeck, Leo Panitch, Bob Jessop, Toni Negri, Michael Hardt and the unforgettable Manolis Glezos.

On a personal level, I will never be able to repay my dear parents, Ronny and Peter, for their unconditional support throughout all my travels and travails; my beloved sisters, Louise, Milou and Mimi, for tolerating my long absences and always giving me such joy in coming home; my parents-in-law, Jan and Dominique, for showing so much interest and excitement throughout; and of course to all the *compas*, especially in Greece: Leonidas

Oikonomakis, Markos Vogiatzoglou and Myrsini Antoniou, Maria Kanellopoulou, Manolis Michelakakis, Antonis Vradis, Dimitris Dalakoglou, Katerina Tsapopoulou, Manos Cizek, Theodoros Karyotis, Antonis Broumas, Christos Staikos, and so many more.

I owe the *compagne e compagni* in Collettivo Prezzemolo for the fun and action in Florence, and the ROAR Collective for their help with the new print journal: Leonidas Oikonomakis (again!), Carlos Delclós, Jelle Bruinsma and above all my good friend Joris Leverink. Special thanks to Ingeborg Beugel for sharing her knowledge of Greece during the many late-night political discussions on Hydra, to Michael Albert for landing me a columnist gig while writing up the thesis, and to Marianne Maeckelberg and Brandon Jourdan for their help with our research foundation. A special shout-out to Dr. 7 and I.G. Karfield.

This thesis is dedicated to the people of Greece who are now opening their arms and doors to those fleeing war, poverty and persecution even as they face the most severe economic calamity in living memory. Over all these years, the Greeks have taught me more than any social science degree ever could about the true meaning of solidarity. As the wayward son of a stingy creditor nation, I know we owe them more than we will ever know we owe.

But personally, above all, I owe Tamara, *mi querida compañera de vida*. She was there at the beginning and at the end of it all. Only she knows what went into this thesis – so much of it hers. Its cover may bear my name, but her boundless love, brilliance and support reflects back on every single line of the 320 pages that follow.

Abstract:

This thesis aims to answer a simple question with far-reaching implications: why do heavily indebted peripheral states not default on their external debts more often? Building on case studies of substantively important sovereign debt crises in Mexico (1982-'89), Argentina (1999-'05) and Greece (2010-'15), the findings of this research demonstrate that the traditional explanations of debtor compliance proposed in the economics literature – centering on reputation, sanctions and democratic institutions – hold limited explanatory power.

Instead, the thesis spells out a *political economy* approach to sovereign debt that recognizes the importance of social conflicts and power struggles over the distribution of adjustment costs. In these conflicts, it is argued that finance possesses a unique advantage over indebted states: through its capacity to withhold the short-term credit lines on which the latter depend for their reproduction, lenders can inflict debilitating spillover costs that greatly limit the debtor's room for maneuver. This *structural power* of finance has increased markedly as a result of globalization and financialization, and the main objective of this project is to identify the exact mechanisms through which it operates and the conditions under which it is effective and under which it breaks down.

The findings highlight the importance of debt concentration in the lending structure (which eases the formation of creditors' cartels, strengthening market discipline); the exposure of big banks and institutional lenders in core countries (which compels creditor states and international financial institutions to intervene as lenders of last resort and provide emergency loans under strict policy conditionality); and the bridging role fulfilled by bankers and elites inside the borrowing country (which endows them with a privileged position in financial policymaking and internalizes fiscal discipline into the debtors' state apparatus). The thesis concludes by spelling out the implications of these findings for the quality of democracy and the study of political economy more generally.

Contents:

Introduction: The Default Puzzle 1

Why Do Countries Repay their Debts? 1

A Very Brief History of Sovereign Default 3

The Puzzling Absence of Default Today 5

A Comparative Study of Mexico, Argentina and Greece 8

Summary of the Argument: The Structural Power of Finance 10

Structure of the Thesis: Chapters Outline 15

Chapter I – Theory of Sovereign Debt and Default 19

The "Enforcement Problem" of International Lending 19

Reputation: Capital Market Exclusion and the Reluctance to Repudiate 22

Sanctions: Asset Seizures, Trade Embargoes, and Gunboat Diplomacy 25

Institutions: Private Property, Credible Commitment, and Democratic Advantage 31

Spillover Costs: Bank Runs, Output Losses and Private Borrowing 36

Repoliticizing the Theory of Sovereign Debt 39

Problematizing the Unitary Agent Assumption 41

Making the Structure of Sovereign Lending Visible 44

Distinguishing Between Ability and Willingness to Pay 45

Towards a Political Typology of Default 49

Chapter II – The Structural Power of Finance 53

Business Power and the Capitalist State 53

Polyarchy: Robert Dahl and the Pluralist Approach 54

The State-as-Object: Miliband and Instrumental Marxism 57

The State as Social Relation: Poulantzas and Structural Marxism 59

Public Finance: O'Connor and the Structural Dependence of the State 61

The Market as Prison: Lindblom and the Privileged Position of Business 64

Globalization, Financialization, and the Debt State 66

The Impossible Trinity and the Capital Mobility Hypothesis 66

Structural Power in the Global Political Economy 69

Neoliberalism, Financialization, and the State-Finance Relation 72

The Debt State and the Rise of the Marktvolk 74

Enforcement Mechanisms of Debtor Compliance 76

Market Discipline and the Creditors' Cartel 78

The Policy Conditionality of the Lender of Last Resort 83

The Privileged Position of Domestic Elites 86

Chapter III – Methodology & Research Design 91

Methodological Approach 91

A Comparative Case Study Method 93

Systematic Process Tracing 94

Structural Power Analysis 95

Research Question and Design 97

Hypothesis: The Structural Power of Finance 98

Alternative Hypotheses: Reputations, Sanctions, and Democratic Advantage 100

Dependent and Independent Variables 101

Falsifiability: Warding Off Confirmation Bias 101

Case Studies and Case Selection 107

The Lost Decade: Mexico (1982-'89) *108*

The Great Default: Argentina (1999-'05) *109*

The Specter of Solon: Greece (2009-'15) *110*

Chapter IV – The Lost Decade: Mexico (1982-'89) 111

Introduction 111

Reputation Hypothesis *113*

Sanctions Hypothesis *117*

Democratic Advantage Hypothesis *119*

Spillover Costs Hypothesis *121*

Enforcement Mechanisms 124

Syndicated Lending and the International Creditors' Cartel *126*

The IMF: Fiscal Disciplinarian and "Global Capitalist Planner" *129*

The Bridging Role of Mexico's Bankers' Alliance *135*

Outcomes of the Crisis 145

Very Limited Room for Maneuver *146*

Crisis Resolution at the Initiative of the Creditors *152*

"The Rich Got the Loans and the Poor Got the Debts" *156*

Conclusion and Possible Alternative Interpretations *159*

Chapter V – The Great Default: Argentina (1999-'05) 163

Introduction 163

Reputation Hypothesis *165*

Sanctions Hypothesis *168*

Democratic Advantage Hypothesis *170*

Spillover Costs Hypothesis *173*

Enforcement Mechanisms 177

The Return to Bond Finance and the Collective Action Problem *179*

The Weakening of the IMF and Policy Conditionality *183*

The Rise and Fall of the Patria Financiera *192*

Outcomes of the Crisis 205

Argentina's Exceptional Room for Maneuver *206*

US Hedge Funds as Big Winners of the Debt Restructuring *214*

A Rearrangement of Domestic Power Relations *217*

Conclusion and Possible Alternative Interpretations *222*

Chapter VI – The Specter of Solon: Greece (2010-'15) 227

Introduction 227

Reputation Hypothesis *229*

Sanctions Hypothesis *231*

Democratic Advantage Hypothesis *234*

Spillover Costs Hypothesis *238*

Enforcement Mechanisms 244

The Financial Markets as "Global Supra-Government"? *245*

Troika to the Rescue: Austerity and Financial Control *252*

The "Establishment Triangle": From Compliance to Defiance and Back *268*

Outcomes of the Crisis 284

The Eurozone Straitjacket: Limited Room for Maneuver *286*

Restructuring and Socialization of the Debt *296*

Unequal Distribution of Adjustment Costs *302*

Conclusion and Possible Alternative Interpretations *307*

Conclusion: The Democratic Disadvantage **311**

Findings and Implications 311

Conclusions from the Findings *313*

Implications for Political Economy *315*

Bibliography **323**

Tables & Figures:

Tables:

Table 1.1: Typology of default 51

Table 1.2: Definitions of default 52

Figures:

Figure 3.1: Reputation hypothesis 103

Figure 3.2a: Trade sanctions hypothesis 104

Figure 3.2b: Legal sanctions hypothesis 104

Figure 3.3: Democratic advantage hypothesis 104

Figure 3.4: Spillover costs hypothesis 104

Figure 3.5a: Structural power hypothesis 105

Figure 3.5b: Structural power hypothesis (continued to outcomes) 106

Figure 4.1: Reputational mechanism 113

Figure 4.2a: Trade mechanism 117

Figure 4.2b: Legal mechanism 118

Figure 4.3: Institutional mechanism 119

Figure 4.4: Spillover mechanism 121

Figure 4.5: Market discipline mechanism 126

Figure 4.6: Policy conditionality mechanism 129

Figure 4.7: Privileged position mechanism 135

Figure 4.8: Outcomes according to structural power hypothesis 145

Figure 5.1: Reputational mechanism 165

Figure 5.2a: Trade mechanism 168

Figure 5.2b: Legal mechanism 169

Figure 5.3: Institutional mechanism 170

Figure 5.4: Spillover mechanism 173

Figure 5.5: Market discipline mechanism 179

Figure 5.6: Policy conditionality mechanism 184

Figure 5.7: Privileged position mechanism 192

Figure 5.8: Outcomes according to structural power hypothesis 205

Figure 6.1: Reputational mechanism 229

Figure 6.2a: Trade mechanism 231

Figure 6.2b: Legal mechanism 232

Figure 6.3: Institutional mechanism 234

Figure 6.4: Spillover mechanism 238

Figure 6.5: Market discipline mechanism 245

Figure 6.6: Policy conditionality mechanism 252

Figure 6.7: Privileged position mechanism 268

Figure 6.8: Outcomes according to structural power hypothesis 284

And many a man whom law or fraud had sold
Far from his god-built land, an outcast slave,

I brought again to Athens; yea, and some,
Exiles from home through debt's oppressive load,

Speaking no more the dear Athenian tongue,
But wandering far and wide, I brought again;

And those that here in vilest slavery
Crouched 'neath a despot's frown, I set them free.

~ Solon (c. 368-558 BC)

INTRODUCTION:

The Default Puzzle

Why Do Countries Repay their Debts?

Why do heavily indebted countries not default on their external debts more often? This question, which lies at the heart of a long-standing debate in the economics literature and touches upon some of the most important controversies in political science, has gained renewed relevance in light of the ongoing European debt crisis. Recent events have revealed how international lending is governed by a fundamental paradox: in the absence of a world government capable of enforcing debt contracts between sovereign borrowers and private foreign lenders, we would expect default to be a widespread phenomenon. Since repayment effectively constitutes a wealth transfer from the borrower to its lenders, a distressed debtor that spends more of its tax revenues on foreign debt servicing than it attracts in new loans has an inherent incentive to suspend payments. In fact, this is precisely how international debt crises were generally resolved in the nineteenth and early-twentieth centuries: through the imposition of unilateral moratoriums by the debtors. And yet such payment standstills

are exceedingly rare today: recent decades have witnessed a *generalized trend* away from unilateral default as a prevalent and permissible policy response; a trend that holds important lessons about the asymmetric balance of power between debtors and creditors in the global political economy and the evolution of state-finance relations more generally.

This PhD thesis aims to contribute towards the development of a political economy approach to sovereign debt that can account for this generalized trend away from unilateral default. The main argument developed in these pages is relatively straightforward: over the past decades, the dual processes of globalization and financialization have greatly enhanced the disciplinary force of finance, providing international lenders with a form of structural power over heavily indebted peripheral states, revolving around their capacity to withhold the short-term credit lines on which these states depend for their own reproduction. While this "structural power hypothesis" is by no means original – as we will see, its roots go back to the political economy debates on the capitalist state of the 1970s – this project hopes to contribute to the recent revival of scholarly interest in the structural power of finance by identifying the exact enforcement mechanisms through which this power operates and the precise conditions under which it is effective and under which it breaks down. Building on in-depth case studies of three of the most important sovereign debt crises of the past decades – Mexico (1982-'89), Argentina (1999-'05) and Greece (2010-'15) – the thesis aims to shed a new light on the enforcement of debtor compliance and the ways in which contemporary crisis management systematically favors the interests and ideas of private lenders over those of working people inside the debtor countries and taxpayers in the creditor countries, with far-reaching consequences for the distribution of the costs of adjustment and the quality of democracy. This introduction presents the puzzle at the heart of the research project before outlining the main argument and providing a chapter overview of the rest of the thesis.

A Very Brief History of Sovereign Default

The starting point of this research project is the simple observation that things were not always the way they are today. In the early days of international lending, between 1820 and the 1930s, sovereign default was widespread and often unavoidable. While there were always exceptions, the declaration of unilateral moratoriums by heavily indebted peripheral states was so common that it was considered to be “part of the rules of the game” (Ocampo 2013).[1] Indeed, all the four major lending cycles prior to World War II ended in a wave of defaults. Take the first cycle of the 1820s, in which the independence struggles of a number of Mediterranean and Latin American countries coincided with a speculative boom in the London Stock Exchange. In the space of just three years, between 1822-'25, dozens of newly emerging countries contracted multi-year loans in international money markets to finance their costly independence wars. The experience ended in tears as virtually all the new states unilaterally suspended payments in the bust that followed. Peru was first to default, in April 1826, followed by Colombia. By 1829 all Latin American and Southern European countries except Brazil and Naples were in arrears, and there was remarkably little bondholders could do to recoup their investments (Flandreau and Flores 2009:659). As a leading historian of the episode wrote, “during a quarter of a century most of [the new borrowers] maintained an effective moratorium on their external debts, which indicated an appreciable degree of economic autonomy from the great powers of the day” (Marichal 1989:66).

In the late 1860s and early 1870s, European capital began to flow back towards Latin America and the Mediterranean, but the expansion of international lending again turned

1 One observer lamented early on that “the fiscal history of Latin America is replete with instances of governmental defaults. Borrowing and default follow each other with almost perfect regularity. When payment is resumed, the past is easily forgotten and a new borrowing orgy ensues” (Winkler 1933:1).

out to be short-lived, with most borrowers suspending payments in the depression of 1873. As in the previous wave, the defaults of the 1870s were unilateral and outright; governments generally did not resume payments until after the economy had recovered, foreign exchange reserves had been replenished and the defaulted debt had been restructured on terms favorable to the borrowers. By the 1880s, a third international lending frenzy nearly led to the collapse of the Barings Bank when a financial panic surrounding bad investments along the River Plate ended in the Argentine default of 1890. It was in this period, the classical gold standard era of 1870-1913, that the creditor states began to assert themselves more aggressively to defend bondholder interests and enforce debt repayment. With inter-capitalist rivalries feeding the imperialist ambitions of the European powers and to a lesser extent the United States, the use of force became increasingly frequent in the settlement of international debt disputes. While there is still scholarly disagreement over how widespread military action really was in this period, Mitchener and Weidenmier (2011:156) find that non-compliant debtor countries risked a 30 percent chance of being subjected to military invasion, gunboat diplomacy or the establishment of international financial control. Often-cited examples include the imposition of foreign control over public finances in Egypt, the Ottoman Empire and Greece, the naval blockade of Venezuela, and the occupation of the customs houses of numerous Caribbean and Central American states by US Marines.

While the First World War brought the age of high imperialism to a violent end, the roaring 1920s that followed gave rise to yet another major bout of speculative investment. Like the previous ones, this fourth lending cycle quickly turned to widespread default in the Great Depression of the 1930s – with the major difference that this time around the use of military might to enforce debt contracts had been ruled out, leaving bondholders once again powerless in the face of a wave of defaults. With the exception of Argentina and some

of the smaller debtors, all Latin American countries suspended payments, as did the vast majority of European states. Jorgensen and Sachs (1989:78) stress that "the defaults of the 1930s present lessons for contemporary experience because these countries actually ceased payment on their foreign debts and these defaults were acknowledged, accepted, and eventually negotiated on terms favorable to the debtors." The leading sovereign debt scholar of the time even concluded that "defaults are inevitable when attempts are made by lenders to take advantage of temporarily embarrassed borrowers by exacting all sorts of concessions and imposing all sorts of impossibly harsh terms" (Winkler 1933:xvi). The lessons from history are therefore unambiguous: in suspending payments, the heavily indebted states of the periphery displayed a remarkable degree of autonomy, as a result of which the burden of adjustment tended to be shared relatively equitably with foreign bondholders; countries that defaulted experienced faster recoveries than those that repaid in full; and most debts were eventually restructured on terms favorable to the debtors.

The Puzzling Absence of Default Today

This experience contrasts sharply to the management of sovereign debt crises in recent decades. Even in the absence of a military enforcement regime, the repayment record of distressed borrowers appears to be better today than it has been at any other point in history. Unilateral defaults are anathema and increasingly rare. By the early 1980s, a new rule seemed to have emerged: governments should repay their debts and avoid a unilateral suspension of payments at all costs. In his review of five centuries of sovereign lending, Dyson (2014:323) confirms that "the absence of sovereign default became the new norm." Insofar as sovereign defaults still occur today, they tend to take the form of voluntary reschedulings

or negotiated settlements rather than the unilateral moratoriums that characterized the first four waves of sovereign default. This is a puzzling observation, as the four decades since the collapse of the Bretton Woods regime in the 1970s have been by far the most tumultuous in economic history, with financial crises twice as frequent between 1971-'97 as they were during the first era of globalization before 1914 (Eichengreen and Bordo 2003). Still, the incidence of default today is remarkably low compared to previous periods. A new database compiled by the Bank of Canada (2014) shows that between 2009-'11, including the worst of the European debt crisis, only 0.1 percent of world public debt was in a formal state of default. The fact that international capital markets are thriving in spite of the frequency and intensity of sovereign debt crises is a clear indication that international investors generally expect governments to honor their external debts – even if they can not.[2] But how can these investors be so sure? That is the central question this thesis seeks to address.

The question itself is by no means original. In fact, there is a venerable and rapidly expanding academic literature dealing precisely with this so-called "sovereign debt puzzle": why do sovereign borrowers honor their external obligations in the absence of gunboats or some form of world government capable of enforcing international debt contracts? Why do heavily indebted countries not default more often? The question has eluded – and divided – professional economists ever since it was first posed by Eaton and Gersovitz (1981) at the start of a new era in financial history and at the peak of a large international lending boom.

2 Of course none of this is to say that the specter of default has been banished altogether. According to data compiled by Reinhart and Rogoff (2009), default continues to be a pervasive feature of financial markets. In fact, by the latter's metrics, the 1980s and 1990s were the decades with the highest rate of sovereign borrowers in a state of default ever. But as we will see in greater detail in the following chapters, this statistic tells us little about the *type* of default and the *willingness* of the borrowers to repay. If we leave voluntary reschedulings and negotiated restructurings out and look purely at unilateral moratoriums and outright repudiations, default is an exceedingly rare phenomenon today.

Eaton and Gersovitz proposed reputational concerns and long-term exclusion from international capital markets as a credible reason for governments to repay in the absence of an international enforcement regime. Another group of scholars, following Bulow and Rogoff (1989), has proposed sanctions like lawsuits and trade embargoes. Others still have argued that the institutions of liberal democracy compel the executive to credibly commit to its financial obligations. Yet while a large number of books and articles has been published purporting to deal with the intractable "enforcement problem" at the heart of the sovereign debt puzzle, scholars have so far failed to reach a conclusive answer on the matter. As three prominent experts in the field noted on the eve of the European sovereign debt crisis:

> *Almost three decades after Eaton and Gersovitz's path-breaking contribution, there is still no fully satisfactory answer to how sovereign debt can exist in the first place. None of the default punishments that the classic theory of sovereign debt has focused on appears to enjoy much empirical backing ... In sum, thirty years of literature on sovereign debt do not seem to have resolved some of the fundamental questions that motivated the field.* (Panizza, Sturzenegger and Zettelmeyer 2009:693)

The research project presented in this PhD thesis intends to make a contribution to the scholarly debate by situating the intractable question of sovereign debt and default in its appropriate theoretical context as a political question rather than a purely economic one. And as a matter of politics, it is argued, scholars of sovereign debt and default would be well advised to pay more attention to the fundamental importance of *asymmetric power relations* and *distributional conflict* in processes of economic policymaking. In a word, the decision to repay a foreign debt cannot be isolated from questions about who gets to call the shots and who gets to bear the burden of adjustment in the management of international debt crises. Every time a government chooses to repay rather than suspend or repudiate its outstanding obligations, it finds itself making a political as much as an economic calculation, and it does

so within a context that may structurally constrain a government's room for maneuver and systematically incentivize one set of policy choices over another. Understanding the role of such external constraints and internal motivations in enforcing debt repayment is therefore fundamental to the effort of developing an adequate theory of sovereign debt and default.

A Comparative Study of Mexico, Argentina and Greece

In an effort to shine a fresh light on the sovereign debt puzzle, this study takes an in-depth look at three of the most severe and substantively important sovereign debt crises of the past decades. The focus on the "hard times" of financial crisis is deliberate. From Marx to Gourevitch, political economists of various stripes have long known that moments of crisis tend to lay bare – and shape – underlying interests, allegiances and power relations. As political flash points, these brief episodes often tell us more about the deep structures and dynamics of social reality than the decades of tranquility that preceded them.

Departing from a critical political economy perspective and proceeding on the basis of a qualitative comparative case study approach that contrasts crises in Mexico (1982-'90), Argentina (1999-'05) and Greece (2010-'15), this thesis hopes to make several contributions to the literature. First, it aims to problematize the existing economic theory on sovereign debt and default by revealing how the literature tends to *depoliticize* the subject matter. In its place, a number of orientating principles are defined that could inspire the development of a *political economy* of sovereign debt. Such an approach would recognize and emphasize the redistributive consequences of default/repayment; the centrality of conflicts of interest and protracted power struggles over the burden of adjustment; the asymmetric balance of forces and structural constraints on national autonomy that lie at the heart of the global

political economy; and the different forms that default can take in practice. In relation to the last point, the theory chapter proposes a new and explicitly *political typology* of default that in many important respects moves beyond the widely used technical definition of the term, distinguishing instead between unilateral action by debtors and negotiated settlements with creditors. Without recognizing the decline in the incidence of unilateral action, it is argued, scholars will be unable to recognize the disciplining effects of "crisis management" and the dramatic shift in power relations at the heart of contemporary capitalism.

A second contribution this thesis seeks to make is to the political economy debate on the power of finance and the nature of the capitalist state. Here, the emphasis is on the concept of the *structural power* of capital, which has recently been staging a comeback in the literature after decades of scholarly neglect. One of the reasons original formulations of structural power went out of vogue after the 1980s and '90s was that they proved incapable of accounting for variation in outcomes (Culpepper 2015). If the power of capital is structural in nature, how do we explain those situations in which corporate interests actually lose out over other social concerns? Until recent years, scholars working on business power have struggled to specify the exact conditions under which structural power is operative and the conditions under which it breaks down. This thesis proposes a two-pronged way out of the theoretical mire: first, by focusing on the *enforcement mechanisms* through which the structural power of finance is brought to bear on heavily indebted states and identifying the conditions under which these mechanisms are effective and the conditions under which they are not; and second, by taking social struggles and political conflicts seriously and allowing for the structural power of capital to be contested from below. In the process, it is hoped that the thesis will not only provide an answer to the question why governments by and large repay their external debts, but also why they sometimes choose to defy their foreign

creditors and default on their obligations. The disciplinary framework of the project thus aims to combine the strengths of the International Political Economy literature, with its focus on the global financial structure and its interest in explaining world-historical change at the systemic level, and the Comparative Political Economy literature, with its keen eye for detail and its emphasis on explaining variations in outcomes across specific national contexts. The selected case studies – contrasting Mexico's compliance to Argentina's defiance and applying the lessons of this comparison to Greece – are especially useful for parsing out the precise ways in which the hypothesized enforcement mechanisms of debtor compliance function (or fail to function) under specific national and international conditions.

Summary of the Argument: The Structural Power of Finance

The first premise of the thesis is that recent decades have witnessed dramatic changes in the material and normative structure of the global political economy and the nature of the capitalist state that have in turn caused the international balance of power to shift decisively in favor of finance and the main creditor states, and the domestic balance of power decisively in favor of local elites whose interests and ideas are broadly aligned with those of foreign creditors. Three structural changes are identified in particular. First, the processes of globalization and financialization have massively increased the mobility and concentration of capital among a decreasing number of systemically important ("too big to fail") financial institutions in the core countries. In terms of international lending, this has meant that the liabilities of peripheral borrowers like Mexico, Argentina and Greece have increasingly been held by an ever-smaller group of big banks and institutional investors in the US and Northern Europe. This highly concentrated lending structure contrasts sharply to the

dispersed bondholdings of the aforementioned pre-war lending cycles, in which small and atomized retail investors found it exceedingly difficult to coordinate collective action and exert the requisite leverage over defaulting governments. In comparison, the concentrated lending of the post-1970s period has made it much easier for investors to coordinate collective action and maintain a relatively unified creditor cartel capable of credibly threatening a withdrawal of further credit in the event of non-compliance. It is argued that this first development has strengthened the primary enforcement mechanism of *market discipline*.

The second structural change is related to the first and concerns the active "financial interventionism" of the dominant creditor states and official multilateral lenders from the 1980s onwards. The growing concentration of international debt among a small group of systemically important financial institutions in the advanced countries has meant that a disorderly sovereign default in the periphery now risks triggering a deep financial crisis in the core countries. As a result, a systemic need arises for state intervention and an international lender of last resort capable of "bailing out" distressed borrowers in order to prevent contagion towards over-exposed financial institutions in the core. The US Federal Reserve and US Treasury Department actively intervened in the international debt crises of the 1980s and 1990s, while Eurozone creditor states – led by Germany – and the European Central Bank played a key role in the management of the Eurozone debt crisis of the 2010s. In all cases, bailout loans provided by official lenders were disbursed in tranches and conditional on far-reaching budget cuts, tax hikes, privatizations and market reforms aimed at freeing up public revenue for full debt servicing. From the early 1980s onwards, creditor states have increasingly relied on the intervention of the International Monetary Fund (and to a lesser extent the World Bank and the Bank for International Settlements), which has effectively assumed the function of an international lender of last resort, enforcing fiscal discipline and

structural reform through its loan conditionality. Beside its own emergency lending, the IMF's most important contribution has been to monitor the performance and compliance of debtor states, providing the Fund with a gatekeeping function over market access. This transformation of the IMF has ended up institutionalizing a set of surveillance and control functions that had hitherto been only partially, irregularly and improvisationally fulfilled by private international banks and creditor states. In the process, it has served to entrench the second enforcement mechanism of *policy conditionality.*

The third change involves the thorough restructuring, over the same period, of the state apparatus itself. This transformation is probably best captured in Streeck's (2014:72) conceptualization of the *debt state* as “a state which covers a large, possibly rising part of its expenditure through borrowing rather than taxation, thereby accumulating a debt mountain that it has to finance with an ever greater share of its revenue.” The debt state's structural dependence on private credit conspired with the international mobility of capital and the deregulation of the financial sector to greatly increase competitive pressures on national governments, which consequently found themselves compelled to continuously reproduce the ideal conditions for foreign lending and private investment. This development ended up greatly strengthening the privileged position of those social groups whose material interests and ideological convictions were closely aligned with those of international investors, at the expense of those political actors whose loyalties continued to lie with working people back home. The result was a dramatic reconfiguration of domestic power relations in favor of financial and political elites who were perceived to be capable of fulfilling a “bridging role” towards global finance, thereby entrenching the third enforcement mechanism of debtor compliance: the *privileged position* of wealthy local elites with shared views and close ties to foreign creditors and the international financial establishment.

These structural changes have gone hand-in-hand with a set of normative and ideological changes that led to the firm entrenchment of neoliberal ideas about crisis management and the reaffirmation of a culturally-embedded creditor morality that places the responsibility for adjustment squarely on the shoulders of the debtor.[3] This ideological realignment has in turn had far-reaching implications for prevalent norms about debt repayment, clearly expressed in the stark contrast between the pre-war concern with preventing moral hazard and the current concern with defending "creditor rights." While the Palmerston doctrine of 1848, one of the keystones of the regime of *laissez-faire* liberalism, still held that the British government reserved the right *not* to intervene on bondholders' behalf in international debt disputes, so as to discourage "hazardous loans to foreign governments who may either be unable or unwilling to pay the stipulated interest thereupon," and while during the 1930s President Franklin D. Roosevelt personally apologized to his Bolivian counterpart for Wall Street's "supersalesmanship" in the lead-up to the crisis, acknowledging that "of course" the Latin American countries were "unable to pay either the interest or the principal" on their debts (both citations from Winker 1933), the idea that non-payment could be considered a permissible policy response or that unsustainable debts could actually be forgiven is clearly anathema today. Ever since the Mexican debt crisis of 1982, the widely shared expectation is that borrowers will bear the full burden of adjustment even as the lenders are made whole. Never before in modern economic history, it seems, have prevalent norms of sovereign debt repayment and dominant ideas about crisis management been so kind to bondholders. This thesis aims to investigate *how these norms and ideas are enforced in practice.*

---

3 This creditor morality is powerfully expressed in the German and Dutch word *Schuld*, which means both debt and fault or guilt, so that a distressed debtor is always-already considered to be guilty or at fault for their own predicament. For a discussion of the morality of debt, see Graeber (2011) and Lazzarato (2012). Dyson (2014) applies some of these cultural and ideational themes to sovereign debt and the crisis of the Eurozone. For a related history and critique of the "dangerous idea" of austerity, see Blyth (2013).

The main argument is that, by greatly raising the costs of default and increasing uncertainty about the consequences of more confrontational courses of action, the structural and normative transformations of recent decades have significantly reduced the room for maneuver available to the governments of heavily indebted states, undermining both the actual and the perceived viability of more debtor-friendly alternatives to full repayment. If a heavily indebted state were to default tomorrow, it would not only be forced to move into primary balance right away, as lenders would cut off short-term credit lines; it would also have to contend with devastating and unpredictable spillover costs into the wider economy. These spillover effects would initially operate through the transmission belt of the domestic financial sector, with a default on foreign creditors likely to provoke capital flight, a stock market crash and a collapse of domestic banking and pension systems. But given the centrality of finance to contemporary capitalism, the consequences would quickly ripple through the national economy, risking massive social dislocation. Firms would no longer be able to obtain trade credit and would start laying off workers; depositors would no longer be able to access their savings and would likely instigate a bank run requiring far-reaching capital controls; households would no longer be able to obtain credit for consumption, as a result of which industrial and agricultural producers would see demand and private investment dry up, bringing production to a halt – in sum, the bankruptcy of the state risks provoking the bankruptcy of large parts of the domestic economy, with high social costs in the short-term and grave consequences for the state's capacity to legitimize itself in the eyes of its citizens. Given the ability of lenders to inflict such devastating but largely unpredictable short-term spillover costs simply by withholding credit and withdrawing capital, it is perhaps no surprise that many governments – including those of a leftist or even of an anti-capitalist persuasion – are hesitant to defy their foreign creditors. Compliance becomes the rule.

Still, since these spillover costs tend to be short-lived, a government that finds itself under immense popular pressure from below may yet decide to pursue a rupture with international creditors if it considers the alternative – continued repayment – to be even more costly politically. It should be stressed, in this respect, that a debtor country is not simply a unified actor always responding in coherent fashion to economic shocks. Different groups inside the country are affected differently by different policies, and some will stand to gain more from repayment than others. One common aspect of sovereign debt crises is therefore the proliferation of distributional conflicts between different social groups over who gets to call the shots and who gets to bear the burden of adjustment. If those opposed to austerity and repayment manage to gain the upper hand in such struggles, the government may end up switching its policy preference from compliance to default. Given the crippling short-term consequences of a default, however, there is unlikely to be any real confrontation with foreign lenders without a deep legitimation crisis and intense social mobilization leading to the rise of a pro-default coalition, or at least forcing the political and financial establishment to make far-reaching concessions to the domestic population in an attempt to restore social peace and preserve the political status quo. In this sense, the push for a unilateral suspension of payments is unlikely to emanate from within the state apparatus itself; it will only emerge from the broader field of social antagonism and political contestation – unless, that is, the debtor is forcefully pushed over the edge by the creditors themselves.

Structure of the Thesis: Chapter Outline

This thesis is divided into six chapters – the first two theoretical, the third methodological and the last three empirical. Chapter I looks at the economics literature on sovereign

debt and summarizes the main theoretical contributions in the field. After presenting the four main hypotheses in the existing literature – the reputation hypothesis, the sanctions hypothesis, the democratic advantage hypothesis and the spillover costs hypothesis – and weighing the relative merits and shortcomings of each, the second part of the chapter takes the existing literature to task for its depoliticization of the subject matter and outlines the basic contours of a *political economy* approach revolving around the analysis of structural constraints, the redistributive consequences of compliance and default, conflicts of interest over the burden of adjustment, disagreements and uncertainty over the perceived costs of alternative courses of action, and protracted power struggles over who gets to decide on matters of financial policy. It concludes by proposing an alternative *political typology* of default that distinguishes crucially between unilateral action and negotiated settlements.

Chapter II is a review of the political economy literature on business power and the nature of the capitalist state. It starts with an outline of the main political science debates on the issue – between pluralists and elite theorists, and between instrumental Marxists and structural Marxists – and presents a number of key analytical concepts, most importantly the *structural dependence of the state on capital* and business' *privileged position* in capitalist democracy. The second section takes the analysis to the global level and briefly discusses the globalization and financialization debates as well as Wolfgang Streeck's concept on the evolution of the "debt state" as a state that increasingly depends on private credit. Finally, the third section starts by highlighting the main shortcomings of the original formulation of structural power – the fact that it cannot always account for variations in outcomes across cases – and proposes to focus explicitly on the enforcement mechanisms that connect the structural power of finance to the outcome of debtor compliance, and the conditions under which these mechanisms are effective and the conditions under which they are not. This

part presents the three enforcement mechanisms and the hypothesized conditions under which they break down and default becomes possible.

Chapter III on methodology and research design is significantly shorter. It starts by presenting the project's three-pronged methodological approach, drawing on a comparative case study method combined with process tracing and structural power analysis, and then outlines the research design, main questions, variables, hypotheses and case study selection. The exact conditions shaping the enforcement mechanisms are also further spelled out here.

Chapters IV, V and VI present the case studies of the Mexican debt crisis (1982-'90), the Argentine default (1999-'05) and the ongoing Greek debt crisis (2010-'15), respectively. These longer chapters are each structured in the same way. The first section weighs the evidence in favor of the conventional hypotheses discussed in Chapter I. After deriving a set of predictions from each of these explanations, this first part aims to assess whether the observed processes and outcomes of the respective crises are in accordance with what the theories would lead us to expect. The second part then weighs the evidence for the hypothesized enforcement mechanisms outlined in Chapter II – market discipline, policy conditionality and the privileged position – tracing the processes through which the observed conditions impacted the operativeness and effectiveness of each of them. The third part looks at the outcomes of the crises and compares these observations to what we should expect if the structural power hypothesis were correct. The final part of each chapter briefly considers other possible explanations for the findings.

Finally, the conclusion sums up the main findings of this project and outlines their implications for future research on sovereign debt, structural power and political economy more generally – especially in relation to the concentration of wealth and power, the trans-

formation of the state-finance relation and the deepening tensions between capitalism and democracy. The study concludes by proposing the entrenchment of a distinct "democratic disadvantage" at the heart of financial capitalism, systematically disincentivizing democratic responsiveness through higher borrowing costs and limited access to credit.

CHAPTER I:

Theory of Sovereign Debt and Default

The "Enforcement Problem" of International Lending

As the introduction has shown, the study of sovereign debt has long been plagued by a seemingly irreconcilable paradox. More than three decades after the seminal theoretical contribution by Eaton and Gersovitz (1981), economists still do not fully understand how sovereign debt can exist in the first place. Since there is no world government to enforce international debt contracts, a country that is unwilling or unable to repay its debts should in theory be able to default without repercussions. Why transfer scarce public funds abroad if there is no greater power to enforce compliance? Assuming rational representatives and national autonomy, distressed sovereigns would simply refuse to repay. At the extreme, this logic would cause international capital markets to collapse altogether, as rational creditors would in turn refuse to extend further credit to unreliable sovereigns.[4] Yet this is far from what happens: international capital markets have been thriving ever since the 1970s, and

4 "The most radical way of posing the question is to ask whether there would be a sovereign debt market if creditors had no direct power to enforce repayment whatsoever" (Panizza *et al* 2009:9).

borrowers generally do repay their debts. As renowned sovereign debt lawyer Lee Buchheit puts it, "conventional wisdom is that sovereigns will rarely, if ever, default on their external debts in circumstances where it is clear that they have the capacity to pay" (Buchheit and Gulati 2009:1). Similarly, Lienau (2014:1) observes that international lending is governed by a simple rule: "sovereign debtors must repay, regardless of the circumstances of the initial debt contract, the actual use of loan proceeds, or the exigencies of any potential default."

As a result, many governments choose to go through great pains to avoid default even when the costs of debt servicing have become politically, socially and economically highly disruptive – during a major debt crisis, for instance, when investors take fright and the cost of public borrowing shoots up. IMF economists have recognized that policymakers appear to prefer avoiding default "even if that implies running down reserves, shortening the maturity of the debt, and ceding part of their economic policy sovereignty to multilateral institutions" (Kruger and Messmacher 2004:3). If, for whatever reason, a government is unable to repay its debts in full or on time, it will generally try to negotiate an orderly settlement with its creditors over a unilateral suspension of payments. In practice, it therefore remains extremely rare for governments to simply stop paying, let alone to repudiate their obligations outright (Rose 2005:191; Eaton and Fernandez 1995:1). So why are governments willing to incur such high economic, social and political costs to avoid default?

This puzzle of sovereign debt has long been known as the "enforcement problem" of international lending: clearly there is some kind of enforcement at work, but the precise mechanism is invisible and scholars still do not understand how, exactly, it operates. "The central issue," Martínez and Sandleris (2011:909) write, "is not why governments default, but quite the opposite: why they usually choose not to do it." Or, as Reinhart and Rogoff

(2009:52) put it slightly more dramatically: "why on earth do foreign creditors ever trust countries to repay their debt anyway...?" Apparently governments do consider default to be costly, even more so than the painful experience of fiscal adjustment. But why is this so? In the past three decades, this question has inspired a set of hypotheses about the precise costs of default and the invisible mechanisms through which debtor compliance is enforced.

This chapter begins by outlining the four main hypotheses that have been developed by economists over the years. The first stresses the *reputational costs* of default, which are theorized to lead to long-term capital market exclusion; the second emphasizes the directly imposed costs resulting from *legal*, *trade* or *military sanctions*; the third argues that *liberal-democratic institutions* tie the hands of the executive power and increase the credibility of its commitment to repay; and the fourth focuses on the *spillover costs* of default into the wider economy – specifically through the channel of the domestic financial sector – and the effects on indicators like growth, employment and overall economic performance. After briefly discussing the merits and shortcomings of each, the second part of the chapter outlines the overarching defect of the economics literature on sovereign debt (the depoliticization of a highly political subject matter) and stresses the need for a political economy approach that can account for *conflicts of interest* and *conflicting ideas and interpretations* on appropriate policy responses within the debtor country; the asymmetric *distribution of power* in the global financial architecture; the differences between *economic and political determinants* of default; and the *different forms* that default can take in practice. It concludes by proposing a new typology of default that seeks to re-politicize the concept and thereby to do justice to the qualitative differences between, on the one hand, unilateral moratoriums and repudiations, and on the other, negotiated reschedulings and restructurings.

Reputation: Capital Market Exclusion and the Reluctance to Repudiate

The puzzle of sovereign debt only really became an issue of interest for economists in the late 1970s and early 1980s. The wave of defaults that rocked the world during the Great Depression had effectively caused international capital markets to freeze up for the next forty years, and it was not until the emergence of the Eurodollar markets in the 1960s and the eventual collapse of the Bretton Woods regime in 1973 that capital began to flow across borders again. This led to renewed interest in the question of sovereign debt and how it can exist to begin with. The first paper to systematically identify this puzzle was the early theoretical contribution by Eaton and Gersovitz (1981), which argued that countries repay their external debts because they are concerned about their reputation. In this reputational model, countries borrow in order to be able to smoothen out consumption in the event of unforeseen adverse shocks on the economy. Governments therefore have an inherent incentive to repay in order to retain access to international capital markets. "Should the country refuse to repay," Eaton and Gersovitz wrote, "we assume that it faces an embargo on future loans by private lenders and that this embargo is permanent." In short, countries repay because repudiating their obligations would leave them "forever unable to use international borrowing to smooth absorption across periods of varying income" (1981:290).

It is immediately apparent that the original reputation hypothesis hinges on two questionable assumptions: first that lenders can and do act monolithically in their refusal to extend further credit after default, and second that default means *permanent* exclusion from international capital markets. In reality, countries often succeed in securing credit not only from the same lenders on whose loans they previously defaulted but from new lenders as well (Kolb 2011:6). Not surprisingly, therefore, subsequent empirical evidence has largely

disproved Eaton and Gersovitz' reputation hypothesis – at least in its rigid original form. Eichengreen and Portes (1988a; 1988b) and Lindert and Morton (1989) importantly found that countries that defaulted in the 1930s did not borrow systematically less in the 1970s, nor did they borrow on terms different from non-defaulters. Jorgensen and Sachs (1989) found that in the decades following the defaults of the 1930s, Latin American countries faced severely restricted access to foreign credit, but the effect was just as strong for a non-defaulter like Argentina as it was for the other Latin American countries that did default. When international lending was resumed in the 1970s, there was no difference in terms of market access between past defaulters and non-defaulters. Lindert and Morton (1989:40) concluded that "investors seem to pay little attention to the past repayment record of the borrowing governments," while Eichengreen and Portes (1989:3) pointed out that "there is little evidence that countries which defaulted in the 1930s suffered inferior capital market access subsequently." Indeed, "they were offered virtually identical access to the capital market as were countries which had maintained debt service without interruption" (*ibid*). The evidence for the post-1982 period, including a wave of defaults in the 1980s and 1990s, appears to further challenge the original reputation hypothesis. Citing a rare large-N study by Gelos *et al* (2004), one recent contribution concludes that, "contrary to predictions from reputational theories, the probability of market access is not strongly influenced by a default in the previous year" (Datz 2013:9).

In a subsequent paper, Eaton and Fernandez (1995:31) acknowledged that the evidence to support Eaton's thesis was "ambiguous" at best. For instance, while Ozler (1992) found that defaults after the 1930s did affect the interest rates for these countries, the effect does not appear to be strong enough to deter default. When Eichengreen and Portes (2000) studied the crises of the 1990s, they again found no evidence that defaulting countries

suffered reduced capital market access in the form of higher risk spreads. This finding was echoed by a study using a more extensive historical database, which found a "surprisingly small" default penalty (Obstfeld and Taylor 2003). A number of scholars have nonetheless sought to resuscitate the original framework proposed by Eaton and Gersovitz. Building on evidence from three centuries of sovereign lending, a major study by Tomz (2007) currently stands as the most important contribution in defense of the reputation hypothesis.

Still, even proponents of the reputation hypothesis now admit that "the empirical support for this proposition is mixed" and that most of the empirical research of the past three decades finds the default premiums in sovereign credit markets to be negligible (Das, Papaioannou and Trebesch 2012:60). To the extent that countries do pay higher interest rates after default, most scholars would agree that these costs tend to be short-lived. Gelos, Sahay and Sandleris (2004:1), for instance, find that it only took past defaulters an average of 4.5 years to regain full capital market access in the 1980s. By the 1990s, this duration had been reduced to 0 to 2 years, with an average of 3.5 months, leading the authors to conclude that "we are unable to detect strong punishment of defaulting countries by credit markets" (*ibid*). Similarly, Borensztein and Panizza (2008) find that yield spreads tend to stabilize one or two years after default. The consensus view is therefore that the original reputation hypothesis is not clearly backed by the available evidence and is, if anything, disproved by it (Panizza, Sturzenegger and Zettelmeyer 2009:27; Das, Papaioannou and Trebesch 2012:61).

Aside from the lack of empirical evidence on long-term capital market exclusion or higher borrowing costs, the reputational explanation has also been criticized on theoretical grounds. In the second most important contribution to the early sovereign debt literature, Bulow and Rogoff (1989) famously pointed out that countries have other ways of insuring

themselves against adverse shocks on the economy. Instead of repaying, for instance, a government could simply repudiate its debts outright and invest the savings thus obtained in foreign capital markets, which would provide a more profitable cushion for bad times. If true, the reputational mechanism, hinging entirely on the debtors' concern about retaining long-term access to foreign credit, would simply collapse. In order to have any effect at all, "the reputation approach therefore requires some discipline" (Reinhart and Rogoff 2009:54).

Sanctions: Asset Seizures, Trade Embargoes, and Gunboat Diplomacy

In contrast to Eaton and Gersovitz, Bulow and Rogoff proposed direct punishment as the main enforcement mechanism of debtor compliance. By imposing sanctions – or by threatening to impose them – private creditors and their governments could directly coerce debtors to repay (Eichengreen and Portes 1988a). For these authors, such sanctions could take either of two forms: the seizure of a debtor's assets abroad and the imposition of trade embargoes. Subsequent work has highlighted the historical importance of so-called "super-sanctions," where direct state coercion and the threat of outright military action served as the principal enforcement mechanism. What these different types of sanctions have in common is that they all seek, through some form of direct intervention, to "raise the cost of default sufficiently high to make repaying the foreign obligations in the self-interest of the sovereign debtor" (Kolb 2011:9). Like the reputation hypothesis, the sanctions approach – particularly in its legal and trade forms – therefore remains firmly within the boundaries of neoclassical cost-benefit analysis and rational choice theory. "In this sense," Reinhart and Rogoff (2009:57) acknowledge, "the reputation and legal approaches are not so different."

Legal Sanctions:

In the legal approach, sovereign borrowers will do almost anything to avoid default because of the danger of lawsuits inflicting further damage on an already strained economy (Eichengreen 2002). Since most emerging market debt is denominated in foreign currencies and under foreign legal jurisdictions, the debtor is liable to the laws of the country where its debt was issued. Scholars in this tradition argue that there is therefore no way for the borrower to protect itself from aggressive litigation strategies pursued by foreign creditors inside the issuing country. Selective default, discriminating between domestic and foreign creditors, is often not an option either, especially in the case of securitized bond finance, where secondary markets add a veil of anonymity to bondholdings and where a suspension of payments might trigger so-called cross-default clauses. The notorious example of the US-based vulture fund Elliot Associates buying up Peru's greatly depreciated post-default bonds at far below par, and then suing the government for its refusal to repay the full face value, is often cited as an exemplary case of aggressive legal sanctions bearing fruit for the persistent creditor (Moody's 2000). After Elliot succeeded in attaching some of Peru's foreign assets – including a payment on its Brady Bonds that was to be channeled through a Brussels-based clearing house – Peru found itself forced to settle and repay part of its defaulted debt.

However, aside from anecdotal evidence, even legal scholars recognize that lawsuits alone could never constitute an effective enforcement mechanism at the global level. "As an initial matter," Choi, Gulati and Posner (2012:133) point out, "one can wonder why anyone pays attention to sovereign contracts at all, [since] it will almost always be impossible for creditors to march into a country and simply repossess the assets of the sovereign even if a contract so allows." In an extensive historical survey, Mauro, Sussman and Yafeh (2006:133)

found that, in the period prior to World War I, the legal doctrine of sovereign immunity – religiously adhered to by the courts of the main issuing countries, the UK and later the US – made it literally impossible for private creditors to sue defaulting foreign governments. While the doctrine of sovereign immunity has since been greatly diminished in commercial dealings, the empirical evidence still contradicts the idea that legal sanctions are really taken seriously by debtor countries (*cf.* Buchheit and Gulati 2002). An early scholar of sovereign debt wrote that "judicial remedies of foreign bondholders are hardly effective" (Borchard 1951:172). During the crisis of the 1980s, a *Financial Times* reporter noted that "bankers' hopes – and borrowers' fears – that crippling costs could be imposed on recalcitrant debtor countries through court action appear to be greatly exaggerated" (Kaletsky 1985:21). Three years after Argentina's 2001 default, some 140 lawsuits had been filed against the country in several jurisdictions, but even though the creditors won most of them, "attempts to actually attach assets turned out to be fruitless" (Panizza, Sturzenegger and Zettelmeyer 2009:9).

Similarly, legal considerations clearly did not withhold Ecuador from defaulting on part of its external debts in late 2008. In the wake of Ecuador's default, Lee Buchheit, who served as the country's contract lawyer in negotiations with foreign creditors, observed that "the breakdown of the [legal] line of defense is significant because this was the first time that the modern theory of supermajority creditor control of sovereign debt problems was tested in practice" (Buchheit and Gulati 2009:1). At the other end of the extreme, Greece refused to unilaterally default even though, prior to the private sector debt restructuring of 2012, the majority of its bonds were issued under Greek law, meaning the government always had the option of changing these laws to forestall legal reprisals by bondholders (Choi, Gulati and Posner 2011). So while legal considerations may play a limited role in deterring default, mostly in terms of preventing the hassle of having to deal with bothersome lawsuits by

speculative vulture funds, such lawsuits do not appear to make for a credible enforcement regime by themselves. Indeed, it has been pointed out that the majority of lawsuits from 1994 through 2007 "had no effect on bond yields" (Ahmed, Alfaro and Maurer 2010:45).[5]

Trade Sanctions:

The second form of direct punishment proposed by Bulow and Rogoff consists of trade sanctions. Unlike legal sanctions, trade sanctions would be pursued not by the private creditors themselves but by their host government. It has been claimed, for instance, that Argentina's decision to maintain payments in the 1930s – while the rest of Latin America fell into arrears all around it – was due to fears that the British would impose a particularly harmful embargo on Argentine beef imports (Eichengreen 1992:260; Jorgensen and Sachs 1989:66; Skiles 1988:24). Economic historian Carlos Díaz Alejandro (1983:29) argued that this would have had far-reaching repercussions domestically, as "tampering with the normal servicing of the Argentine debt would have involved not only a bruising commercial clash with the UK, but also probably a major restructuring of the Argentine political scene, at the expense of groups linked with Anglo-Argentine trade." Tomz (2007), however, shows that this long-standing argument does not hold up to scrutiny, not least because Argentina honored its obligations to US banks as well, even if the US was in no position to impose similarly harmful trade sanctions on Argentina. Overall, while Rose (2005:205) finds that default is associated with a significant decline in bilateral trade between a debtor and the host country of its creditors, amounting to roughly eight percent per year and lasting for fifteen years, he also notes that he is unable to identify whether the negative effect is due to

5 A more recent paper by Schumacher, Trebesch and Enderlein (2014) challenges this perspective, finding a "drastic rise of sovereign debt litigation" and "significant externalities" outside of the courtroom.

a "natural shrinkage" in trade credit or due to a deliberate attempt by the government of the creditors' host country to deter default.

In a subsequent study, Martínez and Sandleris (2011) point out that for commercial punishments to be an effective enforcement mechanism, the fall in bilateral trade between the defaulter and its creditor countries should be significantly larger than the fall in trade with non-creditor countries. The authors do not find any evidence for this proposition (see also Das, Papaiouannou and Trebesch 2012:61-2). "Contrary to the prediction of the trade sanction argument," the authors summarized their findings later, "there seems to be no significant decline on bilateral trade between the defaulting country and defaulted creditor countries in the aftermath of defaults." Given these unambiguous findings, Martínez and Sandleris (2011:911) conclude that "trade sanctions can be ruled out as the enforcement mechanism for sovereign debt repayment." Absent direct sanctions, "the channel linking default to trade remains a mystery" (Panizza, Sturzenegger and Zettelmeyer 2009:29).

Super-Sanctions:

Finally, another debate has taken place in recent years about a third possible type of sanctions: so-called "super-sanctions." Mitchener and Weidenmier (2005), joined by Ahmed, Alfaro and Maurer (2010), have argued that the abolition of fiscal sovereignty and the threat of outright military intervention served as the most important deterrents for sovereign debt repudiation in the classical gold standard era (1870-1913), also known as the age of high imperialism or the first wave of globalization. Mitchener and Weidenmier (2005:26) write that "contrary to recent studies examining modern defaults, we do not find that, in general, trade fell in response to default, nor do we find that sanctions applied by private creditors

were an effective mechanism for preventing future defaults or cleansing the reputation of defaulters." The most important enforcement mechanism, they argue, "was the imposition of foreign financial control or gunboat diplomacy." From European powers taking over tax collection in the Ottoman Empire, Egypt and Greece and sending gunboats to Venezuela, to the US invasions of the Dominican Republic, Haiti and Nicaragua, there are plenty of examples of military or financial coercion by creditor states to restore repayment to private bondholders. Indeed, Mitchener and Weidenmier (2011:156) find that "the probability that a country would be *supersanctioned* was almost 30 percent during the period from 1870 to 1913," and "extreme debt sanctions were applied to more than 40 percent of defaulted debt during the first era of globalization." Most importantly, after the defaulters were subjected to "fiscal house arrest" or "gunboat diplomacy," their spreads fell by some 1,200 basis points – almost 90 percent. Prior to these interventions, the countries in the sample spent nearly half of the gold standard era in a state of default, while the same countries spent practically no time in default after suffering the indignity of being "super-sanctioned" (*ibid* 2011:163). Historical case studies by Borchard (1951) and Wynne (1951) also appear to confirm the effectiveness of foreign financial control and military sanctions in enforcing repayment.

Tomz and Wright (2008:6-7), however, have contested these findings. In his extensive study of three decades of sovereign default, Tomz (2007) finds little proof that creditors used – or threatened to use – gunboat diplomacy to coerce debtors to repay, arguing that while sovereign default was often invoked as an excuse to invade a country, the real motivations had to do more with underlying geo-strategic and imperial interests. Either way, while The Hague Peace Conference of 1907 ironically still recognized "the legitimacy of the use of force in settling debt disputes," the debate is a purely academic one in the post-war era, now that armed intervention has been fully ruled out as an acceptable enforcement mechanism

(Mauro, Sussman and Yafeh 2006; Finnemore 2003). As Panizza *et al* (2009:28) write, “regardless of how the debate between Tomz (2007) and Mitchener and Weidenmier (2005) is resolved, there does not appear to be any recent evidence for supersanctions.” We are therefore compelled to look beyond both reputational costs and the costs of sanctions to uncover the hidden forces behind sovereign debt repayment in the post-war era.

Institutions: Private Property, Credible Commitment, and Democratic Advantage

One explanation that has not been widely picked up in the economics literature on sovereign debt but that has nonetheless been very influential among political scientists and developmental economists focuses on the role of political institutions in protecting creditor rights. Towards the end of the Cold War, at a time of great neoliberal triumphalism, North and Weingast (1989) published an article emphasizing the connection between political and economic rights – and, indeed, between the underpinning institutions of market capitalism and liberal democracy: private property and limited government. Extrapolating from a case study of England before and after the Glorious Revolution of 1688, North and Weingast based their argument on the idea that liberal institutions limiting the power of the executive greatly enhance the government's ability to credibly commit to upholding property rights and hence honoring its debt contracts. In North and Weingast's (1989:808) formulation, liberal-democratic institutions “do not substitute for reputation-building and associated punishment strategies,” but “appropriately chosen institutions can improve the efficacy of the reputation mechanism by acting as a constraint in precisely those circumstances where reputation alone is insufficient to prevent reneging.” In sum, the institutional innovations of an empowered parliament, an independent judiciary and strong rule of law, and a central

bank to safeguard "sound money" collectively served to "dramatically increase the control of wealth holders over the government," thereby constraining the sovereign and reducing the likelihood of default (North and Weingast 1989:829).

Expanding on these ideas, subsequent work by Schultz and Weingast (2003) posited the existence of a distinct "democratic advantage" allowing liberal regimes to borrow larger sums at lower interest rates than their less democratic or authoritarian counterparts. "The institutions of limited government," Schultz and Weingast (2003:11) wrote, "can modify the incentives of the sovereign by increasing the ability of those with a stake in the repayment of debt to impose penalties on him." The problem with this argument is that its logic only holds when the private creditors are domestic constituents. While this might make sense for advanced capitalist economies, which largely raise credit domestically and in their own own currencies, it does not apply to developing or peripheral economies, which still depend on credit denominated in currencies and legal systems other than their own – a weakness that Eichengreen, Haussman and Panizza (2005) have referred to as "original sin," which is often considered an important determinant of default.[6] Since foreign creditors are not represented by the democratic institutions of these peripheral countries (or at least are not supposed to be), the institutional explanation has still not solved the enigma of *international* lending.

An important caveat here is that the democratic advantage could be hypothesized to operate via the enforcement mechanism of "domestic audience costs" developed by Fearon (1994), which hypothesizes that "leaders that break international commitments will lose the support of constituents at home and damage their chances for reelection" (Tomz 2002:2;

6 Buckley (2009:2) puts this in simple terms: "As a nation can only print its own currency, and as poor countries invariably can only borrow abroad in other nation's currencies, sovereign debtors can be unable to service their foreign-currency denominated debts as they fall due."

Jensen 2002). This domestic audience constraint is claimed to be much weaker for autocrats, "who do not jeopardize their domestic political future when they abrogate international agreements or violate international norms" (McGillivray and Smith 2000). In this particular interpretation, the government's creditors need not necessarily be domestic. The problem, however, as Tomz has extensively documented, is that this line of argument in turn hinges on a number of further assumptions that are not very likely to hold across a great variety of cases. Most importantly, it assumes that the interests of the median voter are aligned with those of foreign creditors, while Tomz (2002:1) has convincingly demonstrated that "even knowledgeable and motivated voters may favor noncompliance as the best way to promote the national interest or their personal welfare." Tomz (2002:2) thus concludes that, "to the extent that democracy empowers those champions of noncompliance, it could make default more rather than less likely." Saiegh (2005a:99-100) argues that "democracy alone does not create credibility. What matters is representation of debt-holder interests, which democracy provides only when those with a stake in the repayment of debt are electorally pivotal."

Aside from these theoretical questions, there appears to be a further problem with the democratic advantage hypothesis: the empirical evidence simply does not stack up in its favor. First of all, pertaining to North and Weingast's English case study, Robinson (1998) has highlighted that the fall in interest rates following the Glorious Revolution was actually part of a much more long-term downward trend that went back to at least the late sixteenth century. Furthermore, as Stasavage (2002) shows, interest rates remained volatile even after the Glorious Revolution, and the establishment of democratic institutions ensuring credible commitment far from abrogated opportunistic behavior by the executive. And while these two contributions call into question the internal validity of the democratic advantage thesis, a number of other studies have challenged its external validity (e.g., Brewer and Rivoli 1990;

Sussman and Yafeh 2000; Stasavage 2002; Tomz 2002; Saiegh 2005b). One study by Mauro, Sussman and Yafeh (2006b:1) finds that "news about institutional reforms seldom [has] a rapid and significant impact" on bond yields, indicating that investors were often either unaware of (or unmoved by) institutional factors. Another study by Enderlein, Trebesch and Von Daniels (2011:24) finds that "democratically-elected politicians respond with more aggressive policies towards foreign financial markets" than their autocratic counterparts.

Historical evidence casts further doubt on the democratic advantage hypothesis. In his case studies on the emergence of public debt in early-modern Europe, Stasavage (2007a; 2007b; 2011) finds that representative institutions only enforced compliance when merchant interests were represented; insofar as they were, the nature of the political regime tended to be oligarchic rather than democratic. Pezzolo (2007:15-16) also writes that "the key feature that underpinned the [debt in the Italian city states] and supported a vivid and large market – which in turn called for a certain degree of credibility – lay in the close permeation between major bondholders and a power elite. As long as this identity persisted it would have been unlikely the government defaulted." Also, while a body of work finds support for the commonplace view that "institutions matter," those studies based on extensive datasets find little evidence for a real democratic advantage. Most notably, a study by Archer, Biglaiser and DeRouen (2007) of 50 developing countries between 1987 and 2003 finds that the three big credit rating agencies – Standard & Poor's, Moody and Fitch – did not favor democracies over comparable autocracies. Another study by Saiegh (2005b), building on a dataset of 80 developing countries between 1971 and 1997, finds that while democracies and non-democracies paid similar interest rates, the democracies were actually *more* likely to reschedule their debts. According to Flandreau and Flores (2009), who study the development of global capital markets in the 1820s, the key role of financial intermediaries like the

House of Rothschild virtually dissolved the democratic advantage. Indeed, the authors note that the intermediaries displayed a distinct "bias in favor of arch-conservatives who had no remorse about implementing unpopular policies or even ruthless repression" to extract wealth and revenues from their respective populations for the servicing of their debts. "This somewhat frightening conclusion," Flandreau and Flores (2009:679) conclude, "is antithetic to the 'democratic advantage' view, which neo-institutionalists have recently emphasized." In a word, while a ruthless dictator may be willing and able to face down popular resistance to austerity measures and structural reform, a democratic leader may in fact "prefer protests from the financial markets to the protests from their own people" (Balcerowicz 2010:4-5).

These findings have prompted scholars to ask a simple question: "where is the democratic advantage?" (Beaulieu, Cox and Saiegh 2011:1). Not only does the evidence seem to indicate that "regime type and most other political factors have little effect on bond rates" (Archer, Biglaiser and DeRouen 2007:341), but it actually points in a politically disturbing direction: when it comes to debt repayment, coldblooded dictators may be more reliable partners for creditors than democratically accountable leaders. Extending the argument, Saiegh (2005b) contends that, insofar as democracies obtain better terms than non-democracies, this is only due to the intervention of multilateral lenders. Once the role of IMF policy conditionality is taken into account, "dictatorships are more likely to honor their debts than democracies" (2005b:20). This leads Saiegh to a provocative but not altogether far-fetched conclusion: "if multilateral agencies can condition democracies to behave as non-democracies on debt matters, then the problem dissolves. Namely, if the decision-maker is no longer the median voter but the political leadership ... repayment is assured." In other words: "we will bail you out but you promise to conduct yourself as if you were a dictatorship when it comes to repaying the debt" (*ibid*:20). Paradoxically, in other words,

the democratic advantage may consist of a mechanism whereby democratic countries are systematically conditioned by the IMF to behave more like non-democracies.

Spillover Costs: Bank Runs, Output Losses, and Private Borrowing

The puzzle at the heart of this chapter – and of the academic literature on sovereign debt more generally – has still not been resolved. "At some level," the IMF's former chief and deputy-chief economists Kenneth Rogoff and Carmen Reinhart (2011:57) were forced to admit, "neither the reputation-based model of Eaton and Gersovitz nor the institutional approach of Bulow and Rogoff seems quite adequate to explain the scale and size of international lending or the diversity of measures creditors bring to bear in real-life default situations." Since democratic institutions, creditor sanctions and the threat of long-term capital market exclusion do not seem to be sufficient reasons for private creditors to keep lending to foreign governments, a small but growing body of literature has recently focused on another set of factors that may motivate governments to repay: the so-called spillover costs of default. This literature suggests that the main costs of default may be borne not so much by the government as by the private sector.[7] Starting with theoretical contributions by Cole and Kehoe (2000), Dooley (2000), Alfaro and Kanczuk (2005), Sandleris (2008; 2010), Catão, Fostel and Kapur (2007) and Mendoza and Yue (2011), sovereign debt scholars have become increasingly aware of the ways in which sovereign default could either affect private actors directly, or otherwise indirectly harm the government's trust relationships with domestic

7 Borchard (1951:178) made an early allusion to such spillover costs: "[T]he most effective sanction for the service and payment of a foreign bond in the minds of bankers is the consequence of default on a nation's credit and the effect on all credit-seeking subdivisions and even private business. By making new loans unavailable, or obtainable only at a cost commensurate with the risk involved, prolonged default may exert a depressing if not disastrous effect on the economic life of a country."

businesses (Gelos, Sahay and Sandleris 2004:5). The consequences of default could spill over into finance, trade and production, harming not only bankers, traders and industrialists, but also affecting overall economic performance, output and employment.

A number of recent contributions seem to indicate that these theoretical intuitions may indeed hold true in practice. Kaminsky and Schmukler (2002), for instance, find that sovereign credit ratings strongly impact the performance of bond and stock markets, while Levy-Yeyati *et al* (2011) show that sovereign debt crises tend to lead to a loss of confidence among depositors, thereby contributing to the risk of bank runs. Borensztein and Panizza (2008) also find that sovereign distress can trigger broader banking crises, while Borensztein *et al* (2007) find that sovereign credit ratings strongly influence the private credit ratings of emerging market firms, implying strong negative consequences on the ability of firms to borrow in the event of a sovereign default. Another study has shown that, "contrary to conventional wisdom, government defaults are costly because they destroy the balance sheets of domestic banks," especially in countries with more more developed financial institutions, in which banks tend to hold more government bonds (Gennaioli, Martin and Rossi 2013:1; see also Angeloni and Wolff 2012). Brutti (2010:16) also finds that "default episodes appear to lead to banking crises," which in turn disrupt private investment and reduce domestic production. A recent paper by the Bank for International Settlements (BIS 2011:1-2) identifies four principal channels through which the loss of a sovereign's credit-worthiness affects the domestic banking sector:

> *First, losses on holdings of government debt weaken banks' balance sheets, increasing their riskiness and making funding more costly and difficult to obtain ... Second, higher sovereign risk reduces the value of the collateral banks can use to raise wholesale funding and central bank liquidity ... Third, sovereign downgrades generally flow through to lower ratings for domestic banks, increasing their wholesale funding costs, and poten-*

tially impairing their market access. Fourth, a weakening of the sovereign reduces the funding benefits that banks derive from implicit and explicit government guarantees.

It is not just the banks that are affected by a sovereign's loss of creditworthiness: the spillover costs of default ripple through the entire economy. Cruces (2007), for instance, has shown that sovereign default risk leads to significantly higher equity risk premiums in the stock market, while Arteta and Hale (2005) observe that sovereign debt restructurings have an adverse effects on private sector access to credit. Das, Papaioannou and Trebesch (2009; 2011) find a 40 percent drop in foreign borrowing by the private sector following restructuring, while Fuentes and Saravia (2010) observe a reduction in FDI inflows of 2 percent of GDP per year. Trade may also be affected. Because international commerce depends on a complex network of short-term credit arrangements, it has long been argued that "the interruption of trade finance might turn out to be the heaviest penalty for a defaulter," and that "trade finance could be the Achilles' heel of a default strategy" (Kaletsky 1985:36-38).[8] It has been said that "a defaulting country first loses access to its trade credit" (Cohen 1991:1), while Rogoff (1999:31) has suggested that "the strongest weapon of disgruntled creditors, perhaps, is the ability to interfere with short-term credits that are the lifeblood of international trade." Building IMF (2002) research, Panizza *et al* (2009:29) conclude that "defaults could cause output drops, or make already bad output states worse, at least in the short run." Mengus (2014:3) notes that the inherent opacity of securitized bond markets leaves governments unable to "precisely observe individual domestic exposures to domestic debt," and argues that "repayment derives from the fear of the messy consequences of a default and from the government's inability to compensate for those consequences. Financial opa-

8 "Trade finance is a critical issue because most trade is conducted on a credit basis of one kind of another. A common rule of thumb is that a country's lines of trade credit may cover as much as six months' merchandise imports and should at a minimum cover about three months. A debtor country which lost the whole of this trade finance would find it a daunting sum to recoup" (Kaletsky 1985:36-37).

city, by making domestic portfolios more difficult to assess, prevents government to costlessly default by perfectly reallocating resources."

As with the evidence on capital market exclusion, the spillover costs of sovereign default do appear to be short-lived. According to Fuentes and Saravia (2010:337), "if there are any costs derived from default, it is likely that they last only for a limited number of periods [*sic*]." Borensztein and Panizza (2010) show that the impact of default on exports tends to last only one to two years. Moreover, these costs affect different economic groups differently, with default particularly costly for exporting companies and the financial sector. Import-competing industries, by contrast, may actually end up benefitting from a default, especially if it is accompanied by currency devaluation (Lanau 2008). A Rabobank study (2011:1) concludes from these findings that "the economic costs of sovereign default, as estimated by scholars, are found to be less drastic than most believe." Yet these costs also appear to be unpredictable, messy and disproportionately costly to banks and businesses. If it is true that these banks and businesses wield disproportionate influence over economic policymaking in the debtor countries (see Chapter II), that may help explain why unilateral default remains such a relatively rare phenomenon today.

Repoliticizing the Theory of Sovereign Debt

The spillover costs literature therefore points in an interesting direction. If default has strong negative effects on the financial sector, on trade and on the capacity of domestic firms to borrow, then one would expect banks and other businesses to be strongly opposed to it. As Tomz (2002) has shown, such opposition does not necessarily hold for all social groups. In times of crisis, in particular, the alternative to default – full repayment – tends to

require major sacrifices from the working population, often involving protracted austerity, deep wage, pension and welfare cuts, steep tax hikes, and large-scale privatization of state assets. Most economists working on the spillover costs of default do not yet appear to fully grasp the theoretical implications of these observations: their findings risk undermining one of the unspoken assumptions within the economics literature, namely the conceptualization of sovereign debtors as "unitary agents" responding in neutral fashion to straightforward market signals. Dimsky (2011:119) summarizes the assumption as follows: "the borrower country, conceptualized as a unitary agent, compares the relative utility of repaying its debt and of defaulting on its debt; as a rational agent, it defaults when the utility from default is larger." Once we accept that some domestic groups derive greater utility from repayment than others, the unitary agent assumption begins to crumble, and the decision whether to default or to repay can no longer be reduced to straightforward utility maximization. With the redistributive consequences of default and payment now exposed, the fundamentally *political* nature of debt management finally comes to the fore.

The economics literature has so far largely ignored such overtly political questions. Who benefits from default? Who benefits from repayment? Who decides upon the course of action to be taken? The answers to these questions cannot be taken for granted; they must be subjected to critical theoretical analysis and thorough empirical research. The remainder of this chapter will try to outline a basic critique of the depoliticization of sovereign debt in the literature and proposes a number of alternative theoretical insights derived from critical political economy. First, the unitary agent assumption that underpins the existing literature should be replaced with a recognition of the inevitable conflict of interests in and conflicting ideas and interpretations about crisis management and debt repayment. Second, social structure and the distribution of interests and power should be made visible and endoge-

nous to our modes of analysis. Third, scholars should clearly distinguish between willingness and ability to pay, and especially the role of foreign exchange depletion in circumscribing the latter. Finally, the conceptually stretched technical definition of default should be replaced with a political typology that recognizes the crucial qualitative differences between various forms of default. These points will then be taken up in greater detail in Chapter II.

Problematizing the Unitary Agent Assumption

Most economists working on sovereign debt still treat debtor countries as singular entities whose different social groups are aggregated into an overarching national interest. Governments, then, are merely "representative agents" that negotiate with foreign creditors on behalf of the country as a whole. In the process of this aggregation, however, all possible conflicts *within* the debtor country are quietly assumed away: all social groups are assumed to share the same interest in compliance or non-compliance, repayment or default, and the country's government is presumed to apolitically represent this singular national interest.[9] Yet, Guembel and Sussman (2008:3) have rightly noted, "this aggregation ignores important conflicts of interests within the debtor country, [arising] because some agents, presumably those who are better off, are invested in their own country's sovereign bonds, while poor agents have no such positions." In fact, wealthy elites may derive much greater utility from repayment than others, giving them a vested interest in compliance even if this inflicts harm on the wider economy and on the population at large (Tomz 2002:2; Drazen 1998; Beetsma 1994; Calvo 1988). Insofar as borrowing governments can be said to represent the "national

9 Lienau (2014:37) has also criticized this conception: "[I]n the preferred metaphor of international relations theory, this account of sovereignty conceives of the state as a 'unitary black box' whose internal machinations are irrelevant to its foreign interactions."

interest," scholars of sovereign debt should first try to explain how this national interest is determined and whose interests it truly reflects. As Streeck (2013:14) has put it, "the politics of public debt may be conceived in terms of a *distributional conflict between creditors and citizens*," with both constituencies laying a claim on scarce public funds "in the form of contractual-commercial and political-social rights, respectively."

The redistributive implications of repayment suggest that a government's decision to honor a debt contract is not just the outcome of some disinterested rational calculation taking place inside the finance ministry, but is rather a product of protracted social and political struggles within the debtor country itself – and between the debtor country and its international creditors – over who is to bear the burden of adjustment. In these social and political struggles, domestic elites "can be expected to exert all their influence to prevent the government from repudiating" (Waldenström 2011:287-288). As we saw before, this may be true even if these elites do not hold government bonds themselves, since the spillover costs of default tend to disproportionately affect the private sector and wealthy elites regardless of whether they hold government debt. As stock markets collapse, inter-bank lending freezes up, and firms can no longer obtain access to trade finance and foreign investment, bankers and businessmen will find themselves facing serious losses. By contrast, other social groups, including workers, civil servants, students, pensioners, the poor and unemployed – basically those who rely on wage labor and/or state expenditure for their livelihoods – are likely, in relative terms, to be more negatively affected by the austerity measures required in order to keep servicing the debt, possibly leading these groups to favor a moratorium or repudiation over continued repayment, thus pitching them against both foreign creditors and domestic elites (Tomz 2002; Saiegh 2005b; Lapavitsas *et al* 2012). How such conflicting interests are represented politically and eventually transformed into policy (or not) is a matter of fierce

power struggles between these different groups at both the domestic and international level. In discussing the determinants of default, the *politics* of sovereign debt cannot be ignored.

These politics of sovereign debt are not just characterized by distributional conflicts over the burden of adjustment, but also by grave uncertainty over the exact consequences of default. While the aforementioned economics research on spillover costs has clearly shown how the consequences of default can ripple through the wider economy, the unpredictable nature of such spillover effects will in practice regularly lead actors to misjudge the actual costs of default and perceive the consequences to be either more or less dramatic than they really are. Any theory of sovereign debt therefore needs to reckon with possible divergences between the *perceived* and the *actual* costs of default for individual actors, social groups and society at large, creating space for the role of ideas, beliefs, interpretations and affects about the consequences of non-compliance, which can in turn become political battlegrounds in their own right. One group, for instance, may be more inclined to downplay the costs of default for itself, while another – presumably those with a vested interest in repayment or those fearful of future losses – may end up wittingly or unwittingly overestimating the costs for other groups and society as a whole. As a result, while the *actual* costs of default will by definition only manifest themselves in the lead-up to and the aftermath of the event itself, the *perceived* consequences can become an important site of political contestation and thus a key determinant of policy outcomes. In such conflicts over the "correct" interpretation of the likely consequences of default, those with access to the mass media, those in positions of financial power and those with expert knowledge on the economy are likely to gain in political influence over those who do not enjoy such privileges, as the former can deliberately or passively mobilize popular and political fears over the consequences of non-payment as a compelling motivator of fiscal discipline and debt compliance.

By contrast, at the other extreme, popular indignation about the social costs of fiscal consolidation and the lack of political representation afforded to working people and the general citizenry may motivate disaffected social groups to underestimate or even ignore the actual costs of default and push for non-compliance as a means of punishing foreign lenders and unresponsive domestic elites or restoring national sovereignty in the face of powerful external constraints. The importance of ideas, beliefs, interpretations and affects thus goes to show just how fundamentally *political* the question of debt repayment really is, and how little neoclassical rational choice theory – with its problematic unitary agent assumption – can tell us about the underlying uncertainties, conflicts and power dynamics.

Making the Structure of Sovereign Lending Visible

Yet the politics of sovereign debt are not only domestic. Wherever foreign investors hold a significant amount of bonds, the issue automatically becomes an international one. Here, too, the economics literature has largely tended to bypass questions of politics and power. Streeck (2011:9) again rightly remarks that "standard economic theory treats social structure and the distribution of interests and power vested in it as exogenous, holding them constant and thereby making them both invisible and, for the purposes of economic 'science', naturally given." One of the most important contributions of a political economy approach to sovereign debt would be to render visible the *structure of sovereign lending* and the continuously evolving distribution of interests and power within that structure, treating the resulting social struggles and political conflicts as endogenous to the decision whether or not to repay. As Dyson (2014:36) puts it, "sovereign debt rests on an inbuilt asymmetry of power that is readily disguised by abstract economic models and legal principles."

This brings us right back to the question of international enforcement mechanisms. Crucially, the fact that there is no formal enforcement mechanism for debtor discipline does not preclude the fact that there may in fact be a set of *in*formal mechanisms that ensure the same outcome (or alternatively a set of formal mechanisms, like the IMF's stringent policy conditionality, that unofficially serve the same purpose). As Lipson (1981:606) pointed out years ago in a seminal article in *International Organization*, "the metaphor of anarchy, so often used to describe the underlying conditions of international relations, should not be interpreted as an absence of structures that constrain state behavior and give rise to stable expectations. What must be explored … is the character of the international political structures that have thus far prompted debt service by sovereigns, even when they have found it onerous to continue payments." These structures can be said to include both global capital markets and international financial institutions. As Lipson (1981:606) notes, "what is most compelling about these structures is that sovereigns are constrained less by other sovereigns than by sanctions and incentives organized primarily by multinational banks and official multilateral lenders." In the next chapter we will see how these global power structures can become intermeshed with domestic power structures as foreign creditors, international financial institutions and domestic elites are corralled into an international coalition in their concerted efforts to enforce compliance both from the outside and from within.

Distinguishing Between Willingness and Ability to Pay

Of course the assumptions of mainstream economic theory also have implications for our understanding of the *determinants* of default. To cite Streeck (2011:9-10) again, "the only politics [that standard economic] theory can envisage involves opportunistic or, at

best, incompetent attempts to bend economic laws. Good economic policy is non-political by definition." In other words, the only politics that mainstream scholarship on sovereign debt can envisage is the "opportunistic" decision to default. Repayment is considered non-political by definition. Unsurprisingly, this neoclassical smokescreen leads many economists to a warped understanding of policy choices. On the one hand, most economists end up *depoliticizing* repayment, simply considering it "good economic policy" and therefore not really a choice in the political sense of the word, while on the other they lump together all forms of default and brand them – often without qualification – as universally political. Kolb (2011:7) perfectly illustrates this tendency when he writes that "default by a sovereign borrower is almost always a choice, and because the default is by a government, such a choice necessarily has a political component." The observation is somewhat paradoxical: while repayment is seen as "apolitical" compliance with the expectation that governments will always repay their debts, non-payment is stigmatized as an irrational and explicitly political choice, precisely because it goes against this norm. For many economists, politics therefore comes in through the back door – only in the event of non-compliance – as something to be avoided. The fact that the norm of repayment is itself a pre-established political fact is simply ignored. As Lienau (2014:5) writes, "one of the most puzzling elements of the conventional narrative is the notion that the sovereign debt regime's repayment rule could be apolitical." As we have established by now, it clearly is not.

Moreover, while the choice to repay is always by its very definition a political act with important redistributive consequences, not all defaults are necessarily the result of the same political calculations. Often a government may simply be unable to service a debt in time or in full, even if it is politically committed to doing so. By depoliticizing repayment and universally politicizing all forms of default, the literature ends up collapsing the crucial

distinction between ability to pay and willingness to pay. Insofar as the distinction is still recognized, the former is often brushed away as irrelevant – all defaults are presumed to be a result of the latter (for an example of this, see Reinhart and Rogoff 2009:54). Years ago, Eaton, Gersovitz and Stiglitz (1986:31) declared that, since national wealth is always greater than the total outstanding debt, "it seems implausible that lending to developing countries is constrained by their ability to pay. Long before a country's ability to pay would become relevant, its willingness to pay constrains its access to credit." More recently, Mauro, Sussman and Yafeh (2006:140) echoed a similar conclusion, arguing that "willingness to pay seems to have been more important than ability to pay," while Panizza, Sturzenegger and Zettelmeyer (2009:668) claim that ability to pay is of limited import "since even crises that are triggered by a bad shock could be viewed as 'willingness to pay' crises in the sense that, with sufficient adjustment (e.g., a large decline in consumption), repayment would be feasible." In this line of reasoning, whether or not the debt is repaid is really just a question of how far the government is willing to go: "Greece, for instance, could theoretically sell the Parthenon or some of its sovereign territory" (Choi, Gulati and Posner 2012:132-3).

The distinction between a country's ability and its willingness to pay is, of course, a unique and crucial aspect of sovereign debt. While a country's ability to pay can largely be defined in economic terms of illiquidity and insolvency, its willingness to pay is indeed an inherently political question (Cooper and Sachs 1985). A government may, for instance, "be unwilling to pursue large fiscal adjustments or enact reforms to achieve debt sustainability," preferring instead to renege on its external obligations (Das, Papaioannou and Trebesch 2012:67). Still, despite the repeated insistence that default is always the result of an explicitly *political* unwillingness to pay, there is overwhelming empirical evidence for the stylized fact that external economic conditions play a crucial role in default sequences. Indeed, it is now

well-known that defaults tend to occur in clusters during "hard times," often involving a strong external shock to the economy and a marked deterioration in the terms-of-trade and debt burden.[10] These findings strongly suggest that ability to pay – constrained not so much by national wealth but rather by an acute shortage of foreign exchange with which the debt is to be serviced – may be an important determinant of default after all. The vast majority of developing country debt contracts (between 93 and 100 percent, depending on the measures) is denominated in foreign currencies (Eichengreen, Hausmann and Panizza 2005). With the exception of the major financial centers and Europe, developed countries also have between 70 and 90 percent of their debt issued in foreign currencies (Gennaioli, Martin and Rossi 2013:12). A shock in the exchange rate, a decline in the terms of trade, a serious bout of capital flight, or a sustained run on a borrower's currency could easily lead to the failure of an otherwise compliant sovereign borrower to meet its contractual obligations in full and on time. This is precisely what happened in previous default waves like the 1930s.[11]

The recognition of the size of foreign exchange reserves as a measure of liquidity, and of foreign exchange depletion as an immediate limitation on the ability to pay, remains remarkably absent from the economics literature, which, insofar as it discusses ability to pay at all, focuses almost entirely on national wealth as a measure of solvency. While it may be true that national wealth will on paper almost always tend to be greater than a country's total outstanding debt, making it difficult to objectively determine the long-term solvency of a sovereign borrower, such observations are ultimately beside the point. What matters in an acute debt crisis is a government's ability to redeem the bonds falling due *tomorrow*; not

10 For recent evidence, see Reinhart, Reinhart and Trebesch (2016).

11 "Many … sovereign crises are of a systemic nature, clustered around panics in the financial centers … We find that systemic crises are different. The international collapse of liquidity is at their core. Default spells and recovery rates are also affected by liquidity crashes" (Kaminsky and Vega-Garcia 2014:1).

its ability to service a long-term debt five or ten years from now, after the meager proceeds from the privatization of the Parthenon have finally been checked in. In many cases, the immediate factor inhibiting repayment is not unwillingness to pay, nor the insufficiency of national wealth, but simply the lack of available foreign exchange.

Towards a Political Typology of Default

This brings us to the final point, which is that a default arising from the inability to pay in the short term is something qualitatively different from an outright denial of liability over a long-term government debt. Moreover, this qualitative difference has crucial political implications. As it turns out, the mainstream economics literature has not just depoliticized the borrowing country, the structure of sovereign lending, the decision to repay, and the determinants of default; by defining default in purely technical terms it has also ended up depoliticizing the concept of default itself.[12] This final section of the chapter therefore aims to outline an alternative typology of default that recognizes the different forms that default can take, and that is capable of accounting for the political implications of each.

We have so far followed the literature in using default as a homogeneous catch-all term referring to the failure or refusal of a sovereign borrower to live up to its contractual obligations to repay a debt in full and on time. This standard definition, widely used in the literature, is due to Standard & Poor's, which considers a country to be in default whenever it fails to make an interest or principal payment by the contractually-specified due date (or within the stipulated grace period), *or* if its debts are restructured on terms "less favorable" than those specified in the original debt contract (Reinhart and Rogoff 2009:11; Wright

12 Grossman and Van Huyck's (1985) recognition of "excusable defaults" is a notable exception.

2010:3; Tomz and Wright 2007:353; Beers and Chambers 2006:22). While it may be easy to operationalize and quantify, the trouble with this technical definition is that it is far too broad. By lumping all defaults together into a single overarching category, the literature ends up stretching the concept beyond its proper meaning, representing what Sartori (1970) might have referred to as "a deliberate attempt to make our conceptualizations value free."

In the real world, defaults occur in many forms and guises. While few scholars make an explicit distinction between the different types of default, a small but growing body of literature has begun to recognize that "there is some controversy over how one should define a default in practice" (Miller, Tomz and Wright 2006:2-3). What especially concerns us here is the relative absence of *unilateral default* in the post-war era. Unilateral default can in turn be divided into two sub-types: it can take the form of a moratorium (a temporary suspension of payments) or of an outright repudiation, which can be defined as "a legislative or executive act of government denying liability" over its obligations (Pescatori and Sy 2007:309). Borchard (1951:129) made a similar distinction between outright repudiation ("a refusal to admit the binding character of an obligation") and simple default ("which admits the binding character of the debt but pleads inability to meet its terms"). The International Swaps and Derivatives Association (ISDA) defines repudiation as "a situation in which an authorized officer rejects or challenges the validity of one or more obligations" (Das, Papaioannou and Trebesch 2012:9). Historically, repudiations have been extremely rare, and countries have tended to reject their obligations only in the wake of wars, like Turkey after WWI; or revolutions, like Mexico in 1914, Russia in 1917, China in 1949, Czechoslovakia in 1952 or Cuba in 1960 (Sturzenegger and Zettelmeyer 2006; Bordo and Oosterlinck 2005).

In an attempt to contribute to the formulation of a political economy of sovereign debt and an appropriate conceptualization of sovereign default, tables 1 and 2 outline an alternative typology of default that breaks down and *re-politicizes* the concept by identifying four specific sub-types.[13] Unsurprisingly, a political typology of default that recognizes the differences between unilateral and negotiated default, and between rescheduling with a view to later repayment and restructuring with a view to cancelling at least part of the debt, has major political implications. Most importantly, it reminds us that sovereign default is rarely an aggressive act imposed by an all-powerful sovereign on its poor and hapless lenders; very often, a voluntary debt rescheduling or restructuring may in fact be in the enlightened self-interest of the collective of creditors. This leaves moratoriums and repudiations as the only types of default that seek to unambiguously prioritize the debtor's interests over those of its creditors, with the former deliberately shifting the costs of adjustment onto the latter. This differentiation matters because only a government that refuses to honor its debts *even if it is financially capable of doing so* can be said to be "sufficiently powerful to translate resentment into effective resistance" (Marks 1978:231).

Table 1.1 – typology of default:

TYPES OF DEFAULT	***Delay of payments***	***Debt cancellation***
Negotiated	Rescheduling	Restructuring
Unilateral	Moratorium	Repudiation

13 A further distinction that is not recognized in the tables needs to be made between domestic and external default (Reinhart and Rogoff 2008), whereby our interest – as we already established in the introduction to this thesis – is firmly on the latter, involving *international* lending by foreign creditors.

Table 1.2 – definitions of default:

TYPES	*Description*
Rescheduling	A rescheduling is a negotiated agreement with creditors to delay payments on (part of) the outstanding debt by extending maturities and/or amortization schedules on existing contracts with a view to repaying the debt in full at a later date. Reschedulings are agreed to by creditors primarily to bridge periods of illiquidity and do not involve any reduction in the face value of the debt (although the extension of maturities may still involve creditor losses on interest).
Restructuring	A debt restructuring is a negotiated agreement with creditors to cancel (part of) the outstanding debt by writing down or "forgiving" obligations with a view to securing full repayment on the remaining debt at a later date. Restructurings are pursued primarily to deal in orderly fashion with insolvency and can take place either through a reduction in face value or a lowering of interest rates. They are also referred to as "haircuts", "orderly defaults", or "debt reduction".
Moratorium	A debt moratorium is a unilateral suspension of payments by the debtor of (part of) the contractually specified interest and/or principal payments with a view to resuming debt servicing at a later date. As such, moratoriums involve the debtor's attempt (either explicitly declared or implicitly enacted) to bridge a period of illiquidity or fiscal stress. Moratoriums do not involve any reduction in the face value of the debt (although the confrontational delay of payments may still involve creditor losses on interest).
Repudiation	A debt repudiation is a unilateral cancellation by the debtor of (part of) its outstanding debts with a view to never repaying them. As such, repudiations involve a formal statement, publicly declared by an authorized official, in which the government explicitly denies liability over (part of) the state's obligations, regardless of its capacity to honor these obligations or the creditors' willingness to accept the government's rejection of liability.

CHAPTER II:

The Structural Power of Finance

Business Power and the Capitalist State

As we established in the previous chapter and in the introduction, the management of sovereign debt crises is by its definition always a highly political affair involving social conflicts and fierce power struggles over who is to bear the costs of adjustment. It is therefore clear that the study of sovereign debt, and of political economy more generally, cannot proceed without a proper appreciation of the centrality of business power to redistributive conflicts, and of the particular ways in which the policy responses to international debt crises are conditioned by the distribution of power and interests in the structure of the global political economy. Yet the literature on sovereign debt has largely ignored questions of structure and power, just as the political science literature has increasingly abandoned the study of corporate influence on policymaking. As Culpepper (2011:185) writes, "the study

of business power is currently more neglected than it has been for the last half century." This study aims to contribute to the recent revival of scholarly interest in business power by situating the study of sovereign debt firmly within a number of long-standing debates on the nature of the capitalist state, the privileged position of business in capitalist democracy, and the ways in which the two have been impacted by globalization and financialization.

The first part of this chapter will present an overview of the main political science debates on business power and the capitalist state. The second section shifts the analysis towards the international level and considers how globalization and financialization have impacted the autonomy of the state and the power of finance. This section also introduces Streeck's concept of the debt state. Finally, after outlining the shortcomings of original formulations of the structural power hypothesis, the final section outlines the main theoretical contribution of this thesis: its emphasis on the mechanisms through which the structural power of finance operates and the conditions under which these mechanisms are effective and under which they are not. This section introduces the three hypothesized enforcement mechanisms of debtor compliance mentioned in the introduction: (1) the market discipline enforced by an international creditors' cartel; (2) the policy conditionality imposed by the international lender of last resort; and (3) the privileged position of wealthy domestic elites capable of fulfilling a bridging role towards foreign lenders.

Polyarchy: Robert Dahl and the Pluralist Approach

The origins of contemporary political science literature on business power are often traced back to a classical debate between the pluralists and the elite theorists; a debate that reached an early apotheosis in landmark studies by C. W. Mills (1956) and Robert A. Dahl

(1961). Analyzing the concentration of political power in the hands of a small “inner circle” of businessmen, bankers, military officials and party leaders, Mills had tried to demonstrate how US policymaking was slanted in favor of a powerful minority, highlighting the fundamentally undemocratic nature of American politics. Against Mills and the Marxists, Dahl forcefully contended that theories of elite power and class domination ignored conflict *among elites*, rendering the entire concept of a dominant class problematic to begin with. Dahl and his pluralist followers stressed divisions within business itself, with different firms and sectors pursuing their own particular interests, vying for political influence not only against other groups like trade unions or civil society organizations but also amongst themselves. For the pluralists, business could therefore not be seen to wield any extraordinary power compared to other organizations; it is just an interest group like any other.

Capitalist democracy, then, is conceived of as “polyarchy,” or the rule of many. It is portrayed as a relatively balanced multi-polar system in which contending interest groups compete for specific policy decisions and state power more generally, allowing no single group to ever become fully dominant over the others. In Dahl's (1959:36) formulation, the idea of polyarchy means “that there are a number of loci for arriving at political decisions ... businessmen, trade unions, politicians, consumers, farmers, voters and many other aggregates all have an impact on policy outcomes.” Moreover, pluralism contends that “none of these aggregates is homogeneous for all purposes; that each of them is highly influential over some scopes but weak over many others; and that the power to reject undesired alternatives is more common than the power to dominate over outcomes directly” (*ibid*). Dahl and the pluralists thus sought to disarm the Marxist theory of elite domination by shifting attention away from the relations of production and focusing narrowly on the importance of business conflict in the political sphere, which its proponents claimed to be evidence for

the fact that capital as a conceptual category is simply too broad and too vague to allow for careful and sophisticated empirical analysis of when business interests do and when they do not win out (Vogel 1987). The implicit value statement behind the pluralist approach is that while the ideal of a thoroughly democratic polity may be fundamentally unattainable, polyarchy contains within its institutional design a sufficient set of checks and balances to guarantee at least an acceptable degree of democratic accountability.

Perhaps most importantly, however, the pluralists challenged the Marxist *method*, narrowing the concept of power to those forms that can be easily observed and wielding their empiricism as a powerful weapon against the Marxists' excessively theoretical analyses of class-based power. For the pluralists, the influence of business on the political process is conceived in Weberian terms as a form of *relational power,* wielded "instrumentally" by its bearer, in the sense that power is conceived to be at play only when actor A mobilizes its resources in order to intentionally force actor B to do something they would not otherwise have done. This instrumentalist conception of power, however, had already been criticized by Bachrach and Baratz (1962) for eliminating the possibility of analyzing less direct forms of power. Specifically, Bachrach and Baratz observed that power is not just about making decisions but also about what Schattschneider (1960) called the "mobilization of bias" into the institutional fabric of communities; not only about what is organized into the political process but also about what is organized out – the *non-decisions*, in short. Power is not just about A affecting the choices of B directly, but also about A indirectly reinforcing certain institutional practices and social values that limit the scope of the debate to those options that narrowly serve its own interests against those of others. In a word, power is equally about the ability to *set a political agenda* to which others have to adhere. "To the extent that A succeeds in doing this," Bachrach and Baratz (1962:170) wrote, "B is prevented, for all

practical purposes, from bringing to the fore any issues that might in their resolution be seriously detrimental to A's set of preferences." This form of agenda-setting power has since become known as the second face of power. In yet another important contribution, Lukes (1974) subsequently took Bachrach and Baratz to task for not going far enough, proposing a third face of power that explicitly recognized the existence of latent conflict and the possibility that perceived (subjective) interests and real (objective) interests may diverge. Lukes' schema therefore allowed for the exercise of power to be *internalized* subconsciously among subjected actors, in much the same way as Foucault had theorized.

The State-as-Object: Miliband and Instrumental Marxism

It took nearly a decade for the Marxists to conjure up a retort to their pluralist critics, but when they did, the response made waves in social science departments around the English-speaking world. In 1969, Ralph Miliband published his groundbreaking study *The State in Capitalist Society*, which was purposefully formulated as an argument against the dominant pluralist paradigm of the time. Echoing the power elite theory of C. W. Mills, Miliband set out to disprove Dahl's "plural elites" thesis by identifying, through careful empirical investigation, the predominance of capitalist elites – united through their shared ideological, educational and professional backgrounds – at the apex of the state apparatus. Far from being populated by the "many," as proponents of polyarchy had argued, Miliband showed how state institutions were in fact dominated by a tightly-knit minority of wealthy businessmen. Miliband (1969:23) thus identified the existence of a capitalist class that "owns and controls the means of production and ... is able, by virtue of the economic power thus conferred upon it, to use the state as its instrument for the domination of society."

In itself, Miliband's theoretical argument was not particularly innovative. Sweezy (1942) had summarized the instrumentalist view long before when he described the state as "an instrument in the hands of the ruling class for enforcing and guaranteeing the stability of the class structure itself" (cited in Barrow 1993:13). What made Miliband's intervention particularly relevant, however, was his strong commitment to an empiricist methodology and the wealth of evidence he produced in defense of this controversial ruling class hypothesis. As Barrow (1993:25) points out, Miliband took as his key indicator of the power of business "the degree to which members of the capitalist class control the state apparatus through interlocking positions in the governmental, administrative, coercive, and ideological apparatuses." This led Miliband and his followers to adopt a particular interest in – and a narrow focus on – the social composition of the state elite. Since Miliband considered state power to be located within the state apparatus, the question who controlled its various branches logically became the main subject of inquiry. This, in turn, justified the empiricist focus on the "colonization" of state institutions by members of the capitalist class.

After an extended period of relative scholarly forgetfulness, Miliband's propositions have recently resurfaced with the emergence of new empirical evidence in their favor. In a breakthrough statistical study, Gilens and Page (2014:1) now find that "economic elites and organized groups representing business interests have substantial independent impacts on US government policy, while average citizens and mass-based interest groups have little or no independent influence." The authors – whose research builds on multivariate analysis of 1,779 policy issues between 1982 and 2002 – note that their findings "provide substantial support for theories of Economic Elite Domination and for theories of Biased Pluralism" (*ibid.*). Citing Miliband and the instrumental Marxists, Gilens and Page conclude that the US – far from being a polyarchy – in fact constitutes an *oligarchy*: the rule of the few.

The State as a Social Relation: Poulantzas and Structural Marxism

But Miliband's instrumentalist approach was never without its critics. No sooner than his book had been published, a critique appeared in the *New Left Review* penned by the Greek political theorist Nicos Poulantzas (1969) – influenced by the Althusserian school of structural Marxism (Althusser 1965; Althusser and Balibar 1970) – who took Miliband to task for ceding far too much methodological ground to the pluralists. For Poulantzas, the narrow focus on elites at the expense of a more theoretical investigation of class structures and the specifically capitalist nature of the state apparatus, risked reproducing an unspoken assumption in the pluralist literature, namely that "social classes or 'groups' are in some way reducible to inter-personal relations" (Poulantzas 1969:70). Poulantzas praised Miliband for "demystifying" the myth of polyarchy, but at the same time accused him of confusing cause and effect: the direct participation of capitalist elites in the state apparatus, he argued, is not the *reason* for its power but its logical *outcome* (Poulantzas 1969:73).

For Poulantzas, Miliband's narrow focus on actors and groups at the expense of class relations and structures and his definition of the state apparatus as a "state within capitalist society" failed to emphasize and identify the uniquely capitalist nature of the modern state (Jessop 1977:361; Barrow 1993:46). Instead, Poulantzas and the structural Marxists defined the relationship between the capitalist class and the state as an *objective relation* that cannot be reduced to inter-personal relations, the direct participation of capitalist elites in the state, or "the *motivations of conduct* of individual actors" (Poulantzas 1969:70). Pointing to all the Socialist and Communist parties that had conquered state power and had nevertheless failed to fundamentally transform capitalist relations of production, Poulantzas wanted to show that "far more must be at work in the operations of the state and social policy than mere

occupation of the state apparatus by the personnel of a particular class" (Barrow 1993:46). A result of this original formulation was that Poulantzas' earlier work, by appearing to deny the role of state administrators, had fairly strong structuralist overtones (Jessop 1982:223).

Poulantzas was quick to abandon this Althusserian functionalism, however, and by the time of his last major work he had come to think of the state as a *social relation* whose "substantive unity [is] historically contingent and thus an empirical question that cannot be assumed away" (Bratsis 1999:167). In *State, Power, Socialism,* Poulantzas (1978) importantly defined the state as "a relationship of forces, or more precisely the material condensation of such a relationship among classes and class fractions, such as this is expressed within the state in a necessarily specific form," adding that, "by grasping the state as the condensation of a relationship, we avoid the impasse of that eternal counterposition of the state as a thing-instrument and the state as a subject" (Poulantzas 1978:129). In this reformulation, the state becomes less of a functional necessity for the reproduction of capitalist relations of production and more like a material condensation of a long history of class struggle. With the nature of the state considered to be historically contingent on the outcome of concrete conflicts between opposing social forces, the deterministic overtones of Poulantzas' earlier work are replaced with a dialectical understanding of class struggle and collective agency as the motor of history. The capitalist state is no longer just "the state of the capitalists"; it is now shot through with the inherent contradictions of the class relation (Carnoy 1984:98). As Bratsis (1999:168) put it, "since within and between state institutions various classes are engaged in struggle, no one class will have complete control of all the state institutions." Workers' militancy and social movements thus become central in Poulantzas' later work, as the state becomes a *site of struggle* where power is continuously contested from below.

Public Finance: O'Connor and the Structural Dependence of the State

The Miliband-Poulantzas debate dominated the study of the capitalist state for much of the past half-century. Yet, for all the obvious differences between them, there was one remarkable similarity that somehow managed to escape many thoughtful commentators: the insistence on the conceptual distinction between the categories of the political and the economic; between state and capital. As Lasslett (2014:1) noted in a recent contribution, "Marxist state theory has a tendency to treat the modern state as a distinctly political organ disaggregated, relatively speaking, from the economic structure of society." This tendency probably finds its clearest expression in Poulantzas' (1978:54) definition of the state as "a specialized and centralized apparatus of a peculiarly political nature, comprising an assemblage of impersonal, anonymous functions whose form is distinct from that of economic power."[14] In a contemporary critique, Holloway and Picciotto (1978:3) argued that both Poulantzas and Miliband suffered from "an inadequate theorization of the relation between the economic and the political as discrete forms of capitalist social relations." By failing to clearly articulate how state and capital are actually interrelated and deeply interconnected in practice, both sides of the debate ended up reifying a false dualism. If we are to take our critique of political economy seriously, Holloway and Picciotto insisted, we should "break out of this dichotomy by developing an adequate theory of this relation" (*ibid.*).

What is perhaps most remarkable, in this respect, is that neither Miliband nor Poulantzas ever really raised the question how the state is funded. Yet is is precisely here, in the somewhat arcane realm of public finance, that the intricacies of the state-capital relation

14 The citation continues: "The specificity of the modern state therefore refers precisely to the relative separation of the political from the economic, and to the entire reorganization of the respective spaces and fields implied by the total dispossession of the direct producer in capitalist relations of production" (Poulantzas 1978:54, cited in Lasslett 2014:1; see also Tabak 1999:140).

most explicitly come to the fore. As Krätke (2009:5) notes, "the modern state's power to tax [and to borrow] provides an excellent link between economic and political theory proper." After early contributions by Schumpeter (1918) and Goldscheid (1919), the first scholar to properly probe into public finance from a critical perspective was James O'Connor (1973). In *The Fiscal Crisis of the State,* the American sociologist observed a contradiction between the state's two main functions: *legitimization*, on the one hand, and *accumulation*, on the other. If the state fails to establish legitimacy, he noted, it will end up undermining its basis of popular support; if it fails to recreate the conditions for capital accumulation, it "risks drying up the source of its own power, the economy's surplus production capacity and the taxes from from this surplus (and other forms of capital)" (O'Connor 1973:6). The state therefore finds itself in a bind: on the one hand, its legitimization function compels it to respond to ever-growing demands for new spending; on the other, its accumulation function prevents it from taxing capital sufficiently to finance this increase in public expenditure. The result, for O'Connor, was the fiscal crisis of the state, resulting in a stagnation of growth on the one hand and a deepening legitimation crisis on the other.

While this fiscal crisis did not (immediately) materialize in the 1970s, O'Connor did identify a number of elements in the state-capital relation that are of great relevance to the study of business power today. The most important relates to the sources of public revenue. O'Connor noted that the state can finance itself in three ways: through the operation of state-owned enterprises, through taxation, and through public borrowing. All three directly position the state within the process of capital accumulation. To reproduce itself – in other words, to be able to maintain its basic administrative functions and its various budget outlays – the state is compelled to produce its own surpluses, claim part of the existing economic surplus in taxes, and convince capitalists to recycle their untaxed surpluses by lending

them to the state against a pledge of future tax revenues. Since the latter, public borrowing, did not play a big role at the time, O'Connor paid relatively little attention to it. Still, he rightly observed the contradictory nature of public debt, which both enables and constrains state power: "on the one hand, the growth of state debt gives the treasury more power in monetary and fiscal planning. On the other, the institution of the debt normally tightens capital's grip on the state" (O'Connor 1973:188; see also Dyson 2014:34). The same paradox was captured by Ernest Mandel (1971:16) in his metaphor of the public debt as "the golden chains of capital," tying the state to business and *vice versa*. As Mandel explained:

> *No government could last more than a month without having to knock on the door of the banks in order to pay its current expenses. If the banks were to refuse, the government would go bankrupt. The origins of this phenomenon are twofold. Taxes don't enter the coffers every day; receipts are concentrated in one period of the year while expenses are continuous. That is how the short-term public debt arises ... But there is another problem – a much more important one. All modern capitalist states spend more than they receive. That is the long-term public debt for which banks and other financial establishments can most easily advance money, at heavy interest. Therein lies a direct and immediate connection, a daily link, between the state and big business.*

While other scholars did not specifically identify the importance of public debt, this deep connection between big business and the state came to be known in Marxist circles as the "structural dependence of the state on capital" (Przeworski and Wallerstein 1988). This concept of structural dependence highlights the fact that capitalists must continuously be induced to lend and to invest; in other words, the state must at all times try to produce and reproduce the ideal conditions for the accumulation of capital. As Przeworski (1980:55) put it, "as long as the process of accumulation is private, the entire society is dependent upon maintaining private profits and upon the actions of capitalists allocating these profits." It is is this structural dependence of the state that ultimately provides business with the unique form of power it wields under capitalism: structural power.

The Market as Prison: Lindblom and the Privileged Position of Business

It was in this intellectual environment of burgeoning critical scholarship on business power and the capitalist state – and in the real-world context of growing capital mobility *within* states – that Charles Lindblom, one of the founding fathers of the pluralist tradition in political science, slowly became aware of the inherent limitations of his own approach. In his classic work, *Politics and Markets* (1977), Lindblom famously distanced himself from his friend Robert Dahl by contending that business in fact occupies a "privileged position" in capitalist democracy. Identifying a key puzzle left unresolved in the pluralist literature, Lindblom starts out by asking why – if no social group is dominant in polyarchy – not a single democratic polity has ever voted to abolish private property and socialize its means of production. Noting that such a decision could potentially be favored by a majority of voters, who are workers, but that it would at the same time spell catastrophe for private business, Lindblom poses a simple question: could it actually be business that calls the shots in capitalist democracy? "At this point," Lindblom (1977:179) writes, "we must consider the possibility that existing polyarchies are not very democratic, that political debate in them is not very free, and that policymaking in them is actually in the hands of persons who want to protect the privileges of business and property."

In Lindblom's new conceptualization of polyarchy, then, the market becomes like a prison – effectively locking in the political process by structurally enthralling policymakers to business interests (Lindblom 1982). The most remarkable thing, Lindblom argued, is that this disciplinary power of markets is brought to bear immediately, automatically and often unintentionally. "Punishment is not dependent on conspiracy or intention to punish," he wrote. "Simply minding one's own business is the formula for an extraordinary system for

repressing change" (*ibid*:237). State managers find themselves faced with the imperative to maintain a healthy investment climate under all conditions, and to immediately restore business confidence whenever key indicators start trending downwards. As Block (1987:8) later summarized in a dual critique of Miliband and Poulantzas, "it appears that even when the business community is not able to influence the state in the traditional ways," through lobbying, staffing government positions, drawing on personal contacts and doling around campaign contributions, "policy outcomes [still] tend to be favorable to business concerns." This, he observed, suggests that "there are 'structural' factors that operate at a different level from the exercise of personal influence. Even with a change in government personnel, the power of business would continue to have a large influence over governmental policies." Business, scholars like Lindblom and Block noted, is different from any other interest group because – as the primary source of investment – it fulfills a key public function in the capitalist economy. Businessmen allocate investment and thereby determine outcomes, reflected in a number of key socio-economic indicators. Policies or regulations that counter business interests could trigger divestment, which would negatively affect growth, employment and approval ratings. Since elected leaders generally depend on a healthy economic environment for their re-election, they will try everything in their power to "convince managers to keep business firing on all cylinders" (Culpepper 2008:7). Crucially, this mechanism appears to operate irrespective of the ideology or partisan affiliations of those in power; it is the mere possibility or treat of divestment that forces officials to "anticipate and defer" to business interests. It was this insight that led Lindblom (1977:175) to argue that "businessmen cannot be left knocking at the doors of the political systems, they must be invited in."

Globalization, Financialization, and the Debt State

By the 1990s, however, both the study of the capitalist state and Lindblom's thesis of the privileged position of business had largely fallen out of fashion in political science, even as numerous scholars began to note the increasing leverage of multinational firms over national states (e.g. Gill 1992; Cerny 1993; Ohmae 1995; Korten 1995; Gill 1995; Strange 1996; Pauly 1997; Cohen 1998; Hardt and Negri 2000). As it turned out, the main weakness of the structural power hypothesis – or at least the way it was interpreted in subsequent scholarship – was that it put too much emphasis on the independent and automatic nature of market punishment. In short, Lindblom's conceptualization of the "market as prison" and Block's invocation of an "investment veto weapon" were seen to suffer from deterministic overtones. Even though Lindblom explicitly recognized the possibility that policymakers sometimes act *against* business interests – noting that wherever there are prisons there will also be prison breaks – he never specified when business is likely to win out and when it is not. Culpepper (2011:185) has noted how as a result "theories of the structural power of business have been marginalized in the face of careful studies showing how often business organizations fail to get what they want." The question, then, is why the structural power of business varies in practice.

The Impossible Trinity and the Capital Mobility Hypothesis

Over the years, the globalization literature has provided at least one possible answer to this question. As Winters (1996:16) noted, Lindblom's thesis was ultimately plagued by a "narrow focus on single jurisdictions." Its closed economy model recognized the ability of business to reduce overall investment through less vigorous economic activity, or to move

state, but left out the possibility that mobile capital – instead of slamming on the brakes or relocating domestically – might simply move out to another country altogether. "Especially in light of changes occurring in the global political economy," Winters (1996:17) wrote, "this missing element of the model is particularly limiting." Starting with the emergence of the Eurodollar markets in the 1960s and the breakdown of the Bretton Woods regime in the early 1970s, and culminating with the widespread abolition of capital controls and financial deregulation in the 1980s and 1990s, capital had started increasingly to flow across borders, always in search of the highest yields and the path of least resistance. According to Winters (1996:21-22) and others, this international mobility greatly contributed to the structural power of capital, as it added the option of relocation – and thus a credible exit threat – to the traditional "veto weapon" of the investment strike. As Hirschman (1970:82) famously argued, voice is "appreciably strengthened if [it] is backed up by the *threat of exit* ... whether it is made openly or whether the possibility of exit is merely well understood to be an element in the situation by all concerned." This body of literature therefore concludes that, by providing business with an exit option, "financial globalization enhances the authority of market agents at the expense of sovereign governments" (Cohen 2012:175).

Given the centrality of the concept of international capital mobility to its analytical scheme, much of the globalization literature has built – either explicitly or implicitly – on the core ideas expounded in the Mundell-Fleming model and its "impossible trinity" of monetary policy autonomy, fixed exchange rates and free capital flows, which holds that only two of these three policy objectives can ever be realized at any given time (Fleming 1962; Mundell 1963). In other words, a government pursuing both high capital mobility and fixed exchange rates will have to sacrifice monetary policy autonomy. This dynamic was famously observed in the case of Mitterand's attempted socialist reforms in France,

when the pressure of globalizing capital markets, combined with France's participation in the European Exchange Rate Mechanism, forced officials to accept "that their preference for national monetary autonomy was unrealistic" (Goodman and Pauly 1993:75). Rodrik (2011) has more recently extended this Mundell-Fleming model into what he calls the "political trilemma of the global economy," identifying a similar three-way tension between national self-determination, deep economic integration and democratic politics.

But the core argument of the globalization literature is probably best summarized in the so-called "capital mobility hypothesis," which holds that "the degree of international capital mobility systematically constrains state behavior by rewarding some actions and punishing others," as a result of which "the nature of the choice set available to states ... becomes more constricted" (Andrews 1994:199). Hacker and Pierson (2002:282) argue that "capital mobility is a key – and highly variable – element of business' structural position," and conclude that in a context of low mobility business loses its privileged position and ends up looking more like a traditional interest group, whereas in a context of high capital mobility it can wield its credible exit threat to enhance its structural power in regulatory and redistributive conflicts. Be that as it may, it is clear that the capacity of multinational companies to relatively effortlessly relocate capital from one jurisdiction to another creates additional competitive pressures on states, pushing them "to accommodate the preferences of market actors by liberalizing (or in other words, lowering) their regulatory standards" (Andrews 1994:199), a process that has been referred to as the "competitive re-regulation" of domestic markets (Cerny 1993). By transforming the incentive structure and reducing the ability of individual states to effectively regulate, control or tax mobile capital, it is claimed that globalization systematically favors the interests of multinational corporations over those of domestic constituents (Underhill and Zhang 2008; Rodrik and Subramanian 2009).

Structural Power in the Global Political Economy

One scholar who took a particularly strong interest in the growing tensions between globalized markets and national states was Susan Strange. Such was Strange's concern with the role of multinational corporations and big banks in international affairs that she ended up playing a leading role in the creation of a new academic discipline to study its causes and consequences. Credited as one of the co-founders of the discipline of International Political Economy (IPE), Strange is also remembered as the most vocal proponent of the structural power hypothesis (Keohane 2000). Setting out her critique of IR scholarship with an attack on the one-dimensional conceptualization of power in the dominant theoretical traditions of realism and neoliberal institutionalism, Strange argued that there are really two forms of power: what she called relational power, which corresponds to the first face of instrumental power in the political science literature, and structural power, which she described as "the power to shape and determine the structures of the global political economy within which other states, their political institutions [and] their economic enterprises ... have to operate." Structural power is "the power to decide how things shall be done, the power to shape frameworks within which states relate to each other, relate to people, or relate to corporate enterprises" (Strange 1998:25). Like Lindblom, Strange emphasized how this form of power is wielded by businesses, and like Lindblom, she proclaimed that its exercise need not reflect direct, intentional action on the part of its bearer (Lawton, Rosenau and Verdun 2000:5). As Kirshner pointed out, Strange thought of structural power much as Woody Allen conceived of aspiring playwrights: 90 percent of the job is just showing up (Kirshner 2009:208).

Structural power, then, is very different from instrumental power in the sense that it does not require any coercive action on the part of its bearer for it to be effective; it is

operative even when A cannot be observed to exercise direct control over B (Walter 2001:7). As a result, the conceptual emphasis shifts from the resources of actors and their behavior *vis-à-vis* one another towards the systems in which they are embedded (Keohane 2000:x). Most importantly, different structural positions do not endow equal privileges; rather, they distribute *asymmetric privileges*, as a result of which some gain a systematic advantage over others. The classical examples include what Barnett and Duvall (2005:53) refer to as the "co-constitutive internal relations of structural positions" between master and slave, or between capital and labor – the nature of both elements in the equation being generated through the symbiotic yet conflictive relationship of domination or exploitation of one by the other. The same type of conflictive co-constitutive relations can be said to sustain the structural positions of debtors and creditors. Even if the two formally enter into the market as equals, only the creditor has the capacity to create credit (Graeber 2011; Lazzarato 2012). Since the borrower, by contrast, depends on this credit to be able to reproduce itself, the creditor has a structural advantage over the debtor. Its capacity to withhold something upon which the other depends endows it with a peculiar form of power: the power to punish by *not doing*; the power to discipline through refusal; the power, in other words, to dominate simply by "being there." The concept of *structural* power serves to capture this underlying asymmetry.

The main element in Strange's conceptualization of structural power is that it allows its bearer "to change the range of choices open to others, without apparently putting pressure directly on them to take one decision or to make one choice rather than others" (Strange 1988:31). The policy options of national government are structurally constrained by globalized market forces raising the costs or risks associated with one course of action while structurally incentivizing another (Story 2000:32). Through a mechanism of reward and punishment not unlike the one proposed by Lindblom, structural power thus alters not

only the capacities and options but also the interests of subjected actors (Waltzenbach 2000; Kirshner 2005). By raising the costs of a potential course of action sufficiently high, those possessing structural power can alter the cost/benefit calculation of subjected actors to the point where acting in one's self-interest becomes all but inconceivable. Structural power, then, can be said to impose "a bias on the freedom of choice" (Strange 1994:31). Crucially, Strange argued that, while international affairs used to rely on more coercive forms of state power like gunboat diplomacy and outright imperialism, globalization has given rise to the growing importance of less visible forms of power: "in the competitive games now being played out in the world system between states and between economic enterprises, it is increasingly structural power that counts far more than relational power" (Strange 1998:25).

In the epic struggle between states and markets, Strange reserved a special place for the financial structure, which she considered to be "*the* prime issue of international politics and economics," for whoever controls the creation of credit controls the purchasing power and policy options of its borrowers (Lawton 2000:32). Credit, Strange never tired of saying, "is literally the lifeblood of a developed economy." The imperative to keep it circulating through the world economy leads to a situation in which the ability to *deny* credit becomes a key source of structural power. And yet this form of power has been all but ignored in the literature on sovereign debt; insofar as the question of power is touched upon at all, it tends to be in purely relational and state-centric terms (Strange 1988:91; Helleiner 2005a). "What has been much less obvious to IPE scholars," Strange (1991:35) wrote after the 1980s debt crisis, "was the structural power exercised by whoever or whatever determined the financial structure, especially the relations between creditors and debtors." In the quest for credit, all countries will be forced to "dance to the fast or slow rhythms of financial markets," and all states ultimately "run up against the limits set by international finance" (Strange 1998:180).

It is probably safe to say that "the skewed impact of the international financial structure is nowhere more visible than in the impact of international debt" (Leander 2000:350).

Neoliberalism, Financialization, and the State-Finance Relation

Strange's work therefore provides a useful starting point for a political economy approach to sovereign debt and default, but it is not without problems of its own. For one, scholars have in recent years come to recognize the limits of the concept of globalization. In the wake of the 2008-'09 financial crisis it has become increasingly difficult to speak of a "retreat of the state," as Strange (1996) and much of the globalization literature did. In fact, the record bailouts of private financial institutions after the Lehman Brothers collapse have made it amply clear just how central the state really remains within the globalized market economy. In fact, many now argue that, far from being on the retreat, the state apparatus – and the US state in particular – has been foundational to the rise of neoliberalism and the process of financial globalization (e.g., Krippner 2011; Duménil and Levy 2011; Panitch and Gindin 2013). This problematization of the globalization hypothesis has in turn prompted a growing interest in the related concept of *financialization*, which – its proponents argue – allows for a more fine-grained understanding of the recent transformations of capitalism. As Lapavitsas (2013:194) stresses, the period of globalization has principally been characterized by the "ascendancy of finance," which is precisely what financialization aims to capture.

While the exact meaning of the concept continues to be debated, financialization has been defined as "the increasing importance of financial markets, financial motives, financial institutions, and financial elites in the operation of the economy and its governing institutions, both at the national and international level" (Epstein 2001:1); as "a pattern of accu-

mulation in which profits accrue primarily through financial channels rather than through trade and commodity production" (Krippner 2005:174, see also Arrighi 1994); as "a process whereby financial markets, financial institutions, and financial elites gain greater influence over economic policy and economic outcomes" (Palley 2007:1); as "a broad-based transformation in which financial activities ... become increasingly dominant" (Krippner 2011:2); or even as "a systemic transformation of capitalism, as a historical period" (Lapavitsas 2014). Despite the lack of scholarly agreement on a common definition, one advantage of the term is that it allows for a more nuanced and more focused understanding of the beneficiaries of recent transformations in the capitalist world economy.

In contrast to the globalization literature, which had a tendency to conceptualize the relation between nation states and global financial markets in terms of a dichotomy of two opposing and mutually exclusive forces, recent literature tends to conceive of the relation in terms of a symbiosis or mutual dependency (Wade 2014; Mügge 2010; Harvey 2010; see also earlier work by Wade and Veneroso 1998 on the "Wall Street-IMF-Treasury complex"). Far from hailing the retreat of the state, then, the process of financialization seems to involve its ongoing *restructuring*; with notable consequences for the distribution of power in the global and national political economy. As Krippner (2005:181) observes, "one would expect that social actors occupying strategic positions *vis-à-vis* privileged sites of accumulation [banks, hedge funds, rating agencies] would accrue political and economic power." However, since these financial actors continue to depend on active state intervention and market-making, this power does not stand in isolation. As Culpepper (2015:399) notes, "the structure of the capitalist system is one in which each [state and finance] depends on the other. Studying structural power means being attentive to the political implications of both elements of this mutual dependency." Without the bank bailouts of 2008, for instance, many financial firms

would simply have gone out of business; a form of dependence that provided the structurally powerful US state with an unexpected opportunity to exact concessions from rescued banks (Culpepper and Reinke 2014). Even before the bailouts, Foster (2007:6) observed that "the state's role as lender of last resort, responsible for providing liquidity at short notice, [has been] fully incorporated into the system." And as the "guardians of financialization," central banks in particular have seen their role transformed in recent years: "Protected from electoral scrutiny through legal and practical independence, they have focused on inflation targeting, while casting a benign eye on the speculative excesses of finance. Once the crisis broke, they proved instrumental to mobilising social resources in order to rescue financiers, drawing on their monopoly over the issue of inconvertible legal tender" (Lapavitsas 2008:3).

The Debt State and the Rise of the Marktvolk

In recent years, this thorough restructuring of the capitalist state caught the eye of the German sociologist Wolfgang Streeck. In a series of recent interventions, Streeck has explored how the process of financialization has impacted the politics of public debt and the deep-seated tensions between capitalism and democracy, especially in the context of the Eurozone debt crisis. For Streeck, the present turmoil is a belated manifestation of the fiscal crisis predicted by O'Connor in the early 1970s. O'Connor's prediction was partly borne out at the time: while budget deficits in OECD countries had not exceeded 1 percent of GNP prior to the early 1970s, they rose to 3-4 percent by the mid-1970s and up to 4-5 percent by the 1980s (Krätke 2009:19), but O'Connor appears to have erred on two counts. First, it was not rising demand for public spending that drove the state into fiscal crisis, but stagnating or even falling revenues as a result of business and the wealthy escaping taxation.

Second, O'Connor had seemingly failed to anticipate the extent to which the resultant deficits could be plugged through vast increases in public borrowing, "buying time" and staving off the moment of reckoning. Streeck (2011:14) shows how expanding the "[p]ublic debt turned out, for a while, to be a convenient functional equivalent of inflation, [making] it possible to introduce resources into the distributional conflicts of the time that had not yet in fact been produced." The result of this state borrowing, Streeck (2014:72) argues, was a "transformation of the tax state into a debt state – that is, a state which covers a large, possibly rising, part of its expenditure through borrowing rather than taxation," contributing to a growing "debt mountain that it had to finance with an ever greater share of its revenue."

This transition towards the debt state is not just a fiscal development; it should be seen as "the rise of a new political formation with its own laws," whose defining feature is the emergence of the *Marktvolk* as a second constituency alongside the *Staatsvolk*. "In contrast to the *Staatsvolk* of the tax state," Streeck (2014:73/80) writes, "the *Marktvolk* of the debt state is transnationally integrated. They are bound to national states purely by contractual ties, as investors rather than citizens ... As creditors, they cannot vote out a government that is not to their liking; they can, however, sell off their existing bonds or refrain from participating in a new auction of public debt." It is this structural power, derived from the ability to withhold credit, that provides the *Marktvolk* with a privileged position in the governance of the debt state. This privileged position far exceeds anything investors enjoyed in the tax state. Streeck argues that "the emergence of finance capital as a second people ... marks a new stage in the relationship between capitalism and democracy, in which capital exercises its political influence not only indirectly (by investing or not investing in national economies) but also directly (by financing or not financing the state itself)." As a result of its dependence, the debt state "must take care to gain and preserve [investor] confidence, by

conscientiously servicing the debt it owes them and making it appear credible that it can and will do so in the future as well" (Streeck 2014:80-81). Indeed, "the first priority of the international community of debt states is that all members, including the weakest, maintain the fullest possible servicing of their existing debt" (Streeck 2014:93).

However, *qua* democracy, the debt state also retains a legitimization function that it somehow has to fulfill in a context of growing constraints on public expenditure, forcing officials to perform a precarious balancing act between maintaining the loyalty of their citizens while at the same time retaining the confidence of private creditors: "Which of the two sides commands greater attention from a debt state's government will depend on their relative strength. This in turn depends on how likely a threatened withdrawal of confidence or loyalty, respectively, appears to be, and on how much pain it would cause to the country and its government" (Streeck 2014:83-84). The conclusion is that a distressed debt state will only ever choose to renege on its commitments to private creditors when the social costs of repayment have become unbearable and citizens threaten to withdraw their loyalty to the state. Only in the context of a destabilizing legitimation crisis and a democratic "rebellion" from below will the government of a debt state ever consider defaulting on its debts.

Enforcement Mechanisms of Debtor Compliance

As the preceding discussion has shown, recent innovations in the field provide ample opportunity to bring together, first, the somewhat artificially separated scholarship on business power in CPE and IPE; and, second, the equally isolated literatures on sovereign debt and the structural power of finance. However, as this chapter has demonstrated as well, the study of structural power still faces a number of hurdles and challenges. Most importantly,

as a "clunky variable" rooted in the structure of the capitalist economy that is often understood to operate in automatic fashion, original formulations of structural power left past scholarship ill-equipped to account for variation in outcomes (Culpepper 2010). The literature has suffered from deterministic overtones that have resulted in a stigmatization of the study of structural power as a whole, sapping scholarly interest in the concept and leading political scientists to discard it altogether. To salvage the important insights of the structural power hypothesis, what is needed today is a more dynamic theoretical conceptualization and a more sophisticated methodological framework that can satisfactorily account for the fact that, even if it often wins, business still ends up losing at times (Culpepper and Reinke 2014; Hindmoor 2012).

In light of this crucial theoretical question, Culpepper (2015) has recently proposed that future scholarship on structural power focus on three points. First, since the role of structural power will be most difficult to demonstrate in situations where the preferences of business happen to overlap with those of government or public opinion, future scholarship should focus its attention on those situations where business preferences actively clash with the preferences of government or public opinion. Second, scholars should aim to identify the sources of variation in structural power and demonstrate how this variation contributes to differences in outcomes between cases. Third, future work should actively distinguish structural power from instrumental power and find ways to operationalize this conceptual distinction in empirical research. This thesis takes up the challenge by deliberately focusing on the contentious politics of sovereign debt crises, which tend to involve fierce conflicts over the distribution of adjustment costs between debtors and creditors, with the latter preferring to secure full repayment and the former preferring to avoid the painful adjustments necessary to repay; by identifying the exact enforcement mechanisms through which

the structural power of finance is brought to bear on heavily indebted peripheral states and hypothesizing the precise conditions under which these enforcement mechanisms will be effective and the conditions or countervailing mechanisms under which they will tend to break down; and by conceptualizing the structural power of finance in very specific terms as the capacity of foreign lenders and domestic elites to withhold short-term credit lines on which a heavily indebted peripheral state depends for its own self-reproduction, thereby unleashing debilitating and unpredictable spillover costs that quickly ripple throughout the domestic economy, with far-reaching consequences for the borrowing state's capacity to legitimize itself in the eyes of its citizens. The next chapter on methodology will seek to operationalize this definition in the context of this research project.

But first, the following section will introduce the three enforcement mechanisms of debtor compliance – the market discipline imposed by an international creditors' cartel; the policy conditionality imposed by the international lender of last resort; and the privileged position of domestic elites capable of fulfilling a bridging role to foreign creditors – as well as the hypothesized conditions under which these mechanisms are effective and the conditions and countervailing mechanisms under which they are likely to break down.

The Market Discipline of the Creditors' Cartel

The first enforcement mechanism builds on the prior conceptualization of structural power as the ability to withhold credit to those who depend on it. One of the main reasons governments do not default is because they fear this would cut off access to *short-term* credit – not just to the government but to the private sector as well. Even if this exclusion from capital markets tends to be of a temporary nature and hence not a matter of long-term

reputation as such, it can still wreak havoc on the borrowing country by forcing its government to immediately move into fiscal balance and by provoking debilitating and largely unpredictable spillover costs that would instantly leave domestic banks, firms and households unable to obtain private financing, thereby drying up all available liquidity in the economy and bringing finance, trade, production and consumption to a grinding halt – all with potentially catastrophic consequences for the state, the economy and society at large.[15]

Here we have to quickly add that this form of "market discipline" is by no means limited to the abstract, automatic and apolitical market mechanisms that were emphasized in the original structural power literature. In fact, private creditors are capable of *deliberately* wielding their ability to withhold credit as a political weapon to force a non-compliant government back into line. In this respect, Culpepper and Reinke (2014:6) have made the useful theoretical clarification that structural power is not limited to those forms of power that are exercised impersonally and automatically; it is not simply a "background condition against which politics plays out" but "an active resource employed by business in the political arena." As such, the concept should not be defined exclusively as a Lindblom-style "automatic punishing recoil" mechanism: "although structural power can certainly work automatically, it can also be deployed deliberately, with strategic intent" (*ibid*). What makes structural power structural, then, is not the way in which it is exercised – whether strategically or automatically – but the *source* of power as such, which "flows from the economic position of the firm in an economy." In our case, the structural power of private creditors flows from the position of financial firms as the principal creators of credit money.

15 Market discipline revolves around the notion of an *immediate* cut-off of credit, even if such market exclusion is almost always short-lived (Borensztein and Panizza 2008). In this sense, it differs substantially from the reputational mechanism of Eaton and Gersovitz (1981), who emphasize *long-term* market exclusion.

The effectiveness of market discipline is in turn conditional on two factors: first, the capacity of private lenders to maintain an international creditors' cartel[16]; and second, on the debtor's dependence on this creditors' cartel for further financing. On the first point, the threat to punish a non-compliant borrower by withholding short-term credit can only be credible and effective if all creditors stop lending at the same time, maintaining their credit embargo at least until the defaulted debt is renegotiated under conditions favorable to the creditors. If a sufficiently large group of lenders break ranks and offer a defaulting state new loans on better terms in the hope of outcompeting their rivals, the threat of immediate market exclusion loses its credibility and the disciplinary mechanism will break down. It is therefore crucial that private lenders present a unified front in the pursuit of their collective interest as a creditors' cartel rather than in the pursuit of the self-interest of individual lenders competing amongst each other for market share.

This in turn raises an important question: what are the conditions under which the creditors' cartel will manage to maintain its internal coherence and what are the conditions under which it will break down? This thesis argues that the *structure of lending* and the *ownership structure* of the debt are two crucial factors conditioning the internal coherence of the creditors' cartel. To be more precise, what matters is the *concentration of the debt* (and hence the number of creditors involved) and the degree to which the international lending structure aligns creditors' interests, eases coordination and incentivizes collective action as opposed to individual free-riding.[17] When debt concentration is high and creditor interests

16 The term "creditors' cartel" originated in the literature on the 1980s debt crisis and refers to the capacity of creditors to resist incentives for individual free-riding and to act as a unified front (Griffith-Jones 1988).

17 Suter and Stamm (1992:648) hypothesized that "the degree of creditors' influence [is] determined by the actor structure or, more specifically, by the actor structure on the creditors' side ... [T]he capability of creditors to exert far-reaching influence on debtor countries and to enforce hard terms of debt settlements against the interests of debtor countries, depends upon the establishment of strong cooperative networks

are interlocked by the nature of international lending, the coherence of the cartel will be strong. If, by contrast, the debt concentration is low and the lending structure incentivizes opportunistic behavior, creditor coherence will be weak. In practice, highly concentrated syndicated lending and highly concentrated securitized bond finance will make default less likely while dispersed bond finance will tend to make it more likely. Historical research on the concentrated and syndicated lending to King Philip II of Spain by a close-knit Genoese lenders' coalition appears to confirm this observation (Drelichman and Voth 2014).

The second factor – the debtor's dependence on the creditors' cartel – in turn rests on two further conditions: the availability of an *outside option*, and the extent to which the debtor country is *self-sufficient* in financial and commercial terms. If the debtor country has an outside option – like a friendly foreign government willing and able to provide financing – or if it has enough of a buffer to absorb the shock to its economy, the opportunity cost of short-term market exclusion will be relatively low and the disciplinary force of a lender-enforced credit cut-off will be diminished. The capacity of a debtor to cushion the impact of short-term market exclusion will increase when the country is running a primary surplus (i.e, taking in more in revenues than it spends before interest); a trade surplus (exporting more than it imports); sizable foreign exchange reserves (to defend the value of the currency against devaluation pressures and to pay for crucial imports); and the capacity to provide liquidity to its own financial system (requiring control over the central bank, a relatively healthy and well-capitalized banking system, and the ability to impose capital controls in order to stem destabilizing capital flight). When these conditions all apply, the threat of a credit cut-off will lose much of its effectiveness and unilateral default becomes more likely.

among creditors. The institutionalization of such creditor clubs on their part presupposes that a relatively few actors dominate a dense interaction structure... Prior to World War II these conditions were not met."

The conclusion is therefore that the disciplinary power of financial markets will be increased when the debt concentration is high, creditor interests are aligned, and the debtor depends on the creditors' cartel for external financing. This argument is the exact opposite of claims made by scholars who hold that decentralized markets are more disciplinary than concentrated ones (e.g., Kaplan 2013). The problem with the latter view is that it rests upon a neoclassical fallacy assuming efficient markets. In reality, financial markets are prone to panics that can lead individually rational investors to collectively withhold credit when the perceived default risk rises, thereby provoking the outcome that market discipline was supposed to avoid. To prevent default, creditors need to be able to credibly threaten debtors with a cut-off in credit *while at the same time keeping the debtor solvent so it can continue to service its debts*. This is a subtle balancing act requiring a high degree of internal cohesion, creditor coordination and debtor monitoring that a diffuse body of small bondholders will find more difficult to achieve than a handful of systemically important, politically powerful and financially literate repeat players whose interests are structurally interlocked. Still, even the latter will struggle to keep a big borrower afloat when the default risk rises to the point of imminent bankruptcy: in those instances, the incentive to collectively withdraw credit in order to avoid crippling losses may simply become too great for individual market actors to counteract. This gives rise to the systemic need for an official creditor capable of acting as a lender of last resort to distressed sovereign borrowers. As Soederberg (2005:935) notes, "to recreate the power relations within the international credit system it is necessary to ensure that debtors are kept within the lending game." The market mechanism is a necessary but insufficient barrier to default – to be truly effective, it requires some counterbalance.

The Policy Conditionality of the Lender of Last Resort

The second enforcement mechanism – the direct intervention of creditor states and international financial institutions – serves to provide just that. By disbursing emergency loans to distressed sovereign borrowers under strict policy conditionality, official creditors do not merely intervene to keep the creditor solvent but also to enforce and monitor the type of policies and reforms that would free up the maximum amount of public revenue and foreign exchange for continued debt servicing. The main threat in the hands of official creditors is the same as the one that underpins the structural power of private creditors: the capacity to withhold credit in the event of non-compliance, which would leave a defaulting country without any access to external financing, inflicting debilitating spillover costs on its national economy. In the hands of official creditors, however, this threat is enhanced by the fact that emergency loans are disbursed in tranches: a debtor will only receive its next loan installment if it remains current on its obligations to private creditors and carries out the demanded structural adjustment. At the same time – unlike the market mechanism, which will tend to break down in a market panic – the discipline of official creditors is potentially endless as the latter can maintain financing even in the absence of a perspective on profits. It is also more strategic in the sense that it does not depend on any automatic mechanisms but rather on a deliberate choice to disburse or not to disburse the next credit tranche.

The role of official creditors, then, is to act as a *de facto* international lender of last resort and a fiscal disciplinarian of distressed sovereign borrowers. In the pre-war period, these key functions had been only partially, intermittently and improvisationally fulfilled by private bankers and creditor states. For much of the nineteenth century, powerful banking houses like the Rothschild and the Baring had the capacity to "implement conditio-

nality loans and monitor countries' financial policies," which "also enabled them to deal with solvency." As a result, "international capital markets could exact 'structural adjustment' from borrowing governments" (Flandreau and Flores 2011:4).[18] While this proved to be very successful for bondholders buying sovereign debt underwritten by the Rothschilds, who never faced any defaults on their claims, it did not enforce the contracts intermediated by less prestigious underwriters – hence the high prevalence of sovereign default.

In the contemporary financial structure, by contrast, all these functions – providing conditionality loans, exacting structural adjustment, monitoring finances and policies, and determining future market access – now rest with the International Monetary Fund, which has been backed in its crisis management role by the US Treasury Department and the US Federal Reserve, and which has more recently worked together with the EU creditor states and the European Central Bank in managing the European debt crisis. Thus the IMF and the creditor states provide a much-needed counterbalance to the market mechanism. The function of the lender of last resort in this respect is not limited to the money it lends to a distressed debtor; it also provides a *stamp of approval* for a debtor's finances and policies without which a borrowing government would be unable to return to the markets.

What, then, are the conditions under which the second enforcement mechanism of policy conditionality breaks down and a distressed debtor can defy the lender of last resort? This thesis argues that once again the effectiveness of the disciplinary mechanism is a factor of the debtor's dependence on foreign financing and of the capacity of official creditors to

18 The citation continues: "This occurred because of market *structure*. A few prestigious intermediaries had the ability to 'certify' a borrowing government, which enabled them to influence the terms of market access. The intermediaries thus had a measure of monopoly power over borrowers and used it to obtain adjustments that increased the likelihood of repayment. Conditionality lending was an investment in the prestigious bankers' own brand. This explains why prestigious banks were both able and willing to manage their clients' liquidity crises" (Flandreau and Flores 2011:1).

present a unified front *vis-à-vis* the debtor. The conditions for the debtor's dependence are the same as those described in the previous section, relating to its financial and commercial self-sufficiency (whether it has a primary fiscal surplus, a trade surplus, currency reserves and control over domestic liquidity). When a government has sufficient domestic buffers or alternative sources of financing, it will be less inclined to abide by the unpopular measures demanded by official creditors and may be more inclined to forego future loan installments in exchange for a recovery of national sovereignty and the capacity to shift at least part of the adjustment costs onto foreign creditors and domestic elites.

The conditions for the coherence of the official creditor front, however, are a more complicated question revolving around domestic politics in the dominant creditor countries themselves, as well as the nature of the relationship between the creditor states and the IMF. While the domestic politics of the creditor states lie outside of the scope of this study, the thesis does suggest two preliminary hypotheses. First, if the debt of the country in question is highly concentrated in a set of systemically important financial institutions in the core countries, the governments of the dominant creditor countries and the IMF will share a common interest in preventing default at all costs: the IMF because it would thereby fulfill its mission to ensure global financial stability, and the creditor countries because they would avoid financial contagion and the need to bail out their own over-exposed financial institutions. If the major financial institutions of the dominant creditor countries hold very little exposure, by contrast, the risk of systemic contagion towards the core will be lower and official creditors will be less inclined to continue providing bailout loans at all costs.

The second preliminary hypothesis holds that when the provision of further bailout loans to foreign governments encounters insurmountable domestic opposition and becomes

politically unpalatable inside the dominant creditor countries, a split may emerge that sees creditor states withdrawing their consent for further bailouts altogether, leaving the IMF isolated. If the exposure of financial institutions inside the creditor countries is low and opposition to further lending inside the big creditor countries is high, creditor governments and/or the IMF may in fact decide to cancel future credit disbursements, thereby provoking the default that their original bailout program was supposed to prevent. The party most likely to pull the plug on further official lending will tend to be either the nationalist right inside the dominant creditor countries (when public opinion turns against sending taxpayer money abroad) or the IMF itself (when the borrowing government in question consistently fails to abide by its loan conditions). It should be kept in mind, in this respect, that the IMF has a reputation to defend: continuing to lend to an insolvent or a non-compliant government could harm its international standing, risk opposition from its member states and damage its ability to contain future crises. The possibility therefore exists that the IMF will decide to pull the plug on its own program, withholding credit and thus provoking default.

The Privileged Position of Domestic Elites

These two international enforcement mechanism have in turn been complemented by the *internalization* of fiscal discipline within the political and financial apparatuses of the debt state. As we have argued at length in this chapter, the growing dependence of the state on private credit has realigned power relations within debtor countries, strengthening the hand of private creditors at the expense of ordinary citizens. To this we should now add the intermediating role played by domestic elites – regardless of whether they hold any of the government's debt – during a crisis, when the state's dependence on foreign credit becomes

even more acute than under normal conditions. In a context of high state dependence, those capable of attracting credit on better terms will find their position strengthened relative to those who lack the trust of foreign creditors. In practice, this means that internationally mobile, financially integrated and ideologically orthodox elites inside the debtor country will obtain a privileged position in financial policymaking thanks to the "bridging role" they fulfill towards foreign creditors. As Maxfield (1990:93) argued in relation to Mexico, wealthy elites – bankers in particular – will grow more powerful as the state's dependence deepens: "the greater the need for good relations with international creditors, the more weight the creditors and those bankers with close ties to them have in the policy process."

This enforcement mechanism is not dependent on interpersonal ties or connections; it is not the outcome of some international bankers' conspiracy intent on taking over the debtor's state apparatus. Rather, it depends on a structural and normative alignment of the material interests and ideological convictions of domestic elites and foreign creditors, both of whom stand to lose from a unilateral default and both of whom will tend to benefit from and believe in the virtues of fiscal discipline, market liberalization, sound money and debt servicing.[19] As a result of this alignment of interests and ideas, domestic elites are generally willing to commit to an "orthodox policy current," which creditors will then reward with better terms on future loans (Maxfield 1990). This in turn tends to sideline political actors whose loyalties continue to lie with working people and who cannot credibly commit to the orthodox policies required to unlock further credit tranches or regain market access. In practice, this usually means that social democrats will be pulled towards the center while

19 The reason domestic elites stand to lose from default is because they tend to hold a disproportionate share of their own government's debt (Gennaioli, Martin and Rossi 2013:34). Still, the mechanism is operative even when elites do not have exposures – they stand to lose anyway since a default would erode the basis of their own power (their bridging role) and would cripple the financial sector and domestic business.

radicals will either be marginalized or subjected to intense pressure to fall back in line with orthodoxy. What emerges is a powerful and relatively coherent international coalition – an alliance of convenience and conviction, not necessarily the result of direct relations – that systematically insulates itself from popular pressures by undermining possibilities for the institutional expression of social opposition to fiscal austerity and structural reform, for instance through constitutional checks on government spending, legally-binding agreements with official creditors and the sidelining of the legislative at the expense of the executive. Over time, fiscal discipline is gradually internalized into the state apparatus (Streeck 2014).

This indirect form of creditor control over the debtor's political processes will often take on a "technocratic" veneer, with unelected central bankers and financial administrators taking over key government positions to ensure debt repayment and other investor-friendly policies. While such arrangements are usually presented in terms of necessity and expertise, they are really an attempt to depoliticize fiscal policy and naturalize austerity measures by making them appear as economic inevitabilities where in reality they constitute profoundly political interventions aimed at shifting the burden of adjustment onto less privileged and less powerful sectors inside the borrowing country. In keeping with the insights developed in this chapter, however, it should be emphasized that elites are powerful not because they control financial policymaking through their technocratic representatives inside the central banks and finance ministries, but they control policymaking *because they are powerful*. Even with a change in government personnel, the privileged position of domestic elites will continue to constrain the ability of debtors to defy their creditors. In fact, recent research has shown that, the more developed and deeply integrated a country's financial markets are, the more discipline the financial sector will exert over its own government.[20]

20 One such study finds that "the willingness of a government to repay its debts, and thus its ability to

What, then, are the conditions under which the third enforcement mechanism is operative and the conditions under which it breaks down? Since domestic elites derive their privileged position at least in part from their bridging function towards foreign creditors, the mechanism will be conditional on three factors: first, on the government's dependence on foreign credit; second, on the ability of domestic elites to attract that credit; and third, on the ability of elites to fend off popular opposition from below, to prevent a destabilizing legitimation crisis, and to retain ministerial and bureaucratic control over the "commanding heights" of financial policymaking – namely the finance ministry and the central bank.

On the first point, growing dependence on foreign credit will strengthen the hand of domestic elites while lower dependence will weaken it. When the government does not need any foreign credit at all, the bridging function becomes useless and breaks down.

On the second point, the ability of domestic elites to attract credit depends on their capacity to convince foreign creditors of the credibility of their commitment – a factor that is not the result of democratic institutions, as North and Weingast argued, but of the ability and willingness of policymakers to carry out fiscally "responsible" policies and to continue repaying their debts. This ability and willingness will be high when the material interests and ideological convictions of domestic elites are structurally and normatively aligned with those of foreign creditors. The willingness will be low when the material interests and ideological convictions of financial policymakers are *not* aligned, while the ability to commit will be low when the political or institutional capacity to carry out fiscally "responsible" policies is lacking. If domestic elites are unable and/or unwilling to carry out the type of

borrow in the first place, depends on the development of private financial markets. More developed financial markets translate into more severe consequences of public defaults, thereby providing governments with stronger incentives to repay" (Gennaioli, Martin and Rossi 2013:34).

creditor-friendly policies that allow them to attract further loans at decent terms, their bridging role (and hence their privileged position) will crumble and fall apart.

Finally, on the third point, the ability to fend off popular opposition to painful fiscal adjustment and to retain control over the finance ministry and central bank depends on the capacity of domestic elites to contain the legitimation crisis resulting from onerous austerity measures and shield financial policymaking from popular pressures. If the population (Streeck's *Staatsvolk*) withdraws its loyalty from the state and rebels against the establishment, the option of a unilateral suspension of payments may finally be put on the agenda – either as the explicit policy preference of a new pro-default coalition that has just come to power by ousting the old political establishment from office, or as part of an attempt by the existing political establishment to calm social tensions and restore a semblance of political stability in the face of a deep crisis of representation. Still, it should be stressed that, while a successful debtors' revolt or the electoral victory of a pro-default coalition may alter policy preferences, it cannot by itself overcome the state's dependence on credit or the structural power of foreign creditors. For policy preferences to be transformed into actual outcomes requires a degree of autonomy on the part of the debt state. In other words, for the country to unilaterally default on its external obligations, *all three enforcement mechanisms* will need to fail. This means that even if a pro-default or anti-austerity coalition takes power, it may still encounter the external constraints imposed by highly concentrated financial markets and unforgiving official lenders. In short, even a government that has resolved to end austerity or halt payments on its own may eventually be compelled to repay.

CHAPTER III:

Methodology and Research Design

Methodological Approach

This research project builds on a qualitative methodology that combines intensive case studies with cross-country comparison, process tracing and structural power analysis. Such a qualitative approach has some advantages over the quantitative methods normally deployed by economists working on sovereign debt and default. First of all, small-N case study methods tend to be better suited for grasping complex causation in social reality.[21] Rather than establishing mere coincidence of hypothesized causes and outcomes, our main interest is in the exact causal *mechanisms* – mostly invisible from the bird's eye view of

21 Datz (2009:2) writes: "What is clear is that it has been increasingly difficult to treat debt restructuring episodes as homogenous developments amendable to parsimonious and generalizable models. Despite their undeniable importance in creating and analyzing datasets that track correlations among key variables, large-N analyses and formal models cannot condense in agglomerating exercises all the nuances that compose different restructuring scenarios, which, to a large extent, may determine default costs in the short and long-terms." More generally, Hall (2006:26) has observed that, "despite the continuing popularity of regression analysis, recent theoretical developments in social science tend to specify a world whose causal structure is too complex to be tested effectively by conventional statistical methods."

regression analysis – that connect hypothesized causes to real-world outcomes. Secondly, it has been argued that the conceptual validity gained from qualitative approaches tends to feed into more reliable and more innovative results (McKeown 2004; Mahoney 2007). Since parsimonious modeling generally compels economists to prioritize the *operationalization* of variables over the more analytical and qualitative task of *conceptualization*, their results are often plagued by a misspecification of theoretical micro-foundations (hence the qualitative typology of default developed in Chapter I). Finally, questions of power are notoriously difficult to operationalize, especially in large-N studies, leaving most economists to ignore them altogether. And yet, as Chapter II has argued, the study of sovereign debt will have to somehow confront such questions, providing an opening for more qualitative approaches that place the financial structure and the power of creditors at the heart of their analysis.

In important respects, this research therefore seeks to move beyond the deductive-nomological (D-N) approach to social science research, which proposes that qualitative and quantitative methods share the "same logic of inference" and that scholars working in the qualitative tradition should model their approaches on the "more advanced" methodologies of their quantitative colleagues (King, Keohane and Verba 1994). In recent years, social scientists have increasingly come to reject this D-N logic. As Mahoney (2010:122) writes, "it seems safe to say that the field of qualitative methodology has entered a post-KKV era." Instead, this thesis therefore deliberately draws on the advantages of a case study approach, in full awareness that this approach tends to be more apt at hypothesis development than at rigorous hypothesis testing per se. The first part of this chapter will first present an outline of the three methodological approaches on which this research project is based. The second part of the chapter deals with research design, the research question, hypotheses and alternative hypotheses, variables and case study selection.

A Comparative Case Study Method

One of the strong points of the comparative case study method is that it is generally well suited to address "big questions." As Mahoney and Rueschemeyer (2003:7) put it, "big processes and structures were – and still are – most appropriately studied through explicit comparisons that transcend national or regional boundaries [and] could not – and cannot – be analyzed without recognizing the importance of temporal sequences and the unfolding of events over time." Indeed, scholars in the comparative-historical tradition have managed to tackle some of the most substantively important questions in the social sciences in recent decades, including the origins of capitalism, democracy, dictatorship, revolution and labor unions (e.g., Wallerstein 1974; Arrighi 1994; Moore 1966; Skocpol 1979; Collier and Collier 1991). Collier (1993) argued that this "intellectual success ... has played an important role in legitimating a focus on a small N." Research in the tradition also remains diverse. Mahoney and Rueschemeyer (2003:22-23) point out that comparative scholars "do not hesitate to seek guidance from a range of theoretical traditions, including prominently various strands of 'structural' analysis associated with class analytic and conflict theory."

There are good reasons to put the comparative case study method at the heart of this research project. George and Bennett (2005:21), for instance, have stressed that, "compared to the shortcomings of regression-analysis and the D-N model, the advantages of such methods include much higher conceptual validity, the ability to derive new hypotheses from the observations, the exploration of new causal mechanisms, and the modeling of complex causal relations." While early research drawing on case studies methods tended to select their cases largely on the basis of Mill's method of agreement and difference, in which the former serves to eliminate necessary causes while the latter eliminates sufficient causes

(e.g., Mahoney 1999; Skocpol and Somers 1980), recent decades have witnessed a growing recognition of the overly deterministic nature of Mill's logic of causation, in which "a single deviation from a hypothesized pattern of necessary or sufficient causation is enough to eliminate a given explanatory factor" (Mahoney 2007:134). As a result, Mill's logic has been slowly giving way to a more probabilistic view of causality, a less deterministic approach to falsifiability, and greater emphasis on theory development.

Systematic Process Tracing

Partly as a result of the controversy surrounding Mill's highly deterministic view of causality, comparative methodologists now recognize the need for a combination of cross-case and within-case analysis. As George and Bennett (2005:18) put it, there is a "growing consensus that the strongest means of drawing inferences from case studies is the use of a combination of within-case analysis and cross-case comparisons." Some even argue that "within-case comparisons are critical to the viability of small-N analysis" (Collier 1993:17). One such within-case method is systematic process analysis, or process tracing, as it is more commonly known (Hall 2006; Collier 2011; Vennesson 2008). Process tracing has been defined as "the examination of 'diagnostic' pieces of evidence within a case that contribute to supporting or overturning alternative explanatory hypotheses" (Bennett 2004:208). In this method, "the researcher examines histories, archival documents, interview transcripts, and other sources to see whether the causal process a theory hypothesizes or implies in a case is in fact evident in the sequence and values of the intervening variables in that case" (George and Bennett 2005:6-7). As such, process tracing is "an indispensable tool for theory testing and theory development not only because it generates numerous observations

within a case, but because these observations must be linked in particular ways to constitute an explanation of the case" (George and Bennett 2005:207).

That said, process tracing is not without its own problems. As Checkel (2005:3-4) writes, "the method of process tracing is deeply rooted in the tradition of methodological individualism," making it easy for scholars to "lose the bigger picture." Falletti (2006:2) has shown how George and McKeown's (1985) original formulation "attempted to uncover the microfoundations of individual behavior that connect hypothesized causes and outcomes and to reduce the difficulties associated with unobserved contextual variables," without recognizing the relevance of macro-structures (Checkel 2005:1). In his work with Bennett, George seems to have loosened his definition somewhat, "allowing for the identification of causal mechanisms that do not have to be rooted at the individual level" (Falletti 2006:2). Still, Checkel (2005:19) insists that "process tracing forces the researcher to examine, well, questions of process. In making such a methodological choice, it is all too easy to lose sight of broader structural context and the normative implications of one's work." This is where structural power analysis comes in, with its emphasis on the wider context and the systems in which individual actors operate.

Structural Power Analysis

Susan Strange once quipped that comparative scholars often contrast more than they compare. In the Comparative Political Economy literature, this has been especially true of the Varieties of Capitalism literature, which has recently been criticized for its emphasis on the former element of the equation, varieties, at the expense of the latter, capitalism (Bruff 2011; Bruff and Horn 2012). While diverging policy responses to common economic shocks

such as those studied by Gourevitch (1986) are undoubtedly interesting and important, a pattern of similar policy responses in different contexts should equally fascinate the genuine comparativist (Armingeon and Baccaro 2012). As some scholars have therefore pointed out, the objective of comparative analysis should not just be to contrast varying outcomes across cases, but also to "demonstrate that certain relationships among variables hold true in a wide variety of cases" (Peters 1998:26; see also Pontusson 1995:129). The remarkably low incidence of unilateral default is one such outcome that seems to hold true in a wide variety of contemporary cases. As Walzenbach (2000:374) notes, it is precisely in this area of regular outcomes across different contexts "that the overlap between comparative and international political economy is most obvious," and it is precisely here that structural power analysis – with its focus on the bigger picture – comes in as a useful methodological tool.

Still, like process tracing, this big-picture approach is not without problems of its own. Structural power analysis has often been criticized for its deterministic overtones and its failure to account for variation in outcomes. Keohane (2000:x), for instance, writes that Susan Strange "was interested in structures rather than processes, which she regarded as derivative," and points out how as a result she failed to identify the exact channels through which structural power operates in practice. How, and why, does structural power vary? Through what mechanisms does it affect policy outcomes? And how can it be successfully contested? On most of these questions, scholars like Lindblom and Strange remained either ambiguous or silent. For Strange, this shortcoming was at least partly a result of the fact that she never really left behind a methodological framework within which her concepts could be operationalized (Lawton, Rosenau and Verdun 2000). Verdun (2000:78) observes that, "to test rigorously her theoretical analyses would lead [Strange] to having to adopt a methodology that she was unwilling to accept." Instead, she "wanted to provide her insights

into the global political economy, and left it to future generations of scholars to take her ideas further." As a result, Helleiner (2006:84) notes, "even the chief advocate of structural power analysis failed to grasp its full potential." Benjamin Cohen (2000:99) concludes that the task of structural power analysis "would then be twofold: to identify the key conditions that determine, first, when power at either level [instrumental or structural] is or is not likely to be used...; and second, when the use of power is or is not likely to be successful."

Cohen's challenge to identify these conditions cannot be ignored. This thesis hopes to contribute towards the effort of taking structural power analysis forward by emphasizing the need to identify the *precise enforcement mechanisms* through which the structural power of finance compels borrowers to repay, and by specifying the *exact conditions* under which these mechanisms work effectively and the conditions under which they break down, as well as the countervailing mechanisms that allow the structural power of finance to be contested from below.

Research Question and Design

This project is driven by the research question outlined in the introduction: why do countries not default on their external debts more often? Why voluntarily go through great pains to honor foreign obligations? Or, as Eichengreen (2002) puts it, why are governments prepared to impose "extraordinary hardships" on their constituents to avoid default, even if this means giving up part of their national sovereignty and their own chances of re-election in the process? Why not just suspend payments and wait for recovery to take place before renegotiating the remaining debts on more favorable terms, as the majority of European and Latin American countries did in the international debt crisis of the 1930s?

Hypothesis: The Structural Power of Finance

The main hypothesis developed and tested in this study is that the structural power of finance systematically constrains the willingness and ability of governments to default on their external debts. This structural power is in turn hypothesized to operate through three enforcement mechanisms, each of which revolves around the capacity of private and official lenders to withhold much-needed credit; credit upon which the borrowing state depends for its own reproduction and without which it would run into acute financial trouble.

The three hypothesized enforcement mechanisms are the following:

1. The **market discipline** imposed by an **international creditors' cartel**, which can immediately withhold short-term credit in the event of non-compliance;
2. The **policy conditionality** imposed by an **international lender of last resort**, which provides emergency loans in return for structural adjustment, and which can immediately withhold short-term credit in the event of non-compliance;
3. The **privileged position** of **domestic elites**, who are strengthened because of their bridging role towards foreign lenders and their capacity to attract short-term credit, and who can similarly withhold short-term credit in the event of non-compliance.

A unilateral default by the debtor country would immediately result in the lenders' refusal to disburse further credit both to the defaulting government and to its private sector, precipitating debilitating and largely unpredictable spillover costs that would quickly ripple through the financial sector and the domestic economy, undermining the state's capacity to carry out its core functions of accumulation and legitimization. Since these costs tend to be short-lived, those negatively affected by austerity may favor a unilateral default; however, since the spillover costs of default tend to disproportionately harm the interests of domestic elites, the latter are likely to wield their privileged position in policymaking – derived from their bridging role towards foreign creditors – to prevent such a default from taking place.

The operability and effectiveness of the three enforcement mechanisms is therefore conditional upon a number of factors, each of which relates to the debtor state's capacity to reproduce itself in the absence of further short-term credit from private and official lenders:

1. **Market discipline** depends on:
    a) **The ability of private lenders to hold together a creditors' cartel:** the cartel tends to be at its strongest when the debt is highly concentrated and creditor interests are structurally interlocked.
    b) **The debtor's dependence on the creditors' cartel:** this dependence tends to be at its greatest when the debtor does not have an "outside option" for external financing and when its financial and commercial self-sufficiency is low (i.e., when the domestic economy relies on foreign credit).
2. **Policy conditionality** depends on:
    a) **The ability of official creditors to present a unified front:** this front tend to be most unified when the risk of contagion is high and the creditors' internal opposition to bailouts is low.
    b) **The debtor's dependence on the lender of last resort:** this dependence tends to be at its greatest when the debtor does not have an "outside option" for external financing and when its financial and commercial self-sufficiency is low (as above in point 1b).
3. **Privileged position** depends on:
    a) **The capacity of domestic elites to attract foreign credit:** this capacity tends to be high when elites' material interests and ideological convictions are aligned with those of the creditors, and when the institutional capacity to carry out fiscally "responsible" policies is in place.
    b) **The ability of elites to retain control over financial policymaking:** this tends to be high when the legitimation crisis can be contained and financial policy is shielded from popular pressures.

The conditions under which the enforcement mechanisms break down:

1. **Market discipline** tends to break down when:
    a) **Private lenders fail to hold together a creditors' cartel:** the cartel will be difficult to maintain when the debt is highly dispersed and the lending structure incentivizes free-riding;

    Or when:

    b) **The debtor no longer depends on the creditors' cartel:** the debtor has an "outside option" for external financing or it is very self-sufficient in financial and commercial terms.

2. **Policy conditionality** breaks down when:

    a) **Official creditors "pull the plug" on further financing:** this will only happen when the risk of contagion is low and domestic opposition to further bailouts in the creditor countries is high.

    Or when:

    b) **The debtor no longer depends on the lender of last resort:** the debtor has an "outside option" for external financing or it is very self-sufficient in financial and commercial terms.

3. **Privileged position** breaks down when:

    a) **Domestic elites are no longer capable of attracting foreign credit:** this happens when creditors lose trust in the debtor country's elites and cut them loose, especially if there is an ideological misalignment and/or a failure to satisfy bailout conditions (as a result of point 2a).

    Or when:

    b) **Elites lose control of financial policymaking:** this happens when the state loses the loyalty of its citizens as they rebel against austerity and replace the ruling elite with a pro-default coalition. Alternatively, a deep legitimation crisis may force elites to make far-reaching concessions.

The central hypothesis of this research is that a country is only likely to unilaterally default on its external debts when *all three enforcement mechanisms have broken down* as a result of a combination of the conditions and countervailing mechanisms spelled out above.

Alternative Hypotheses: Reputation, Sanctions, and Democratic Advantage

The alternative hypotheses that this project will have to contend with are the traditional explanations of debt compliance proposed in the economics literature and outlined in Chapter I: (1) a government's concerns about its reputation as a borrower and its long-term market access; (2) its fears over legal or trade sanctions; and (3) the credible commitment generated by democratic (i.e., parliamentary, judiciary) constraints on the executive branch. The most recent explanation, revolving around (4) spillover costs through the channel of the debtor's financial system, is incorporated into the structural power hypothesis.

Dependent and Independent Variables

The dependent variable is the *policy response* of a distressed sovereign borrower to an international debt crisis. This response can take the form of (1) full and timely repayment; (2) a negotiated debt rescheduling; (3) a negotiated debt restructuring; (4) a suspension of payments (moratorium); and (5) a rejection of liability (repudiation). Outcomes 1-3 can all be considered variations of debtor compliance as none of them involves unilateral action by the debtor. Outcomes 4-5, by contrast, do constitute unilateral action by the debtor. To ease the analysis, the outcome will therefore be considered a binary variable that can take the value of a unilateral default or the absence of a unilateral default. The interest of this study, broadly speaking, is in the relative *absence of default* and the *prevalence of compliance.*

The hypothesized causal factor is the structural power of finance, defined as the capacity of private and official creditors to withhold credit upon which indebted states and their administrators depend for their own reproduction. This structural power is exercised through three enforcement mechanisms (the market discipline of the creditors' cartel, the policy conditionality of the lender of last resort, and the privileged position of domestic elites) that are in turn dependent on the variable conditions and countervailing mechanisms spelled out in the previous section and discussed in greater detail in Chapters I and II.

Falsifiability: Warding Off Confirmation Bias

The scholarly purposes of this research project can be defined as "theory-oriented explanation" (Hall 2006). The principal goal is to contribute towards theory development in the study of sovereign debt and the structural power of finance; two fields of inquiry that few scholars have so far tried to explicitly connect to one another. Beyond this, the most

immediate objective of the three case studies under investigation is to test one hypothesis (the structural power hypothesis, which incorporates and expands upon the spillover costs hypothesis) and compare its validity against a set of alternative hypotheses (the reputation hypothesis, the sanctions hypothesis and the democratic advantage hypothesis), with a particular emphasis on the specification of the enforcement mechanisms and the elucidation of the exact conditions under which these are operative. With these objectives in mind, the strict requirements of Popperian falsification will need to be loosened a little in favor of a more probabilistic view of causation and research methods oriented towards structured, focused comparison and theory development rather than hypothesis elimination *per se*.

Still, hypothesis testing remains an important part of this research project, and there are a number of ways in which researchers seeking to test hypotheses in a small-N research design can impose some discipline on themselves in order to avoid the risk of confirmation bias. First of all, scholars can contribute to future testing of their own findings by "deriving predictions that are as 'brittle' as possible, against observations and other theories" (Hall 2006:27). The most central prediction of this thesis is that unilateral default will only take place when *all three enforcement mechanisms* have broken down; in other words, when the creditor cartel has disintegrated and private lenders can no longer enforce market discipline on the debtor; when the lender of last resort is no longer able to impose conditionality; and when domestic elites inside the debtor country lose control and can no longer fulfill their bridging role towards foreign creditors. Given the exact conditions listed in the previous section, these are all testable propositions.

The other way in which scholars can ward off confirmation bias is by comparing the outcomes and developments within the case studies to predictions derived from alternative

explanations. In doing so, special attention should be paid to elucidating the causal mechanisms (or their absence) that connect the hypothesized causal variable to the observed outcome. As Mahoney (2007:132) puts it, “when clear mechanisms linking a presumed explanatory variable and outcome variable are identified, one's confidence that the relationship really is causal is increased; if such mechanisms cannot be identified, one's confidence about causality is challenged.” This means that the researcher must continuously engage with the empirical evidence in favor of the proposed hypothesis and the alternative interpretations to which this evidence might lend itself. This thesis aims to do so by starting each chapter with a discussion of the three alternative hypotheses, deriving a set of predictions from each of them and testing whether the observed causal mechanisms in the case are in agreement with what each explanation would lead us to expect. To ease this process, it will be useful to briefly visualize the precise “causal chains” that each hypothesis would lead us to observe in the cases. The following flowcharts provide a rough and very schematic overview of the causal mechanisms through which the hypothesized variables would produce the expected outcomes. Each “balloon” constitutes a moment in the causal chain and a “diagnostic” piece of evidence that we should be able to test against the observed data.

Figure 3.1 – reputation hypothesis:

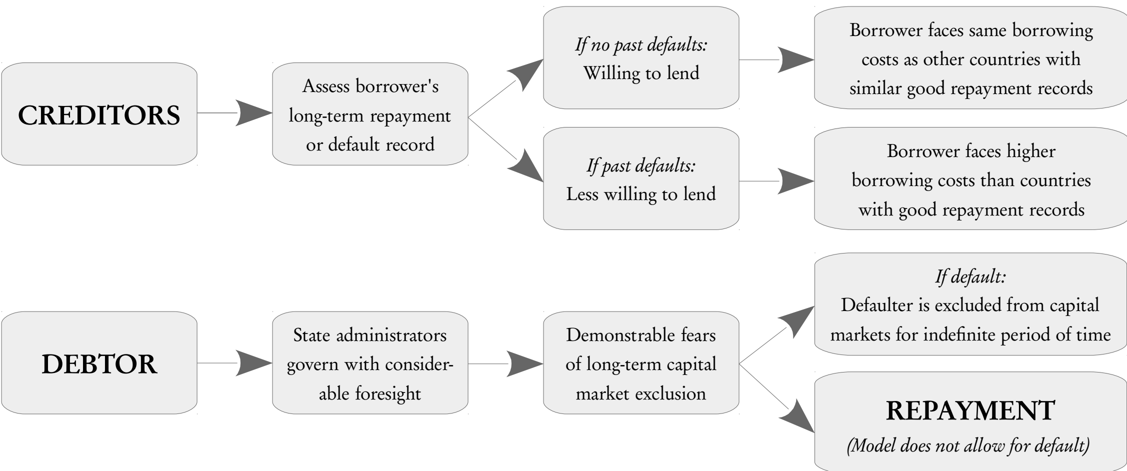


Figure 3.2a – trade sanctions hypothesis:

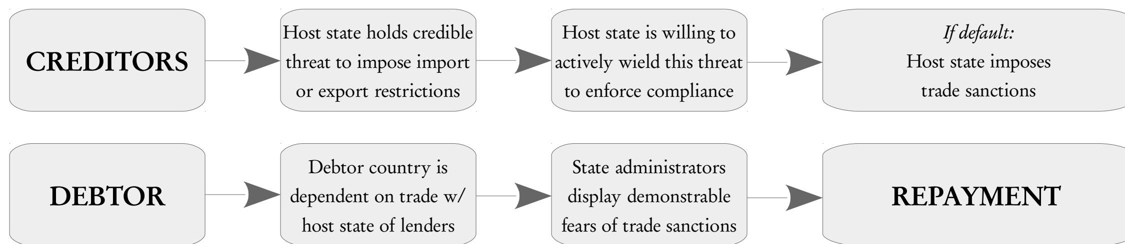


Figure 3.2b – legal sanctions hypothesis:

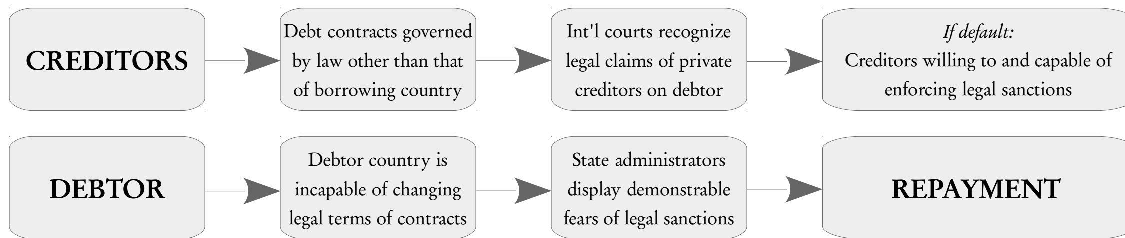


Figure 3.3 – democratic advantage hypothesis:

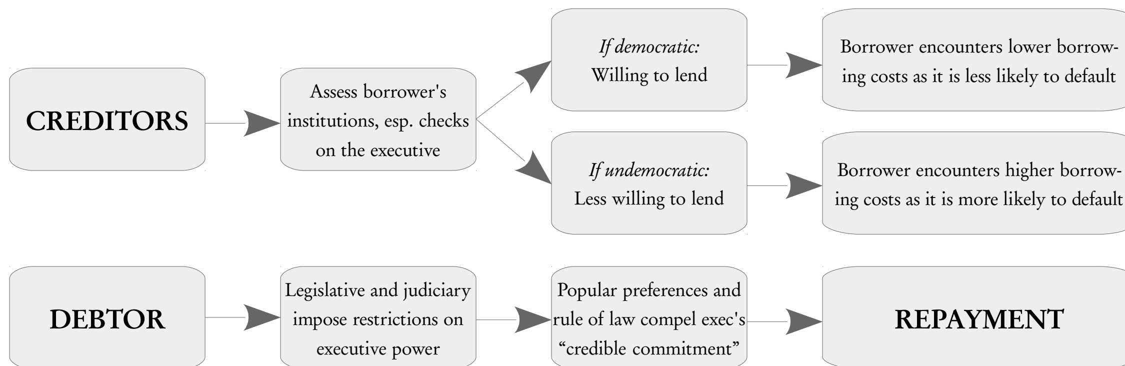


Figure 3.4 – spillover costs hypothesis:

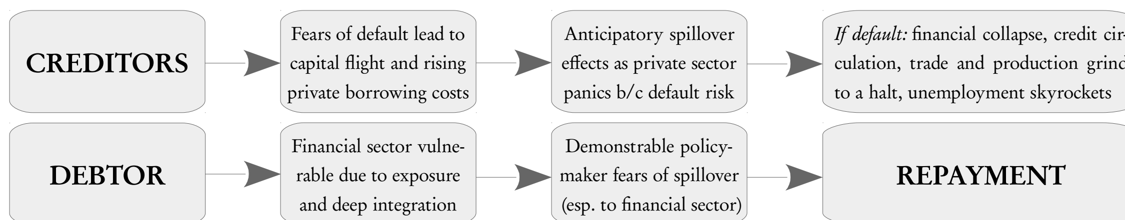


Figure 3.5a – structural power hypothesis:

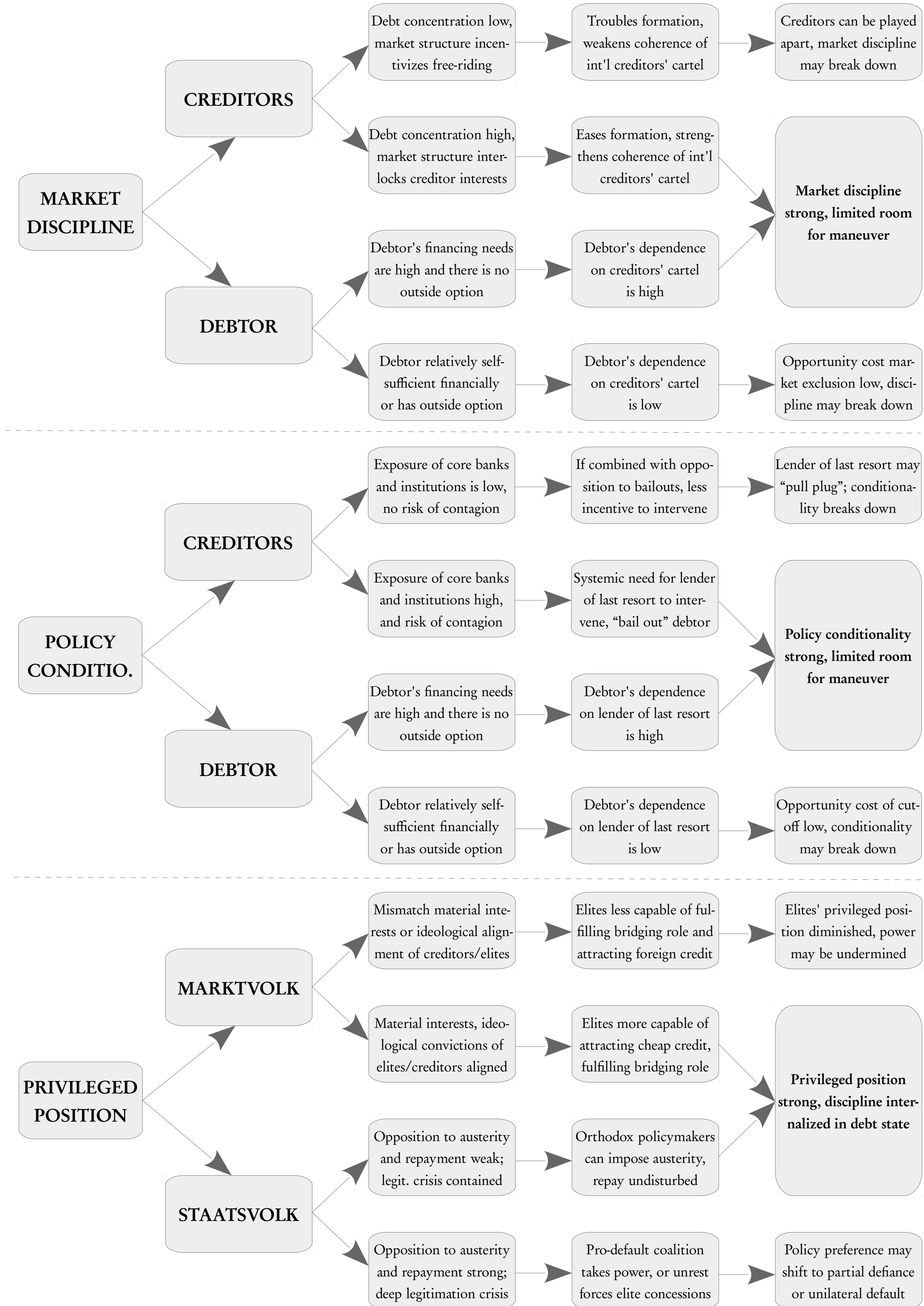
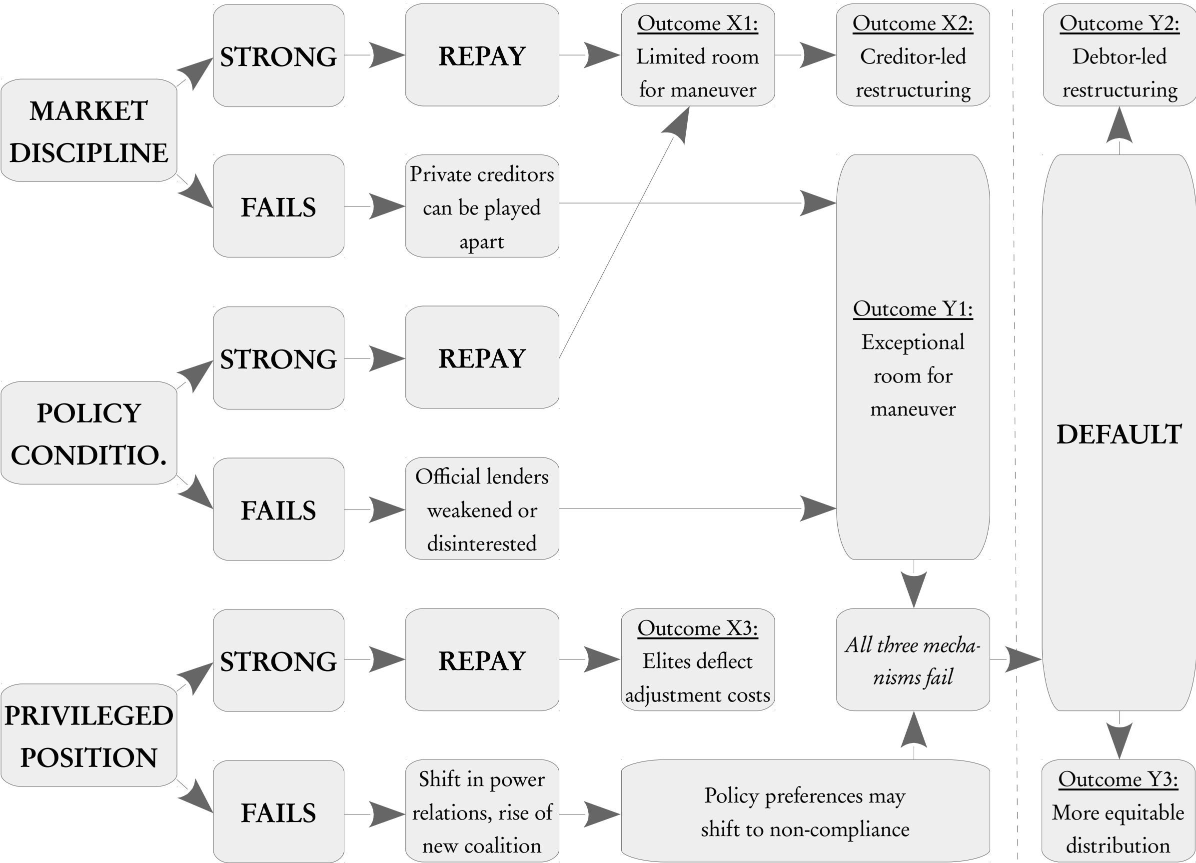


Figure 3.5b – structural power hypothesis (continued to outcomes):



In the structural power hypothesis, as mentioned before, default will only become an option when all three enforcement mechanisms break down. When the mechanisms do not break down, and the structural power of creditors compels the debtor to repay, we will – in addition to the borrower's compliance and its diminished room for maneuver – expect at least two further outcomes: first, we would expect crisis resolution (through an orderly debt restructuring) to be delayed until long after the big banks and financial institutions of the core countries have reduced their exposure, and for any debt negotiations to be undertaken at the initiative of the international lenders with creditor interests firmly in mind; and second, since the structural power of creditors and wealthy elites allows these privileged groups to deflect the costs of adjustment onto others, we would expect the popular sector – working people, the middle class and the poor – in the debtor countries to bear most of the

burden, with foreign creditors and domestic elites emerging as winners. In the opposite case in which the enforcement mechanisms all break down, we would expect – in addition to the possibility of a unilateral default – a shift in the power relation between the debtor and its creditors and between citizens (the *Staatsvolk*) and investors (*Marktvolk*), with the debtor country pursuing a more aggressive negotiated restructuring or even a partial debt repudiation, and with the burden of adjustment shared more equitably between the debtor and its creditors, as well as between social groups in the debtor country.

Case Studies and Case Selection

This study revolves around an investigation of three substantively important and theoretically relevant case studies: Mexico (1982-'89), Argentina (1999-'05) and Greece (2009-'15). Before specifying this choice of cases, there is a need to address the methodological issue of selection bias. In the D-N approach, there is a view – derived from the laws of regression analysis – that one should refrain from selecting along the dependent variable, as such non-random sampling strategies may result in bias or "systematic error" (e.g. Héritier 2008; King, Keohane and Verba 1994). However, as some leading qualitative methodologists have pointed out, "the specific statistical problem of bias resulting from selection on the dependent variable has been inappropriately applied to many comparative historical studies" (Mahoney and Rueschemeyer 2003:14; Collier and Mahoney 1996; Ragin 2008). For Mahoney (2007:129), "many concerns about selection bias in qualitative research are a fundamental misapplication of ideas from regression analysis to qualitative research."

In fact, for small-N studies it is much wiser to deliberately select on the dependent variable. Seawright and Gerring (2008:295), for instance, have noted that "serious problems

are likely to develop if one chooses a very small sample in a completely random fashion." Collier and Mahoney (1996:21) have similarly stressed that "in small-N studies, random sampling may produce more problems than it solves." Instead, they propose theoretically-informed non-random sampling as "an alternative approach ... that deliberately produces a sample in which the variance on the dependent variable is similar to its variance in the larger set of cases" *(ibid.*; see also Mahoney 2003:351; Braumoeller and Goertz 2000). In the end, case selection in comparative studies has the same "twin objective" as random sampling in quantitative analysis, namely that of obtaining a representative sample and a sufficient degree of variation in the variables of theoretical interest (Seawright and Gerring 2008:296). The selection of cases on the basis of their outcome – the absence of default in Mexico, the presence of default in Argentina, and Greece as a case that has been teetering between the two for the past five years – is therefore wholly justified.

The Lost Decade: Mexico (1982-'89)

The first case – the Mexican debt crisis of the 1980s – was chosen for two reasons. First, as the first major sovereign debt crisis of the neoliberal era, the Mexican case occurred in a transition phase for the global political economy that is likely to be reflected in the case itself. If the three hypothesized enforcement mechanisms of debtor compliance really exist, the Mexican case should provide us with a unique insight into how they formed, how they contrasted to previous crises – most importantly that of the 1930s – and how they actually affected policy outcomes. Second, in terms of its overall outcome, which was marked by the notable absence of default, the Mexico case represents somewhat of a baseline of compliance against which the two other cases can subsequently be compared. These case compari-

sons will be particularly interesting as Mexico was considered the “model debtor” of the 1980s for its cooperative attitude vis-à-vis foreign creditors, meaning we should expect to find similar policy responses – albeit in different political contexts – in subsequent sovereign debt crises in Latin America and elsewhere. In terms of its outcome, the Mexican debt crisis serves as a *typical case* representing the essential characteristics of neoliberal crisis management under conditions of financialization (Gerring 2007).

The Great Default? Argentina (1999-'05)

Argentina's well-known sovereign default of 2001 and the broader financial crisis (1999-'05) in which it occurred poses a dramatic contrast to the outcome of the Mexican debt crisis. Where Mexico in the 1980s was a model of debtor compliance, Argentina post-2001 is probably the clearest contemporary example of debtor defiance. At the height of its crisis, facing a devastating economic, social and political meltdown, Argentina declared the single biggest sovereign default (amounting to $100 billion) in world history. Argentina's default therefore poses an important puzzle: if the structural power of creditors is claimed to be so important in prevent unilateral default, then how was Argentina able to defy its foreign creditors in such dramatic fashion? Argentina, in this sense, can be seen as a *deviant case*, fundamentally challenging the structural power hypothesis stipulated in this research (Cooper and Momani 2005:309). And yet, as the case will demonstrate, this conclusion may be a bit too premature: Argentina *before* its default was even more compliant than Mexico in the 1980s, refusing to accept the inevitability of default even as the international financial community actively pushed it to embrace this outcome. Also, as we will see, Argentina's defiant rhetoric post-default may have been targeted at the “vultures” of Wall Street, but the

bondholders who suffered the biggest hit in the Argentine default were ordinary pensioners in Italy and other European countries; Wall Street actually made windfall profits from the default. Argentina is therefore better defined as a specific subtype of the deviant case – a so-called *influential case* – which at first glance appears to call into question or even invalidate a theory's predictions, but which upon closer inspection actually ends up confirming that theory: "the influential case is the 'case that proves the rule'" (Gerring 2007:108).

The Specter of Solon: Greece (2010-'15)

Greece, finally, can be seen as the most substantively important case study under investigation given contemporary concerns. In terms of its (preliminary) outcome at the time of writing, in late 2015, Greece is a remarkable case of debtor compliance. For five years, the country's policy response was marked by an unwavering commitment to continued debt servicing and an absolute refusal to take unilateral action – even if the policy conditions of its bailout loans were not always met, and even if a leftist government briefly (and unsuccessfully) challenges its creditors in the first half of 2015. The "socialization" of Greece's debt between 2010 and 2012 meant that taxpayers in the creditor countries, rather than Greece's original private lenders, will be forced to pick up the bill of any future default or restructuring. Greece is interesting for the purposes of this study because it combines a number of salient elements of the Argentine case (notably its dependence on bond finance and the strong popular opposition to debt repayment and austerity from below) without reproducing the Argentine outcome of a default. As such, it presents an important puzzle: why did Greece, which at a superficial level appears to resemble Argentina, not suspend its payments? Why was the outcome so much closer to the Mexican debt crisis?

CHAPTER IV:

The Lost Decade

Mexico (1982-'90)

Introduction

The Latin American debt crisis of the 1980s was the first major international debt crisis since the Great Depression of the 1930s. While the episode displayed a remarkable degree of similarity to its predecessor in terms of its underlying economic dynamics, the policy response could not have been more different (Marichal 1989). In the 1930s, virtually all Latin American debtors – except Argentina – unilaterally suspended payments on their foreign obligations and, after insisting on a lengthy moratorium, forced highly coercive debt restructurings onto foreign bondholders. Although the defaults of the 1930s may have been costly in the short term, the economic recovery was relatively rapid and the burden of adjustment borne mostly by foreign lenders (Bertola and Ocampo 2012:13). In this respect, the response to the Great Depression mirrored the established pattern of pre-war crisis management, in which the imposition of unilateral moratoriums by crisis-ridden peripheral borrowers was considered "normal and part of the rules of the game" (Ocampo 2013).

The crisis of the 1980s, by contrast, was marked by a striking absence of unilateral default.[22] Instead, the international financial community engaged in a concerted effort to reschedule the amortization of principal, refinance maturing debts and prevent a unilateral suspension of interest. The result of this debt strategy was a protracted economic downturn with extreme social costs. Poverty rates on the continent climbed sharply and hit nearly 50 percent by the end of the decade (Bertola and Ocampo 2012:18). In 1989, Mexico's GNP was still 11 percent lower than it had been at the start of the crisis, while some 15 million Mexicans had been born in the intervening period. As millions saw their jobs vanish, the 1980s became known as *la década perdida*: the lost decade. By the 1990s, a new norm of crisis management thus seemed to be firmly entrenched: all debts must be repaid, regardless of the social, political and economic costs for the borrowing country (Oliveri 1992:2). US Treasury Secretary Donald Regan summarized the rules of the game thus: "I don't think we should let a country off the hook just because they are having difficulty. As debtors, I think they should be made to pay as much as they can bear without breaking them. You just can't let your heart rule your head in these situations" (cited in Quirk 1983:10).

This chapter is driven by a simple research question: what explains the remarkable and unprecedented degree of compliance with this new norm in the 1980s?[23] Building on a case study of Mexico, which remained at the heart of the debt storm and at the forefront of the financial firefighting for most of the decade, it aims to show that the conventional explanations outlined in Chapter I (that the relative absence of default is the result of either long-

22 "The option of unilateral action (leading to default or extended moratoria) has not been officially adopted by any major debtor since 1982" (Griffith-Jones 1988:7-8).

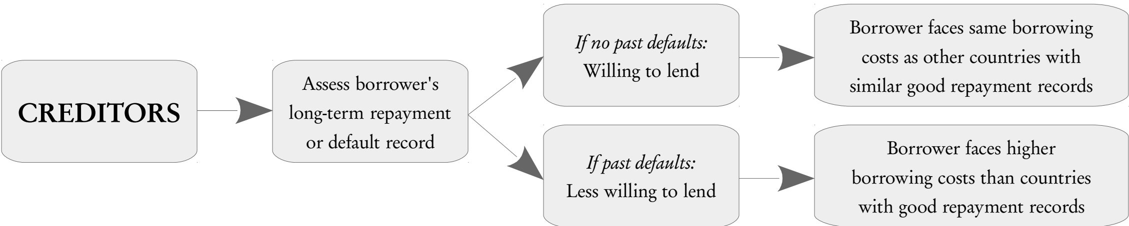
23 "The key questions become: why have the governments of the big Latin American debtors been so reluctant to build up a debt strategy based on default? And why have the governments of the smaller nations been so slow to create an effective debtors' cartel that would give them the collective leverage to default?" (Branford and Kucinski 1988:133).

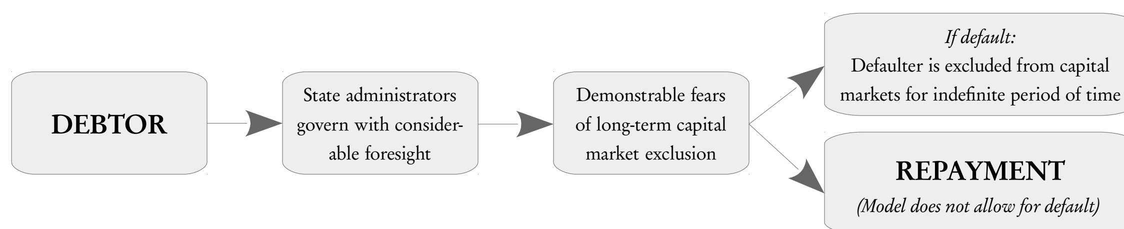
term reputational concerns, a fear of legal or trade sanctions, or a democratic commitment to creditor rights) appears to be rather thin; in many respects the evidence contradicts them all. Instead, a closer look at the Mexican debt crisis reveals a disconcerting picture about the growing power of an international creditors' cartel; the steady evolution of the IMF into a full-fledged fiscal disciplinarian and "global capitalist planner"; and the complex ways in which Mexico's dependence on foreign credit strengthened the hands of a bankers' alliance whose loyalties clearly lay with domestic elites and foreign creditors. In this sense, the year 1982 marked a watershed in the evolution of the global political economy not only because it revealed for the first time how successful the creditors had become in averting default and avoiding losses, but especially because it helped to cement the enforcement mechanisms of debtor compliance that continue to undergird the structural power of finance today.

The chapter is divided into three parts. The first weighs the evidence in favor of the conventional explanations of debtor compliance. The second explores the hypothesized enforcement mechanisms that are at the heart of the theoretical argument of this thesis. The third aims to connect these enforcement mechanisms to the outcomes of the crisis. The conclusion briefly considers possible alternative interpretations for the evidence presented.

Reputation Hypothesis

Figure 4.1 – reputational mechanism:





A central premise of the reputation hypothesis is that reliable debtors with a history of repayment are able to borrow on better terms than unreliable debtors with a history of default. In its original formulation by Eaton and Gersovitz (1981), the theory assumes that defaulters are permanently excluded from international capital markets. While this clearly did not materialize in the case of the Latin American defaulters of the 1930s, a slightly less restrictive formulation of the hypothesis would still lead us to expect a significant difference in risk premiums between past defaulters and non-defaulters (Tomz 2007). As we already saw in Chapter II, however, the empirical data and academic consensus are unambiguous on this point: Argentina, which did not default during the 1930s, borrowed on similar terms in the 1970s as its defaulting neighbors did (Jorgensen and Sachs 1989). As in the 1920s, Latin America shared equally in the 1970s lending boom, irrespective of past repayment records (Eichengreen and Portes 1988a; 1988b; Lindert and Morton 1989). With a vast surplus of petrodollars flowing through the global financial system and international investors hungry for lucrative investment opportunities, the lenders were eager to forget the continent's pre-war history. What mattered was the immediate prospect of easy profits.[24]

This myopic investor attitude was perhaps most clearly expressed in the statement by Citibank CEO Walter Wriston, just before the crisis broke out, that investors need not fear default since “countries do not go bankrupt.” Mexico's Director of Public Credit and

24 Even Cuba was able to accumulate a debt of $3.2 billion to non-US banks and Western governments. As Kaletsky (1985:88) notes, “Cuba's ability to borrow as much per head as Indonesia or Thailand, in a period of twenty years after a major debt repudiation and foreign asset confiscation, provides an eloquent example of the lack of solidarity among creditor nations and private banks in response to defaults.”

current OECD Secretary General Angel Gurría recounts that "the banks were hot to get in ... They showed no foresight. They didn't do any credit analysis. It was wild ... We just issued promissory notes. We were selling them like hotcakes" (cited in Kraft 1984:19/35).[25] For foreign creditors, "the prospect of default seemed too extraordinary to consciously consider" (Oliveri 1992:16). Mexico's wealthy elite were similarly unfazed: "Rather than alarming the local bourgeoisie," Branford and Kucinski (1988:48) noted, "the mushrooming foreign debt reassured them, cementing their alliance with international capital."

A further observation that the reputation hypothesis would lead us to expect is a demonstrable concern among policymakers that their country might lose long-term market access in the event of a default – which would in turn require evidence of policymakers working with considerable foresight and a visible appreciation of the consequences of their actions stretching far into the future and even beyond their own political mandates. This investigation did not uncover any evidence of such long-term considerations or political foresight. Instead, in the heady days of June and July 1982, when Mexico was closest to default, short-term concerns about the government's liquidity seemed to predominate over abstract considerations about long-term market access. With the future heavily discounted against the urgent need to obtain sufficient foreign exchange to keep servicing obligations falling due the next day, Mexico's fiscal policy effectively became a race against the clock. As Finance Minister Jesús Silva Herzog recounts, in mid-1982 Mexican government officials were confronted with a "dramatic and recurrent reality" in which crucial decisions on how to obtain and spend critical resources were made on a day-to-day basis: "Tomorrow we have to pay $40 million to cover maturities due to banks X and Y; and we have only half of that

25 In 1980, an international banker told *Institutional Investor* that "maybe no one's making a fortune here any longer, but you've got to be in Mexico. This is where the action is" (cited in Aggarwal 1996:158).

amount. We need to borrow $20 million at twenty-four or forty-eight-hour terms from bank Z to cover our financial obligations. We will see, afterwards, how we solve the problem for the day after tomorrow" (Silva Herzog 1991:55).

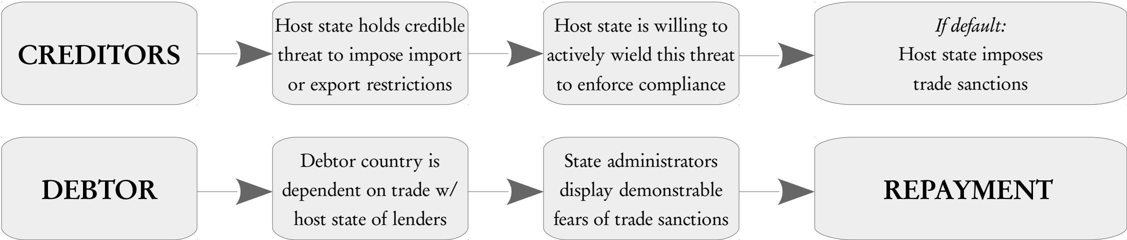
This short-termism was not just a product of the lack of foresight among Mexico's highly sophisticated financial policymakers; instead, it appears to have been at least in part the product of the structure of international lending and the country's debt profile itself. Following the Volcker shock a few years prior, Mexican banks, businesses and households – fearing an impending devaluation – had begun to move vast sums of money out of the country, greatly depressing the central bank's foreign exchange reserves. By the end of July 1982, the Bank of Mexico was losing up to $200-$300 million in foreign currency reserves a day. Silva Herzog remarks that "what entered the country one day went out the following day." Between 1973 and 1982, Mexico's total assets abroad increased by $26 billion, as a result of which the Bank of Mexico had to borrow ever greater sums to be able to replenish its foreign exchange reserves (Gurría 1995b:191). In 1981 alone, the public debt soared from $55 to $80 billion. Investors, increasingly concerned about the sustainability of Mexico's towering debt load, refused to extend further multi-year credit. As a result, interest rates shot up and maturities on new debt shortened dramatically. At the start of the year, only 5 percent of Mexico's debt had been due within a year; by the end of 1981 that amount had risen to 22 percent. As bankers became increasingly wary of lending long-term, almost all the new money came in the form of six-month loans or less (Kraft 1984:35).

Far from being able to worry about the long-term consequences of their actions, Mexican policymakers thus found themselves compelled by market forces to keep running just to stay in the same place, doubling down on their bets simply to pay off their old debts.

At the same time, both in Mexico and abroad, the crisis was deliberately being construed – by economists and policymakers alike – as a problem of *illiquidity* as opposed to a problem of insolvency (e.g. Cline 1983). This dominant interpretation lent itself very conveniently to an official policy response emphasizing short-term adjustment, a temporary rescheduling of maturities, and the disbursement of international emergency loans to bridge the fiscal gap; in other words, precisely the type of short-term solutions favored by profit-maximizing foreign investors and domestic elites. As Silva Herzog (1991:54) himself later confirmed, "it was never considered, by any of the participants, that the problem was of a different character, with structural or more long-term elements."

Sanctions Hypothesis

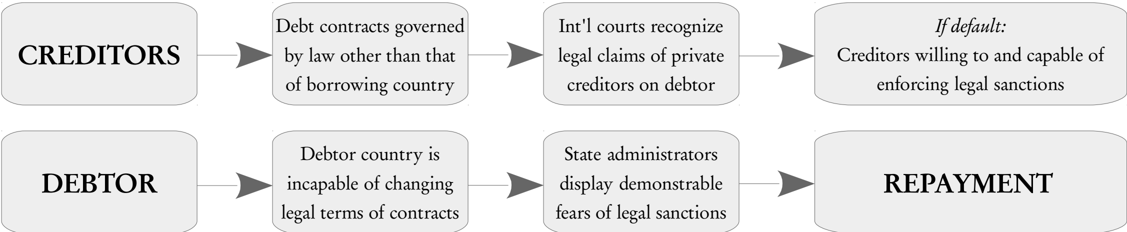
Figure 4.2a – trade mechanism:



Reputation concerns therefore do not appear to have offered a credible regime in the Mexican case or in the Latin American debt crisis more generally. If policymakers were instead driven by a fear of creditor sanctions, as Bulow and Rogoff (1989) have argued, we should expect either explicit threats of such direct legal or trade action, or – if we accept that such threats may be implicit rather than explicit – we should at least be able to see such sanctions carried out against those debtors that took a more confrontational stance, flirting with default like Argentina and Peru did. Again, this investigation has found no evidence

for either proposition. There was certainly never any explicit threat of US trade sanctions against Mexico; in fact, the nature of the relationship between the two remained extremely cooperative throughout the crisis and it was clear to all actors involved that the US government only stood to harm its own economy by imposing import and export restrictions on one of its most important international trading partners. Mexican policymakers themselves did not display any demonstrable fears that the US would impose trade sanctions, and the US never pursued or threatened to pursue trade sanctions against Argentina or Peru.

Figure 4.2b – legal mechanism:

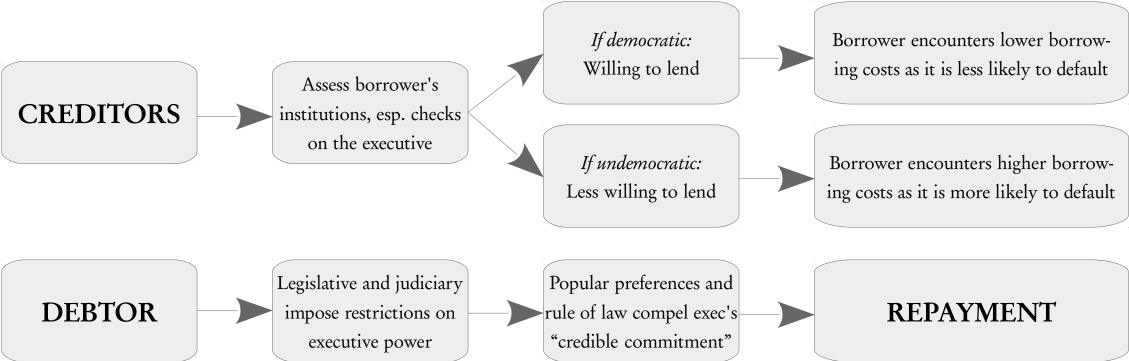


Similarly, legal sanctions by private creditors were unlikely to compel countries to repay since any creditor victory in court would still be impossible to enforce in practice. As an influential *Financial Times* commentator noted, "bankers' hopes – and borrowers' fears – that crippling costs could be imposed on recalcitrant debtor countries through court action appear to be greatly exaggerated" (Kaletsky 1985:21). Of course it is impossible to confirm what would have transpired in the counterfactual case of a unilateral Mexican default, but it is clear that the countries that did temporarily pursue unilateral action did not really face legal reprisals from their creditors afterwards. By 1988, for instance, a leading scholar of the Latin American debt crisis observed that "the Peruvian experience has shown that after two years of unilateral action no legal response has come from the creditor banks to confiscate assets or other drastic measures; the only cost of the unilateral action, as regards creditor banks, has been their curtailment of short-term credit lines" (Griffith-Jones 1988:360). The

same absence of legal sanctions can be observed in Argentina, in spite of the country's brief period of non-compliance under its new democratically-elected president in 1984.

Democratic Advantage Hypothesis

Figure 4.3 – institutional mechanism:



If reputation and sanctions did not provide an effective regime of debt repayment, as North and Weingast (1989) were already arguing by the end of the decade, then what about the supposed virtues of liberal democracy? The democratic advantage hypothesis would lead us to expect two things. First, we should observe mechanisms whereby the classical institutions of liberal democracy – strong parliaments, powerful central banks, independent courts – systematically constrain the options of the executive and compel it, through voter preferences and the rule of law, to credibly commit to its financial obligations (Schultz and Weingast 2003). Second, and as a result of the former, we should expect to find greater compliance by democratic countries and an increased likelihood of contract abrogation by non-democratic regimes. Instead, we find the opposite to be the case on both counts. As it turns out, there is a broad consensus that Mexico's authoritarian one-party regime, dominated by the *Partido Revolucionario Institucional* (PRI) and famously referred to by Vargas Llosa as

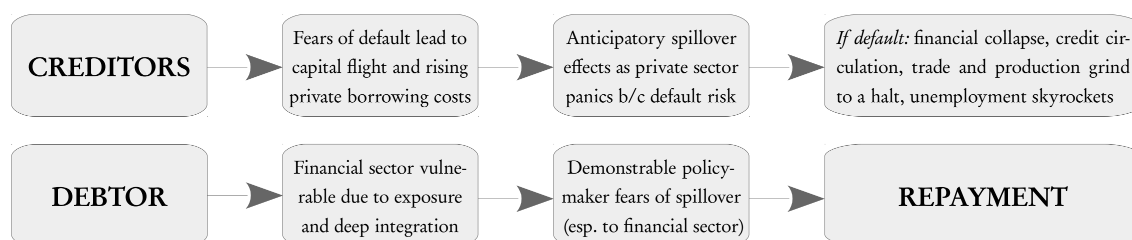
"the perfect dictatorship," offered "the richest example of cooperation from a Latin American borrower" (Oliveri 1992:163/5). The country had a powerful executive and virtually no democratic checks and balances, yet it was precisely these non-democratic institutions that endowed it with the capacity to systematically shield fiscal policy from popular opposition to repayment (Bailey and Cohen 1987). Moreover, through a dual strategy of repression and co-optation, the governments of Miguel de la Madrid and Carlos Salinas actively prevented the emergence of an organized anti-austerity coalition (Middlebrook 1989). As a result, pro-default voices were effectively excluded from the public debate and from policymaking, and the PRI remained immune from electoral pressures over the national debt.

Meanwhile Argentina, following its democratic transition in 1982-'83, did exactly the opposite of what North and Weingast's credible commitment theory would lead us to expect. After the fall of the military *junta*, the country briefly took a considerably more confrontational stance *vis-à-vis* foreign creditors. Upon assuming office in December 1983, President Alfolsín immediately declared a six-month moratorium on interest payments and began to openly call for the formation of a Latin American debtors' cartel to pressure foreign creditors into offering better terms (Roddick 1988:49). Lamenting that "the debt of Argentina and of other Latin American nations is the product of perverse mechanisms that lend us money in order that we do not develop ourselves," Alfolsín declared that "we are not going to pay our debt by making our people hungry" (cited in Berg 1984:4). For the newly elected president, democratic responsibility meant that "the state cannot bow to international financial groups or privileged local groups." Scholars recognized Argentina as "the single most resistant debtor in international finance" (Oliveri 1989:163). In a direct rebuttal of North and Weingast's democratic advantage hypothesis, Kaufman (1985:474) has noted that "the newly democratic government of Argentina ... was by far the most defiant,

[while] Mexico's party-based authoritarian regime has been most compliant." For their part, the creditors did not appear to be very enthusiastic about Latin America's recent wave of democratization either. After meeting with Argentina's new, democratically accountable negotiators, one senior US banker complained that "we expected to get facts and figures, a detailed picture of the country's medium- to long-term economic plans. All we got were some platitudes about Argentina's new democracy" (cited in Tussie 1988:293).

Spillover Costs Hypothesis

Figure 4.4 – spillover mechanism:



If the conventional explanations of debtor compliance do not seem to hold much water, then what about the more recently proposed spillover costs hypothesis? This theory would lead us to expect demonstrable concerns among policymakers over the consequences of default on the wider economy. There is some elementary evidence for this. Rather than fretting about long-term capital market access, direct creditor sanctions or democratic constraints on contract abrogation, Mexico's policymakers themselves claimed to be most concerned about the *immediate* consequences that default would have on access to short-term credit, private sector confidence and international trade. In his written account of the crisis, Finance Minister Silva Herzog (1991:58) observed that "a suspension of payments is always an attractive alternative for debtors; but for Mexico, in those months, the alternative had

some serious risks." Citing the fact that Mexico imported 30 percent of its domestic consumption of corn – the country's main food staple – from the US and that his government feared losing access to trade credit, and citing furthermore the facts that Mexican industry remained "highly dependent on imports"; that the imposition of a unilateral moratorium would "run counter" to Mexico's dependence on foreign resources; that such a moratorium would likely trigger greater private sector uncertainty; and that "a condition of autarky" produced by a failure to service the country's towering debts "would have gone against the growing interdependence among nations," the Finance Minister seemed to firmly underline the crippling knock-on consequences that a state default would have on overall economic performance (Silva Herzog 1991:58). Gurría highlighted similar concerns in an interview, citing as the first and foremost consideration of the Finance Ministry's crisis management team "the loss of access to short-term credit," alongside the danger that a default would cut off investment flows to the private sector and threaten the steady supply of corn from the United States. After all, the former Director of Public Credit and current OECD Secretary-General emphasized, access to credit is the "bread and butter of trade" (Gurría 2013).

These considerations were the product of deliberations made in a small crisis team convoked by Silva Herzog in June 1982. The crisis team, made up Angel Gurría (Director of Public Credit), Miguel Mancera (Director of the Bank of Mexico) and Alfredo Phillips (Deputy Director of the Bank) was instructed by the Finance Minister to weigh the "pros and cons" of Mexico's different policy options. The three men were all deeply concerned about Mexico's access to short-term credit from foreign banks. As Angel Gurría recalled, "it was crazy. We held in our hands the fate of Mexico, maybe the fate of the world. But we couldn't talk to anybody. We couldn't even ask lawyers what to do. If we hired an American lawyer, he'd blab, and the banks would stop all loans" (cited in Kraft 1984:3-4). It later

emerged that the secret crisis team had discussed three policy options. The first was to defy foreign lenders and declare an outright suspension of payments on all or part of the government's current obligations. “That was like the atom bomb, the ultimate weapon,” Phillips recounted (*ibid.*). For Silva Herzog, this weapon “was not an option.” Instead, the Finance Minister pledged that “Mexico would behave as a responsible debtor” (Babb 2001:21). Why so? When pressed on the question, Angel Gurría once again highlighted the fear that the government and private sector would be cut off from foreign credit and investment: “if we defaulted everybody would be bankrupt, but it would also stop capital inflows to Mexico” (Gurría 2013). Silva Herzog remembers that “we asked ourselves the question what happens if we say, 'No dice. We just won't pay,'” and notes that “there were some partisans of that.” But in the end, defaulting on the debt “didn't make any sense” to Silva Herzog (cited in Kraft 1984:4). Angel Gurría (2013) summarized the general consensus of the crisis team as follows: “our logic was simple: there can be no default.”

Mexico was particularly vulnerable to the spillover costs of default because of its relatively deep financial and commercial integration and its dependence on investment and imports from the United States in particular. As Aggarwal (1996:363) has noted, Mexico's “economic recovery depended on trade and foreign investment,” and the country's position “was further weakened by its dependence upon maintaining amicable relations with the international financial community.” A particular weak spot in this sense was the position of the Mexican banking system, which had played an important role in intermediating international loans to the Mexican government and which was very vulnerable to the spillover costs of a sovereign default. As Alvarez (2014:1) has recently shown, “the imbalances which Mexican banks incurred in running their international operations eventually brought them to the brink of bankruptcy once the crisis began. Given that the banks that were at risk

represented a large share of the domestic market, ... the whole Mexican banking system was threatened with collapse." Alvarez (2014:26) furthermore shares archival evidence showing "that the fragility of the commercial banks and their overseas branches was a major worry for the Mexican financial authorities." As a result, during the frenzied days of June and July 1982 – and for the eight years to follow – the principal objective of the finance ministry and central bank was to avert the spillover effects that default would have had for the domestic banking system and on the ability of the public sector and the private sector to trade and to borrow. The consequences of a credit cut-off would have been profoundly destabilizing for the Mexican economy, but they would have been particularly painful for the local elite. "Certainly a moratorium was discussed," Silva Herzog (1991:59) concluded, "but it was rejected. We decided to negotiate and avoid confrontation."

Enforcement Mechanisms

Mexico's growing dependence on foreign sources of credit and its vulnerability to creditor demands was in turn rooted in a number of structural changes in the global political economy. Three changes in particular stand out. First, at the level of international lending, the dispersed bond finance of the 1930s had by the 1960s and 1970s given way to highly centralized creditor syndicates whose international lending was overwhelmingly co-ordinated by big Wall Street banks. This high concentration of Third World debt provided a solution to the collective action problems that had plagued the dispersed bondholders of the gold standard era, facilitating the emergence of a coherent international creditors' cartel. Second, at the level of the global financial architecture, the IMF had been brought into existence and was tasked with international crisis management. In the 1980s, the IMF's role

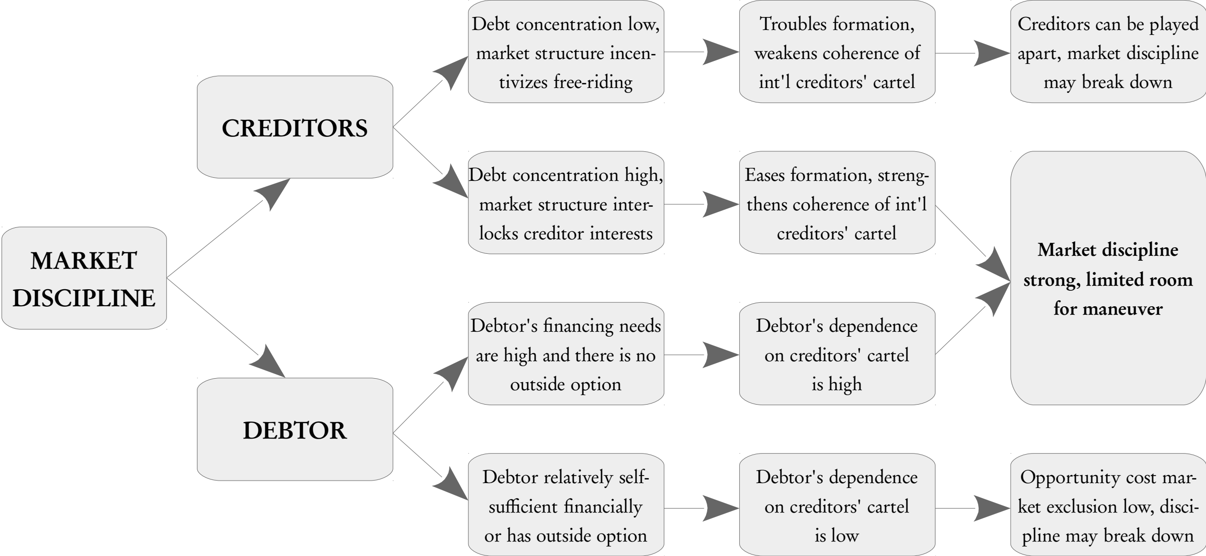
changed dramatically as the Fund sought to re-establish its standing and reinvent its purpose in the wake of the collapse of the Bretton Woods regime. Over the course of the crisis, the IMF developed into a *de facto* international lender of last resort to keep crisis-ridden debtors in the lending game, while simultaneously serving as a fiscal disciplinarian to enforce policy conditionality and a "global capitalist planner" to corral the commercial banks into their international creditors' cartel and induce them to act in their collective self-interest. Third, at the level of the borrowing countries themselves, the growing dependence of governments on foreign sources of credit and investment had important consequences for their *domestic* political economy, empowering social groups that were already relatively integrated into the world economy at the expense of the less mobile groups that remained more popular and national in character. Effectively, this meant that wealthy domestic elites with orthodox policy preferences gained in strength compared to workers, peasants and the unemployed.

The result of these three structural changes was to significantly increase the power of financial interests domestically and abroad. As Lipson (1981:606) pointed out early on, the implicit threat of losing "continued access to credit," whether from international banks, financial institutions or domestic elites, created a set of "stable expectations that debts are to be serviced promptly if there is any economic possibility of doing so." If the theory of structural power is correct, we should therefore expect two different sets of observations in the Mexican case. First, at the level of processes, we should expect to find evidence of the three enforcement mechanisms resulting from the structural changes outlined above: the changed structure of lending should ease the formation of an international creditors' cartel and strengthen market discipline; the emergence of the IMF as lender of last resort should make it easier to enforce policy conditionality and induce private creditors to act in their collective self-interest; and the international bridging role fulfilled by domestic elites should

systematically strengthen an anti-default coalition with close ties to foreign creditors, thus helping to internalize fiscal discipline into the debtor's state apparatus. Second, at the level of outcomes, we should expect to see little room for unilateral action by Mexico and other debtors (i.e., high cost of non-compliance); a generalized absence of default or restructuring *until after* a significant reduction of exposure by the international banks; and a distribution of adjustment costs that has domestic elites and foreign creditors emerging as clear winners from the debt game. The following sections will test the evidence for each of these points.

Syndicated Lending and the International Creditors' Cartel

Figure 4.5 – market discipline mechanism:



The first major difference between the Great Depression and the Latin American debt crisis lay in the structure of international lending and in the emergence of syndicated bank loans as the principal source of external finance for developing country governments. Whereas the lenders of the 1920s had been scattered groups of individual bondholders, who were notoriously vulnerable to collective action problems and who often failed to sustain a coherent creditors' cartel, the lenders of the 1970s were mostly commercial banks that were

in turn organized into international lending syndicates revolving around a small circle of systemically important and politically influential Wall Street banks (Griffith-Jones 1988:6). This led to an extraordinarily high degree of debt concentration in a small number of US financial institutions, which were in turn dangerously over-exposed to Third World debt. In 1982, Mexico's debt alone stood at $82 billion and amounted to 44 percent of the capital of the nine largest US banks, with some institutions holding a sum of Mexican debt equivalent to or in excess of their total capital base (Kraft 1984:9; Sachs and Huizinga 1987:555). The total exposure of these same banks to the 17 largest developing countries stood at a total 194 percent of their combined capital (Cline 1995:6-7). As late as 1987, the six largest Wall Street banks still accounted for more than half of the total developing country exposure in the United States financial system (Claessens, Diwan and Fernandez-Arias 1992:132).

The fact that the debt concentration was so high and that creditor interests in full repayment were now structurally interlocked by the very nature of syndicated lending greatly eased the ability of the big banks not only to establish common positions amongst themselves but also to enlist the support and allegiance of smaller banks and non-bank creditors. As Aggarwal (1987:21) notes, "the oligopolistic nature of the banking community and the acute overexposure of large banks facilitated cooperation." Having already begun to perceive themselves as *international* banks with "longstanding ties to other major institutions and permanent interests in the stable operation of international capital markets," the lenders of the 1980s found it much easier to coordinate collective action than the bondholders of the 1930s (Lipson 1985:210). And by managing to hold together a coherent creditors' cartel, the banks made the threat of cutting off short-term credit that much more credible, as it would be next to impossible for sovereign borrowers to secure alternative sources of finance in the event of default (Oliveri 1992:61/72). This served to strengthen

market discipline and significantly constrain the policy options available to the borrowing countries (Devlin and Ffrench-Davies 1995:129).

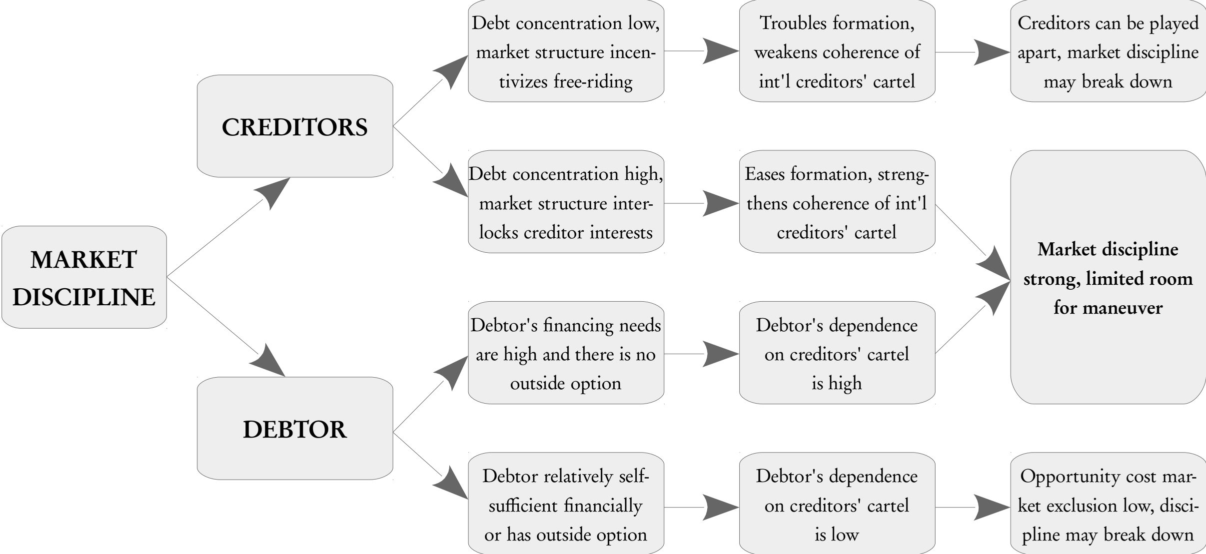
The growing power of creditors was further cemented by their very approach to crisis management. As one Latin American country after another fell into arrears on their amortization schedules after July 1982, creditors embarked on a complex set of negotiations with debtor country governments to reschedule principal payments, refinance outstanding debts, and ensure the continued servicing of interest. The central tenet in these negotiations was that each country was individually responsible for its own fiscal problems and each crisis should therefore be dealt with on an individual, case-by-base basis (Teichman 2001:49). While considered a logical and inconsequential self-evidence by the bankers themselves, it has rightly been pointed out that the "case-by-case approach wasn't innocent at all" (Tussie 2013). In reality, it served to isolate the borrowing countries and diminish their capacity to organize collective action, thereby precluding the formation of an opposing debtors' cartel and frustrating collective efforts to play private the creditors off against one another (Canak 1989:20). The result, as one expert on the international debt crisis of the 1980s has recently noted, was the informal institutionalization of a fundamentally unequal power relation that made it "much more difficult to call a moratorium in the 1980s" than in the 1930s (Stallings 2013). In effect, by 1982, "creditor clubs ha[d] successfully replaced unilateral default with multilateral debt consolidation" (Lipson 1981:622).

This highly unequal power relation between debtors and creditors in turn found an expression in the growing despair of the Latin American leaders. President José Sarney of Brazil described his sense of powerlessness in stark terms: "we cannot destroy the system," he said. "We can scratch it, but it can destroy us" (cited in Roodman 2006:16-17). In the case

of Mexico, this powerlessness was compounded by the country's great dependence on international credit and the import of corn from the United States (as discussed in the previous section). President López Portillo lamented that "my hand is on the helm of the ship, but I cannot direct the storm" (cited in Kraft 1984:39). By the start of 1982, Mexico found itself under intensifying market pressures, and in April López Portillo was compelled by market discipline to produce a stringent austerity budget even in the absence of the IMF.

The IMF: Fiscal Disciplinarian and "Global Capitalist Planner"

Figure 4.5 – market discipline mechanism:



But market discipline was not enough. As interest rates soared, maturities shortened and capital flight spiraled out of control, the bankers' main source of power now threatened to undermine itself. Mexico and the other Latin American debtors were at risk of being cut off from short-term credit and thereby rendered incapable of refinancing their outstanding obligations. This in turn sparked fears in Washington and New York of an impending US banking crisis. According to one White House official, Chairman Paul Volcker of the US Federal Reserve was convinced that "the banking system was about to collapse" and pressed

both President Reagan and Treasury Secretary Regan to take action (Lissakers 1983:164). In a later study, the Federal Reserve Bank of New York wrote that "bankers and policymakers faced a threat of financial disorder on a global scale not seen since the Great Depression" in case Mexico or another major Third World debtor were to default on its obligations (cited in Helleiner 1994:176). In response, the administration began to pressure Congress to raise the US contribution to the International Monetary Fund and at the same time insisted that further loans be made conditional on highly punitive reforms inside the debtor countries to ensure the uninterrupted flow of interest payments. The continued payment of interest was crucial because under US regulations the banks were required to write down any 90-day arrears on interest payments as 'non-performing' loans, which in turn would require them to make loan-loss provisions, cutting into their overall profit rates. For this reason the US made the prevention of a Mexican default the pivot around which its Latin American crisis management strategy was to revolve for the rest of the decade (Bailey and Cohen 1987:24).

As the crisis of the 1980s unfolded, the IMF came to play an increasingly central role both as a fiscal disciplinarian of the debtor countries and as a "global capitalist planner" at the head of the international creditors' cartel. This marks another clear contrast to the 1930s, when there was no IMF and no hegemonic power willing or able to act as a lender of last resort and enforcer of bondholder interests (Kindleberger 1973). Yet the importance of the Fund was not so much a product of the scale of its lending – which remained relatively small throughout the crisis – but rather hinged on the fact that both creditor governments and private banks almost always insisted on an IMF Standby Agreement before opening rescheduling negotiations with the debtors (Wood 1984:705). By making the Fund's stamp of approval a prerequisite for an agreement with the banks, the creditors' cartel provided the IMF with a gatekeeper function that allowed it to threaten debtors with immediate

capital market exclusion in the event of non-compliance (Delamaide 1984:111). This is how the IMF came to play its new and central role in the crisis despite its relatively modest financial contributions in terms of total bailout funds: “It is the catalysing effect of IMF agreements which gives the fund its real powers... [T]he loans negotiated after an IMF agreement are far greater than the IMF loan itself” (Körner, Maass *et al.* 1986:65).

A major turning point came during the annual IMF meeting on November 16, 1982, when Managing Director Jacques de Larosière told an assembled group of bankers that the Fund was no longer capable of shouldering the enormous burden of re-capitalizing Mexico by itself, and informed them that if they did not raise another $5 billion in new loans to the country, the Fund would refuse to sign a crucial stabilization agreement with the Mexican government. Since this would immediately force Mexico into default and thereby possibly push dozens of banks into bankruptcy, the seemingly casual statement really amounted to an unprecedented order: lend or die (Lipson 1985:223; Delamaide 1984:112). Although the bankers were initially shocked and outraged by the IMF's sudden and unexpected shift towards “concerted lending,” they quickly realized that they had little choice in the matter. While it was in the narrow self-interest of each bank to withhold further credit and reduce its exposure, the sum of these seemingly rational investor decisions risked tipping Mexico into insolvency – an outcome that would end up harming all creditors. As Griffith-Jones (1988:3) observed, “'involuntary lending' was in the interest of the *collective of creditors*, because it avoided default.” The banks in effect needed the IMF to counteract the logic of the free market – which would have resulted in creditors pulling out of Mexico *en masse* – and help keep their creditors' cartel together. “In a capital-scarce world,” Pastor (1989:91) concluded, “the IMF became a sort of global capitalist planner.”

Perhaps the most important contribution of the IMF, however, was its function as a financial watchdog capable of imposing and enforcing strict policy conditionality on the debtors. As Citibank chairman Walter Wriston confirmed, "the fundamental contribution of the Fund is the discipline imposed on debtor countries, not the amount it lends" (cited in Bernal 1982:82). Former IMF Managing Director Johannes Witteveen agreed, calling the Fund a "disciplinary mechanism" for indebted states that have lost their creditworthiness (cited in Delamaide 1984:221). Despite the inconvenience of concerted lending, the bankers were therefore quite happy to go along with a greatly empowered IMF. Past experience played an important role in convincing them of the need for a strong lender of last resort. As Roddick (1988:38) pointed out, "the banks had already learned from their experience of negotiating the Polish debt in 1981 the importance of an effective bankers' cartel, and from their attempts to control Peruvian economic policies in 1978 the importance of having the IMF as a watchdog with real teeth to monitor Third World economies." Between 1976 and '78, a number of Wall Street banks had tried to organize a rescheduling of Peru's debt, without IMF involvement, conditional upon an austerity program designed and monitored by the banks themselves. As Delamaide (1984:63) writes, "the experiment failed decisively." Peru's economy collapsed, budget targets were flaunted, the debt spiraled out of control, and the banks were accused of "Wall Street imperialism." Having burnt their fingers once, the bankers "drew the lesson that commercial banks could not impose conditionality, only the IMF could" (Lipson 1981:623).[26] And so the banks – content to let others do the dirty

26 As Karl Otto Poehl, West-Germany's governor to the IMF, put it around the same time: "the IMF is our only hope. It is the only institution that can lend money and impose conditions for doing so. No government can do this, nor any bank" (cited in Branford and Kucinski 1988:18). Similarly, the Vice-President of the Bank of Canada argued that "there certainly is a need for [the IMF] to be in there, as a lender and as a disciplinarian and that's the thing all of us like about the IMF. They, perhaps like no one else, can make conditions on loans, which ensures some tightening of the belt" (cited in Roddick 1988:44).

work – decided to retreat to the wings, "leaving the IMF center stage to face the barrage of criticism" (Branford and Kucinski 1988:111).

Given its central role in administering policy conditionality and thereby preventing default, it is no surprise that private creditors generally hailed what one banker referred to as "the IMF's triumphant return" in the 1980s (cited in Leslie 1983:24). This constituted a remarkable reversal in the Fund's fortunes compared to the capital-abundant conditions of the 1970s: where in the late 1970s global capital markets had been awash with cheap credit, leaving the IMF increasingly incapable of enforcing policy conditionality on its borrowers (who could simply ignore the Fund and turn to the markets to refinance their outstanding obligations), by the 1980s the severe global credit contraction put the IMF in a position of unprecedented power. The proportion of upper credit tranche IMF lending under conditionality increased from under one-third to 96 percent between 1973 and '83 (Pastor 1989:91). By 1984, a total of 66 developing countries – over half the IMF's member countries in the Global South and three out of four Latin American members – had fallen under IMF policy conditionality (Chahoud 1991:31). As IMF chief de Larosière himself put it, "adjustment is now virtually universal ... Never before has there been such an extensive yet convergent adjustment effort" (cited in Wood 1984:706). At the same time, the World Bank stepped up the conditionality of its aid as well, mostly through the expansion of structural adjustment lending and the creation of the Special Action Program, providing rapid disbursements of emergency credit in return for structural reforms. According to some, the World Bank's conditionality was "arguably more demanding than the Fund's" (Wood 1984:707).

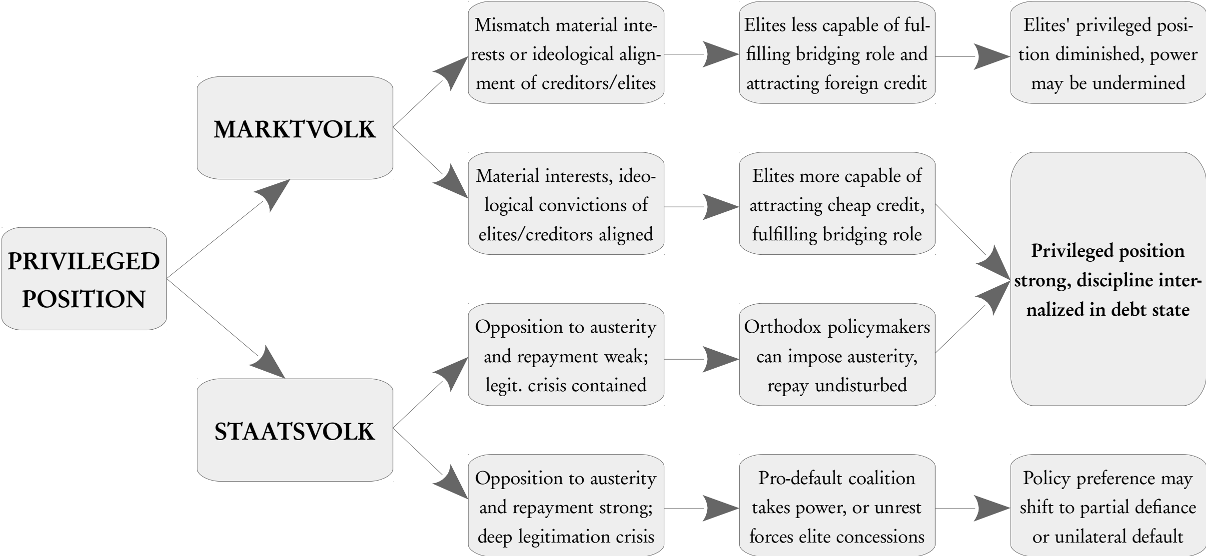
The imposition of policy conditionality and the coordinating role of the Bretton Woods institutions – backed by the US Treasury and Federal Reserve – thus served as a

crucial enforcement mechanism of fiscal discipline, without which the debt could not have been repaid. The Mexican case reveals just how important the Fund had become in preventing unilateral default. When Silva Herzog met Jacques de Larosière on August 13, on the fateful "Mexican weekend" lauding the start of the Latin American debt crisis, the latter expressed his willingness to help but insisted, in the words of official IMF historian James Boughton (2001:290), that "Mexico would have to find a way to avoid defaulting on its debts." In a sign that preventing default had now become the Fund's overarching policy objective, de Larosière informed Silva Herzog that the IMF could only provide him with financial assistance "if the government stayed current on its interest payments and reached agreement with its creditors regarding the rescheduling of principal payments"; a condition that prompted Karin Lissakers – a US Treasury official and later IMF Executive Director – to accuse the Fund of acting as an "enforcer of the banks' loan contracts" and imposing austerity on Mexico with the narrow objective of "free[ing] foreign exchange in order to service debts" (Boughton 2001:290-291; Lissakers 1983:167).

In the same meeting, de Larosière told Silva Herzog to adopt far-reaching austerity measures "to convince the outside world, particularly the banks, that the Mexican economy would indeed soon be set on the path of return to order and stability" (Teichman 2001:48). De Larosière's parting words to the Mexican Finance Minister said it all: "don't do anything unilaterally" (cited in Kraft 1984:7). "The IMF adjustment program," the Fund's Managing Director later reflected, "was the anchor of everything else" (cited in Kraft 1984:8).

The Bridging Role of Mexico's Bankers' Alliance

Figure 4.7 – privileged position mechanism:



It would be all too easy to conclude on the basis of the above discussion that Mexico was forced by external powers – the international creditors' cartel, the US government and the international financial institutions – to keep servicing its debts. Such an interpretation, however tempting given the available evidence, would nevertheless be too simplistic. In fact, Mexico's deepening integration into global financial markets and its growing dependence on foreign credit had major implications for its domestic balance of power, bringing back to the surface a number of long-standing political conflicts in which the political and financial groups that maintained close ties to foreign creditors and shared their interest in austerity, reform and full debt repayment, gradually found their position strengthened *vis-à-vis* those who retained a degree of loyalty towards the popular sector.[27] The reason these more orthodox elites were strengthened was because they were seen to be more capable of attracting cheap credit and providing a bridging role to the international financial establishment.

27 "In economies very open in their capital flows, with a very internationalised entrepreneurial class, there are additional (domestic) constraints imposed on government policy – to those coming from the policy conditionality attached to the IMF or World Bank lending, and to the broader constraints on growth posed by the limited availability of foreign exchange and of domestic savings" (Griffith-Jones 1988:356).

The orthodox elites revolved around the politically influential circle of Mexico City bankers and the big industrial exporters of Monterrey who depended on them for credit, as well as their allies in the Finance Ministry and the Bank of Mexico. This class coalition of sorts, which Maxfield (1990) referred to as the "bankers' alliance," was central to the efforts of the Mexican government to refinance its internal debt, stem capital flight and revamp private investment. As the government moved ahead with IMF-sponsored capital account liberalization, the lucky Mexicans who owned capital could move it to the United States, where they would hold it in bank accounts, real estate investments or stock exchange portfolios, safe and immune from inflation and seemingly endless devaluations. The option of relocation and the credible exit threat that these elites thereby obtained gave them considerably more leverage in economic policymaking. Moreover, it was precisely the integration of this wealthy elite into the US banking system that made it so unlikely that Mexico's rich would ever support a unilateral default or even a negotiated multilateral restructuring; after all, such measures could topple the very banks that now held their savings.

But the bankers' alliance was not the only domestic coalition vying for power. In 1982, Mexico was riven by a fierce political conflict on how to respond to the debt crisis. Silva Herzog (1991:57) has confirmed that "inside the government there were conflicting positions." On the one hand, the bankers' alliance – backed by its ideological allies in the Finance Ministry and the Bank of Mexico – argued for an ambitious domestic adjustment program in combination with a bridging loan from the IMF and a continued commitment to debt repayment. On the other, the representatives of the national-popular coalition inside the PRI – the so-called "radicals", who claimed to represent workers, peasants and national industries and who dominated not only the Ministries of Labor and National

Patrimony but also López Portillo's presidential office[28] – emphasized the structural causes of the crisis and insisted that Mexican citizens should not be made to pay for an investor stampede that had essentially been triggered by the monetarist orthodoxy of the US Federal Reserve. In Silva Herzog's (1991:57) view, the radicals in the administration believed "that it was possible to maintain the economic expansion and resist the pressure of the financial constraints." It was the latter group that had dominated economic policymaking over the past decades of financial repression and import substitution, but with the rapid loss of investor confidence exposing Mexico's increasing dependence on foreign credit, the crisis of 1982 was to reveal the growing ability of the bankers' alliance to set the economic agenda – and the dramatic extremes to which López Portillo and the radicals within the PRI were willing to go in an attempt to counter them (Silva Herzog 1991:58; Maxfield 1990).

As repaying the debt required harsh austerity measures to free up foreign exchange, ordinary Mexicans found themselves bearing a heavy burden of adjustment. Between 1981 and 1983, imports and real wages fell by two-thirds, while the country's debt rose by over a third (Boughton 2001:540). These dynamics angered López Portillo and the radicals inside his administration. The President was reportedly infuriated by regular reports of banks, businesses and wealthy Mexicans sending multiple billions of dollars to the US even as his administration was forced to cut back on public spending and raise taxes on the poor. In August 1982, López Portillo decided that it was time for action. He summoned his top radical economists, José Oteyza and Carlos Tello, and set up a secret advisory committee in Paris to study Mitterand's bank nationalization of 1981 (Delamaide 1984:103). The Mexican

28 Maxfield (1990) refers to this policy alliance as the "Cárdenas coalition", after former President Lázaro Cárdenas (1934-'40), whose national-popular government sided with workers and peasants and who set out to pursue some of the original goals of the Mexican Revolution, including the nationalization of oil, the unionization of workers and some of Emiliano Zapata's envisioned land reforms.

President was under significant pressure from his allies in the left-wing of the PRI, whose intellectual leaders had been critical of the bankers' alliance for years. Some even described the Mexican Bankers' Association as the "owner of the country" (Concheiro and Fragoza 1979:245, cited in Maxfield 1990:144). Carlos Tello himself viewed Mexican "finance capital as the dominant faction of capital in the 1970s" and blamed the banks for undermining the state's room for maneuver and its prioritization of social goals (Tello 1984:45, cited in Cypher 1990:123). Mexico's deepening integration into the global financial system only served to amplify these concerns. One observer noted that, "if, in the past, the president and the government were increasingly helpless in the face of bankers and businessmen in general, with the internationalization of banking ... the possibilities of action were further limited" (Blanco, cited in Maxfield 1990:144). Between 1970 and 1977, the Mexican banking sector had also become much more concentrated, with 225 banks merging into 87 and with "powerful domestic financial groups ... able to boost their market power via the centralization and concentration of finance capital" (Marois 2007:7). There was therefore an acute awareness among radicals of the structural power wielded by domestic banks through their control over credit. Cypher (1990:123) notes that "the banks were important participants in the process of granting the Mexican government international loans from the private transnational banks ... and were crucial to the government in funding and refunding Mexico's *internal* debt." To López Portillo and his advisors, it therefore seemed self-evident that "nationalizing the banks would break the political and economic power of Mexican bankers and of the large-scale industrialists with whom they were associated," and thereby restore a degree of policy autonomy to the fiscally distressed state apparatus (Maxfield 1990:144).

And so, on Wednesday, September 1, 1982, just a week and a half after reaching a preliminary agreement with foreign bankers and the IMF on a rescheduling of Mexico's

debts, President López Portillo – who was due to leave office on December 1 – used his last annual *Informe* to announce the nationalization of the banking system and the imposition of capital controls to stem further capital flight. The head of state dramatically declared that "in the last few years it has been a group of Mexicans, led and advised and supported by the private banks, who have taken more money out of the country than the empires that exploited us since the beginning of time" (cited in Kraft 1984:39). Bank of Mexico Director Miguel Mancera, known for his orthodoxy and staunch opposition to capital controls, was replaced by the radical economist and presidential loyalist Carlos Tello. Finance Minister Silva Herzog, who had been kept uninformed about the President's decision until the last moment, immediately tendered his resignation, but – in a sign of the bridging role he fulfilled towards foreign creditors – the President refused to accept it. Silva Herzog was needed for negotiations at an IMF summit two days later. As Maxfield (1990:146) put it, "Mexico's economic future depended on successful negotiation of the debt. Silva Herzog's key role in the negotiations left López Portillo no choice but to keep him in the cabinet."[29]

Unsurprisingly, the international financial community was terrified by the dramatic bank nationalization, which many feared to be the prelude to a unilateral moratorium or even a wholesale repudiation of Mexico's debt (Bailey and Cohen 1987:20-21). It was clear to foreign creditors that López Portillo could not be trusted. As a result, for all the radical rhetoric in which it was ensconced, the president's poorly planned decision backfired disastrously, leading to a number of profoundly anti-social consequences. While the imposition of capital controls had been intended to stem the outflow of capital, the bank nationali-

29 Mexico's President was not the only one who depended on the Finance Minister's bridging role. In a sign that Mexico's creditors had come to rely on Silva Herzog's pro-creditor leadership as well, US Treasury Secretary Donald Regan actively pressed his Mexican colleague not to resign. "It was a critical moment for Mexico and for the international financial system," Boughton (2001:302) recalls, "and Silva Herzog's resignation would have left a huge vacuum in the [creditors'] circle of power and influence."

zation actually ended up feeding the investor panic and deepening capital flight. Moreover, by taking over the banks the government also assumed the bankers' debts, forcing them onto taxpayers. As Maxfield (1990:160) wrote, “to some extent the nationalization served to bail out financially threatened banks and their industrial partners.” This in turn led some to remark that, although the language of the Mexican nationalization was very different from the 1983 bank bailouts in neoliberal Chile, “the substance of the intervention was quite similar” (Diaz-Alejandro 1984:378). In an attempt to fight the bankers, López Portillo had ended up nationalizing not their wealth and power but their *liabilities*, as a result of which the state now held almost the entire foreign debt of the private sector (Buffie 1990:526). For his part, Director of Public Credit Angel Gurría admitted that, “even though it it could have been managed differently and that the decision to nationalize might have been taken for the wrong reasons, the nationalization was a way of solving the financial difficulties of banks that would otherwise have had to declare themselves insolvent” (Alvarez 2014:26).

In the end, the nationalization did little to weaken the bankers' privileged position. Like a game of Whack-a-Mole, the bankers' alliance instantly popped back up on the stock exchange. No sooner than their banks had been nationalized, their owners set up a parallel banking system that allowed them to continue their moneymaking activities in a new form, most notably through the operation of *casas de cambio*, the exchange houses that dealt in the majority of foreign currency transactions. Given the wild exchange rate gyrations of the 1980s – the peso was to lose more than 2,000 percent of its value against the dollar over the next six years – operating these exchange houses provided the bankers with ample opportunities for currency speculation. Moreover, with the now nationalized banks heavily overexposed to government debt, the government was forced to turn to the stock exchange to refinance its internal obligations – leading it back into the arms of the same bankers López

Portillo had tried to outsmart. The resurgence of the bankers' alliance was therefore a direct consequence of the deepening debt crisis and the growing structural dependence of the state on private credit. Whereas the Bank of Mexico had funded over three-quarters of interest payments on the government's internal debt before 1983, basically moving the debt from one part of the state to another, after 1983 some 57 percent of the internal debt was being funded by the private sector, with local elites becoming the state's main source of new credit (Cypher 1990:175). Since total interest payments on internal debt amounted to more than double the interest on external debt, the bankers not only gained control over "an extremely lucrative underwriting business" in internal debt, clawing back most of their losses from the nationalization, but they also greatly boosted their privileged position in politics and their leverage over the government (Cypher 1990:163).

As the bankers' alliance grew more powerful in spite of the bank nationalization, hopes of a national-popular exit from the crisis rapidly waned. In the months following the announcement of the nationalization, the representatives of the bankers' alliance set out to limit its impact by undermining its implementation. Maxfield (1992:76) highlights the fact that "Mexico's extreme international financial vulnerability in 1982 placed [Silva Herzog] in a very powerful position within the Mexican government." The Finance Minister's close ties to foreign creditors, both private and official, empowered him to almost singlehandedly set the government's spending priorities. Because he enjoyed the trust of the foreign banks, US Treasury officials and the IMF, Silva Herzog was most capable of extracting concessions and attracting credit on good terms, which in turn endowed him with considerable leverage over López Portillo, Tello and the radicals in the administration. This, combined with the systematic isolation of Tello by the close alliance that had already been forged between Silva Herzog, Volcker and de Larosière, meant that Mexico's debt policy effectively remained

shielded from López Portillo's resurgent radicalism. As Kraft (1984:44-45) reported, "Tello, looking back on the [IMF] negotiations a year later, gave the impression of a man battling, almost alone, for a good cause against the massed forces of evil." Despite complaining about the financial bureaucracy's alignment with the IMF and the banks, Tello never managed to outflank Silva Herzog and force foreign creditors to concede better terms. Carlos Salinas, the Minister of Budget and Planning and future President of Mexico, later confessed that he "had the feeling that de Larosière came away knowing he could be tough on Tello." One Finance Ministry official referred to Tello's meeting with de Larosière as "Tello's last stand" (cited in Kraft 1984:46). With the radicals now isolated and Mexico's dependence on foreign credit only growing stronger, the lofty goals of the nationalization never materialized.

The definitive turnaround came on December 1 with the inauguration of Miguel de la Madrid as 52nd President of Mexico. A Harvard-trained economist, De la Madrid was described as "an extremely cautious technocrat who had great admiration and respect for the international banking community" (Bailey and Cohen 1987:32). In a sign that the bankers' victory over the radicals was now complete, the first thing De la Madrid did upon assuming power was to partly re-privatize the banks. Although the new President could not fully reverse the nationalization, he "did whatever possible to ensure that the state administered to the needs and caprices of the old financial barons" (Cypher 1990:163). De la Madrid reinstated Miguel Mancera as head of the Bank of Mexico, kept Silva Herzog as his Finance Minister, and brought with him into government what was at the time considered to be "the most technocratic and homogeneous team ever to rule Mexico," with two-thirds of the cabinet holding graduate degrees in economics and over half having been educated abroad (Teichman 2001:131). This dramatic turn to orthodoxy raises the question why the radically inclined López Portillo ever handpicked De la Madrid as his successor in the first place. Was

this simply about the triumph of neoliberal ideas? The ideological shift certainly played an important role. But there was a more practical reason: the state urgently needed resources to keep itself solvent, which forced the national government to try to attract credit – and for that it had to establish *credibility*. According to Babb (2001:20), the decision by López Portillo's to appoint De la Madrid as his successor "almost surely was a measure designed to inspire the confidence of bankers and investors." Earlier, the President had appointed Silva Herzog to the Finance Ministry for the exact same reason. Just as Silva Herzog was widely considered to be "more popular with the New York bankers than ... with some of the folks back home," De la Madrid enjoyed a reputation among investors as "a technocrat, adept at modern economics but out of touch with Mexico's revolutionary traditions" (*Economist* 1984:60; *Economist* 1981:68). Both Silva Herzog and De la Madrid strongly backed IMF-led adjustment and "made a priority of keeping good relations with the international financial community by servicing [the] debt" (Bailey and Cohen 1987:21).

The final victory of the bankers' alliance cemented the structural power of finance over the Mexican government and served to internalize fiscal discipline into the Mexican state apparatus. For the rest of the decade, apart from some heightened tensions following the disastrous earthquakes of 1985, Mexico remained one of the most compliant debtors on the continent. What is particularly striking about the Mexican case – in particular when contrasted to other countries on the continent – is the relative absence of street protest and political opposition to austerity and debt repayment. Middlebrook (1989:196) notes that "the economic reverses suffered by the urban working class do not distinguish the Mexican case from labour's situation in other Latin American countries," but what does differentiate it is the "generally restrained character of Mexican organised labour's response to these challenges." Organized labor in Mexico was completely controlled and co-opted by the PRI,

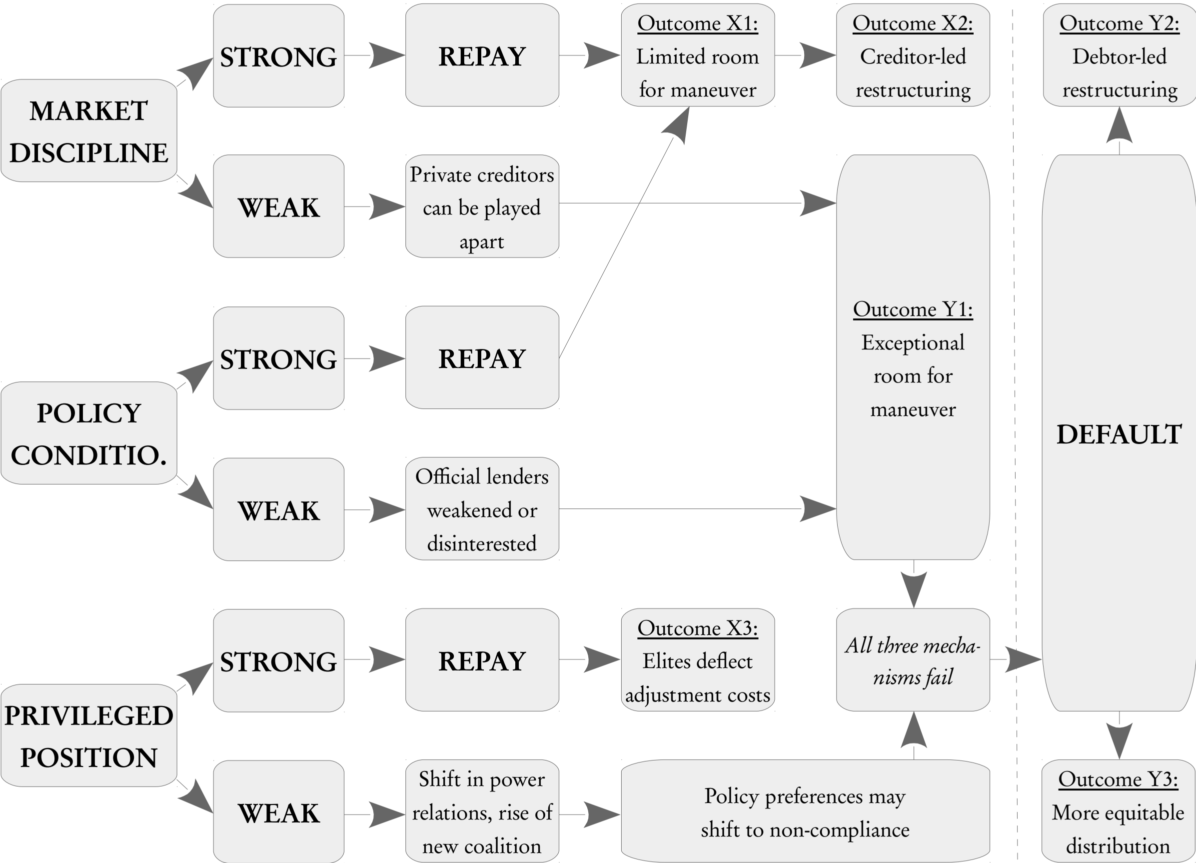
blocking a main channel for the expression of popular concerns and the defense of labor interests.[30] Walton and Ragin (1989:218), in their study of IMF riots across the continent, note that "austerity protest in Mexico has been muted by organized labor's preference for maneuvering within the theater of official institutions, by a defensive Left, and by industrialists' exploitation of the crisis as an occasion to increase productivity." While IMF riots contributed to the downfall of governments in Peru in 1980 and '84, Brazil in 1983, Panama in 1985 and Haiti in 1986, the relative absence of mass mobilization and the thorough co-optation of organized labor in Mexico gave the bankers' alliance free reign to pursue its orthodox austerity measures and neoliberal reforms.

In the remaining years of the crisis, strong ties developed between the IMF and the technocrats in the subsequent governments of De la Madrid and Salinas. As a result, the austerity measures and structural reforms required to service the debt no longer needed to be strictly imposed from abroad but were now to be formulated and monitored in a "collaborative effort" between IMF staff and Mexican authorities. Meanwhile, as Mexico's debts kept being rolled over by its creditors, international bankers quietly rejoiced at the endless sequence of austerity measures and debt reschedulings. One banker even publicly exclaimed that Mexico "is a cash cow for us. We hope they never repay!" (Oliveri 1992:41). This, in turn, prompted Karen Lissakers (1983:175) of the US Treasury Department to lament that "the current solution to the international debt problem is disturbingly similar to the policies and processes that created the crisis in the first place."

30 As Middlebrook (1989:196) notes, the Confederation of Mexican Workers and the Mexican Labor Congress "have not mobilised union members to challenge openly policies that harm workers' interests. Instead, organised labour has persisted in a well-established tradition of incremental, intra-elite bargaining with government officials on a wide range of economic and political issues – despite irrefutable evidence that this approach has failed to provide benefits to compensate for workers' sacrifices."

Outcomes of the Crisis

Figure 4.8 – outcomes according to structural power hypothesis:



The findings presented so far appear to confirm the structural power hypothesis and the effectiveness of the hypothesized enforcement mechanisms. But if the structural power hypothesis is to have real explanatory merit, we should be able to connect these observed mechanisms to a corresponding set of outcomes. First of all, since structural power imposes a "bias on the freedom of choice" (Strange 1994:31) by limiting the policy options available to national governments, we should see little or no room for unilateral action by Mexico and other Latin American debtors. One important sign of this limited room for maneuver would be a very high cost of non-compliance for the more confrontational debtors, as such high costs would systematically disincentivize non-compliance. Second, if private creditors

were truly structurally powerful and the policy options for debtors constrained, we should expect the crisis to be resolved at the initiative of the creditors, not the debtors'. Finally, as a result of the third enforcement mechanism, we should observe a skewed distribution of adjustment costs that has domestic elites and foreign creditors emerging as clear winners, as their power would allow them to shift the burden onto others. As we will see next, these outcomes did indeed materialize in the Mexican debt crisis.

Very Limited Room for Maneuver

How much space did Mexican policymakers have to take more confrontational, unilateral action? Mexico's bankers' alliance remained extremely cooperative throughout the crisis and did not break with any of its foreign obligations, making it difficult to test the counterfactual scenario of a default. Nevertheless, we can identify two points at which the Mexican government briefly did pursue a more defiant response to the crisis. On both occasions it was quickly compelled by its own structural dependence on foreign credit to retreat and return to orthodoxy. The first was the botched bank nationalization of 1982, which has already been discussed above. The following section will focus on the second brief phase of confrontation, which took place in 1985-'86 when Mexico was struck by two external shocks: a catastrophic earthquake that left over ten thousand dead and much of Mexico City in ruins, and a 60 percent fall in the oil price that caused the government to lose 20 percent of its revenue over the course of 1986 (Pastor 1987:13; Gurría 1995a:36). With $1 billion in principal falling due shortly after the earthquake, Angel Gurría – fearing "that he and his colleagues in government would be lynched if they proposed such a use of scarce resources in the midst of this calamity" – saw himself forced to negotiate yet another volun-

tary rescheduling with US banks (Boughton 2001:371). As a result, investor confidence collapsed. Gurría (1988:89-90) recalls that: “the mood in Mexico was ominous. Rumors about tens of billions being requested were widespread, together with the fear of unilateral default by the world's second largest debtor. The drop in oil prices generated a wave of demand for immediately halting payments which included all sectors of society.” He added that “even within the government, where such decisions were usually left to the Minister of Finance, a veritable chorus in favor of a moratorium arose.”

In this climate, even the most orthodox technocrats were now openly starting to doubt if Mexico's compliant approach on the debt still made sense. Gurría (1988:90) wrote that “this 'dialogue of the deaf' caused increasing frustration within Mexico, and made even the most reasonable and sophisticated observers advocate a harder line of negotiation.” As a result, “the Mexican negotiating team ... clearly started drifting towards a stronger response to the international financial community's apparent lack of understanding and support.” It was clear to Gurría and his colleagues that “the year 1986 marked the climax of Mexico's worst economic crisis in the post-war period” (Gurría 1995a:36). For the first time, the real possibility of a unilateral default was being raised by the Mexican government. President De la Madrid, the technocrat favored by Wall Street, openly accused the creditors of “choking Mexico to death” and threatened “an indefinite suspension of all debt service payments to commercial banks” (Bailey and Cohen 1987:42; Roddick 1988:114). In response, Federal reserve Chairman Paul Volcker flew to Mexico City for a top-secret emergency visit, where he impressed upon De la Madrid that there would be “an immediate suspension of all bank credits the moment Mexico took unilateral action” (Roddick 1988:114; Boughton 2001:439). It was this explicit reminder of the structural power of US finance that made De la Madrid climb down, but not before dumping his Finance Minister for having become too close to

foreign creditors (Teichman 2001:135). According to one Mexican official, Silva Herzog had become “a defender of the IMF without considering the internal repercussions” (cited in Pastor 1989:79). In hindsight, Boughton (2001:276) writes, Silva Herzog “wrestled with the idea of default throughout his term but always rejected it.” Gurría (2013) stresses that “we never used the threat of default. We stuck to the thesis that the country will lose its access to credit; it will lose its credit rating ... We never confronted the bankers ... There was a commitment to being responsible, being cooperative.”

Would a more radical administration have acted any differently? Even if the Mexican bankers' alliance had been ousted from power or forced by sustained pressure from below to promote national-popular interests at the expense of foreign creditors, Mexico's room for maneuver was greatly limited by the state's dependence on foreign credit. It is therefore unlikely that a radical government would have behaved very differently – and even if it had, its attempt at defiance would likely have failed, as it did in the case of López Portillo's bank nationalization. Two observations from other Latin American countries lend credence to this counterfactual interpretation: Argentina's brief threat, following its transition towards democracy, to declare a debt moratorium and create a Latin American debtors' cartel, and Peru's failed attempt at a heterodox repayment strategy from 1985 onwards. Both episodes of defiance were quickly undermined by the structural power of international creditors.

As we saw before, Raúl Alfolsín, Argentina's first democratic President after the fall of the *junta*, had announced a six-month moratorium on interest payments and was trying to gain support from regional leaders to build a unified debtors' front. In June 1984, eleven Latin American countries gathered in Colombia to set up the so-called Cartagena Group. Among Wall Street bankers, there was widespread concern that the meeting would be the

first step in the formation of a debtors' cartel to counter their own creditors' cartel. Such a debtors' cartel, they feared, would be able to threaten a collective default and thus extract better terms from the creditors. And so the banks quickly moved to reassert their tested case-by-case approach, making concessions to Mexico in the hope that this “model debtor” would help them defuse the potential bombshell of a Latin American debtors' cartel from within. As one banker put it, “we still think [a cartel is] a danger, and we ought to be ready to do something. Those countries that comply with the terms of [IMF programs] ... should be rewarded with better terms” (*Wall Street Journal*, June 6, 1984). One advisor confirmed that the US government and the banks “are dissuading the Latin nations from collaborating by promising more rapid treatment if they act alone” (cited in Aggarwal 1996:351).

Following the announcement of Argentina's moratorium, the Mexican government – in a clear display of “credit-rating self-preservation” (Cline 1983) – immediately moved to isolate Alfolsín, organizing a $500 million emergency loan by fellow Latin American debtor countries to cover Argentina's interest payments to its commercial creditors before the expiration of the 90-day legal limit on which the US banks would have had to write down their loans as non-performing (Tussie 1988:286-287). According to Roddick (1988:49), “the message was clear: Argentina would be totally isolated in any attempt to call the banks' or the US government's bluff.” Tussie (1988:289), moreover, observed that “the dynamics of 'credit-rating self-preservation' are not just a figment of the debtors' imagination.” Far from leading to the formation of a debtors' cartel and playing Argentina's creditors off against one another, Alfolsín's democratic brinkmanship united borrowers and lenders in their resolve to avoid an Argentine default. The banks insisted that that an IMF agreement was a prerequisite for any renegotiation of Argentina's debt and then waited “until the economy went into such a tail-spin that the recalcitrant debtor must come crawling back to the table”

(interview with a banker in *Business Week*, August 12, 1985). In a reminder of the spillover costs of default, the US Treasury Department made the strategic move of sending out a list of imports that would become unavailable in the event of an Argentine suspension of payments due to the drying up of trade credit. US Deputy Treasury Secretary MacNamar even asked Alfolsín: "have you ever contemplated what would happen to the president of a country if the government couldn't get insulin for its diabetics?" (cited in Roddick 1988:50). The message was clear: continued defiance would cost Argentina dearly.

By early 1985, Alfolsín had been forced into an embarrassing U-turn and found himself in the humiliating position of having to sign an IMF stabilization program while pleading to honor the odious debts of the military dictatorship that had gone before him – in full and on time. "The only solution," he now told the Argentine people in a televised statement, "is a policy of austerity that will be very hard and will require great efforts by everyone; it's called, my dear compatriots, an economy of war" (cited in Solanas 2004). Schuster (2008:164) writes that the government "became a prisoner of its own inability to control economic variables and the aforementioned foreign and domestic economic and financial powers." Mexico, meanwhile, was thrown a bone by the bankers to reward it for taking such a resolutely pro-creditor stance in its dealings with Argentina. In hindsight, for all the fear it stoked among creditors at the time, in light of Argentina's defiance, most observers agree that the Cartagena conference is to be remembered chiefly for what it did *not* do: none of the attending countries followed Argentina in forming a debtors' cartel, none ever threatened unilateral action, and none of them defaulted (Branford and Kucinski 1988:116). One Argentine observer even referred to the Cartagena group as a "phantom" that did "nothing revolutionary at all" (Tussie 2013). Far from laying the foundations of an international debtors' cartel, article 8 of the Cartagena declaration reaffirmed the debtors'

willingness to honor their debts and to continue with the adjustment efforts, as well as their unwavering commitment to the case-by-case approach. As Silva Herzog aptly described it, Cartagena was "a debtors' cartel to pay, not not to pay" – or, as he put it elsewhere, it was simply "a payers' club" (cited in Berg 1985:21; Roddick 1988:14).

The official creditor response to García's non-compliance in Peru was similarly swift and painful. Following García's announcement of a heterodox ceiling on interest payments equal to 10 percent of exports, the IMF and World Bank immediately withheld their next credit tranches and, in October 1985, US regulatory agencies declared US commercial loans to Peru to be "non-performing," undercutting its credit rating and greatly undermining its ability to obtain further credit on international capital markets. In August 1986, the IMF disqualified Peru from future loans altogether, further harming the country's credit rating and casting it – alongside Sudan, Liberia and Cambodia – into the world's credit rating dungeons of utterly ineligible countries (Roddick 1988:175). As with Argentina in 1984, creditors adopted a "wait and see" approach, forcing Peru – simply by withholding further credit – to slowly "stew in its own juice," as one banker put it (cited in Roddick 1988:174). Throughout this period, García had actually been very cautious not to alienate his private creditors. In a speech to Congress, he stated that his heterodox policies did "not mean that we will ignore our responsibilities to our foreign creditors." García promised to "resume payments in full when external circumstances permit. We want to pay because we are honest, and though we are mindful of the injustices of that debt, we assume our responsibility as a people that stands by recognizing its own mistakes" (cited in Roddick 1988:169-170). As Roddick (1988:170) writes, "a total moratorium was also deliberately ruled out, not least because Peru hoped to continue borrowing from some of its creditors."

The curtailment of short-term credit greatly limited Peru's room for maneuver and effectively forced the García government to monetize the governments' budget shortfall, causing hyperinflation and sending the economy into a tailspin. By July 1990, accumulated inflation reached 2.2 million percent, as GDP fell 7 percent and real per capita income dropped back to 1960 levels. Extreme poverty rate skyrocketed up 41 percent to a total of 54 percent, with social expenditures cut from $46 per person in 1986 to $12 in 1990 (Pastor and Wise 1991). With accumulation grinding to a halt, the state had become incapable of fulfilling its legitimization function. In 1990, widespread discontent over his policies led to García's electoral defeat, giving rise to the authoritarian rule of Alberto Fujimori, who immediately pushed through a package of far-reaching neoliberal reforms and privatizations that came to be known as the *Fujishock*, which rapidly restored Peru's standing among international investors and the IMF, but which also contributed to further social dislocation (Gouge 2003:364). Experts later pointed out the irony of the fact that García had actually ended up sending more money abroad in interest payments than the creditor-friendly conservative government before him (Ugarteche 2013). As these two counterfactual cases indicate, should a pro-default coalition ever have assumed power in Mexico, its room for maneuver would have been very marginal, and it is likely that even a defiant government would either have been quickly forced back into compliance, like Alfolsín in Argentina, or would eventually have been undermined by creditor powers, like García in Peru.

Crisis Resolution at the Initiative of the Creditors

A second outcome we should expect if the structural power hypothesis were correct and the room for maneuver of Mexico and the other Latin American debtors was really sig-

nificantly constrained, would be a pattern of crisis management in which the creditors took the initiative and the debtors followed. More specifically, since the lenders were mostly big and over-exposed international banks, we would expect the latter to fiercely oppose any debt restructuring at least *until after* they had managed to reduce their exposure to Mexican and Latin American debt. We have already seen that there was no real unilateral action to speak of, but what is remarkable is that for seven to eight years there was no real attempt to multilaterally resolve Latin America's debt problems either. It was not until the Brady deal of 1989-'90 that the external debts of developing countries – starting with Mexico – were restructured, one by one, slowly helping them to regain access to private credit. Up to that point, the international financial community had muddled through with one rescheduling after another, consistently refusing to force losses onto private creditors or to find a more lasting resolution to the crisis. By 1987, it was clear that this approach had failed to restore the creditworthiness of the borrowers. On November 30, 1987, the *New York Times* neatly captured the contradiction at the heart of the prevailing international policy response to the debt crisis: "There is a consensus of two things. One is that the debt has to be paid, and the other is that the debt cannot be paid."

An important turning point was reached in May 1987, when Citicorp bank took the initiative to raise its loan-loss reserves by 150 percent with an additional $3 billion, boosting its capital reserves to a quarter of its Third World debt. In the second quarter of 1987, the US banks added a total of $21 billion to their loan-loss reserves, as a result of which "the banks no longer had to live in terror of a Mexican default" (Aggarwal 1996:40/361). At least equally important was the proposal made by J.P. Morgan in December 1987 to exchange its discounted Mexican loans for securitized government bonds, which the bank could in turn sell on secondary markets, thus providing Mexico with a modest degree of debt relief while

providing J.P. Morgan with an opportunity to reduce its exposures (Aggarwal 1996:334). The Mexico-Morgan deal, which was concluded in 1989, was hailed as "a watershed for the debt strategy" and has been credited with "influenc[ing] later multilateral efforts to further alleviate Mexico's debt crisis [and leading] the way for the more sophisticated menu-driven deals of the Brady plan" (Boughton 2001:491; see also Gurría 1995a:36; Claessens, Diwan and Fernandez-Arias 1992:20). The build-up of loan-loss provisions and the reduction of the banks' exposure greatly reduced their vulnerability to an eventual debt restructuring. US bank exposure to the 17 largest debtors, which had stood at 130 percent of capital reserves in 1982, fell to 27 percent by the end of the decade. The result, Cline (1995:71/76) notes, "was to disarm the threat of the debt bomb to the international financial system."

At the same time, some members of Congress were becoming increasingly vocal in their criticism of the US approach to crisis management "for defending the interests of the banks to the detriment of US manufacturing firms and their workers" (Cline 1995:216). In January 1989, three bank regulators testified to Congress that the US banks could now withstand a large default, indicating that the Latin American debt crisis no longer posed an existential threat to the banks (*New York Times*, January 6, 1989; Aggarwal 1996:364). As a result, the bankers began to change their attitude towards debt restructuring. As one broker told the *New York Times*, the banks "have diminished vulnerability to Mexico ... The talk in 1982 was that the Mexican debt crisis meant the collapse of the financial system. [But] we have come a long way from that point" (cited in Oliveri 1992:73). While still vehemently opposed to forced losses, some degree of debt cancellation was increasingly starting to look attractive to the bankers as a way to keep Mexico and the rest of Latin America in the lending game. Finally, after the bloody repression of a major IMF riot in Venezuela – the infamous *Caracazo* of 1989, which by some counts left more than 3,000 people dead – US

officials, weary of stoking the flames of radicalism in the region, began to openly discuss the possibility of a multilateral debt restructuring. The result was Mexico's Brady deal of 1989, which paved the way for voluntary debt renegotiation across the developing world.

The full extent of debt relief obtained under the Brady plan has been a source of considerable debate among economists. In a letter to the IMF, Mexico's Finance Minister Pedro Aspe claimed that the Brady deal would save the country $4 billion a year until 1994, while the chairmen of Lloyds Bank and Midland Bank estimated that the plan would "save the country less than $1 billion in interest payments each year" (Aggarwal 1990:26). Sweder van Wijnbergen (1991:17), the World Bank's chief negotiator in the Brady restructuring, has argued that the deal managed to avoid a bailout of the creditors, but other observers have vehemently contested this assertion. Dooley, for instance, noted that "the amount of debt reduction was quite limited, especially when new official debt was added to the calculation of net debt reduction," while net reduction for Latin America as a whole only amounted to 15 percent of the total debt (Dooley 1995:279; Dooley, Arias and Kletzer 1994:7). One influential study found that the banks made significant financial gains in the restructuring while the debtors took big losses (Claessens, Diwan and Fernandez-Arias 1992:37). Others also found that "the amount of debt relief granted to Mexico was rather low, particularly when one compares it to historical standards" (Armendariz and Armendariz 1995:138). In the 1930s debt crisis, Latin American debtors had managed to secure "substantial" debt relief, with Jorgensen and Sachs (1989:79) finding that "the terms of the final agreements settling the defaults of the 1930s were highly favorable to debtors." In the 1980s, by contrast, the creditors clearly had the upper-hand in the negotiations.[31]

31 Cline (1995:220): "various accounts suggest ... that despite the high public profile of the IMF in calling for deep forgiveness, in the actual negotiations the institution did not press the banks." Cline ascribes the Fund's defense of creditor interests to the Treasury's single-minded insistence that the IMF should not

World Bank economists have recognized many of the aforementioned observations. Claessens, Oks and Van Wijnbergen (1993:1) show that Mexico received a total cash flow relief of around $4 billion per year, $2 billion of which would have occurred anyway as amortization would have been rolled over in the absence of debt restructuring. Noting that "in a $200 billion economy, 2 or even 4 billion seems like a small tail to wag a large dog," the authors argue that "the main benefit of debt relief was not to lower expected payments but to reduce uncertainty." The Brady deal, as it turns out, was more effective at restoring investor confidence by reducing bank exposures and marking the remaining debt to market – thereby allowing the banks to more realistically estimate the true value of their assets – than it was in reducing the debt burden. By restoring confidence, however, the Brady deal instantly caused interest rates to drop over 20 percentage points, enabling Mexico to return to capital markets and start borrowing from private lenders again (Crowley 1993:26). The Brady deal, in short, was more important for its psychological role in reducing uncertainty than it was for the financial aim of reducing Mexico's overall debt load (Cline 1995:43).

"The Rich Got the Loans and the Poor Got the Debts"

The final outcome we would expect given the above is a highly unequal distribution of the costs of adjustment in favor of foreign creditors and domestic elites. As it turns out, Mexico's poor did indeed overwhelmingly bear the costs of adjustment while the creditors – having successfully prevented both a unilateral Mexican default and an early multilateral debt restructuring – emerged from the 1980s largely unscathed, even making major profits (Aggarwal 1996:351). There is a broad scholarly consensus that, rather than serving the

take a side against the Wall Street banks in their negotiations with Mexico.

interests of ordinary people in Latin America, the international response to the debt crisis primarily served creditor interests – and the interests of big US banks in particular (Dooley 1995:275; Griffith-Jones 1988:9; Sachs 1986:406; Bertola and Ocampo 2012:16). At the same time, the structural power hypothesis should also lead us to observe a highly uneven distribution of adjustment costs *within* the debtor countries, as privileged domestic elites successfully shift the burden of adjustment onto weaker and less privileged social groups. Again, the evidence appears to confirm this expectation (e.g. Roodman 2006:17; Frieden 1991:218). In Mexico, workers, peasants and the urban poor paid a particularly heavy price under successive adjustment programs even as the elite managed to escape taxation.[32] With inflation averaging 93.1 percent a year between 1983 and 1987 and reaching 177 percent in 1988, the government enforced strict wage controls and dramatic cuts in spending that saw living standards drop drastically over the course of the decade. Overall, per capita income fell at an average rate of 5 percent annually in 1983-'88, while real wages fell between 40 and 50 percent (Lomnitz-Adler 2004:47, cited in Harvey 2005:100). As a result, the labor share of income fell from 35.9 percent in 1982 to 26.6 percent in 1987 (Middlebrook 1989:198-9). This erosion of worker livelihoods fits a broader pattern of class bias in IMF and World Bank structural adjustment programs. Pastor (1987:249) has found statistical evidence for a "strong and consistent pattern of reduction in labor share of income," both in absolute and relative terms, over the course of IMF Standby Agreements and Extended Fund Facilities; findings that have been confirmed by subsequent studies (Garuda 2000; Vreeland 2001). In Mexico, where over half of the population already lived in poverty before the start of the crisis, the purchasing power of the minimum wage fell 66 percent (Robinson 2004:144).

32 "The wealthy have been able to avoid taxation through institutionalized loopholes and weak enforcement, but average wage earners cannot easily escape income tax and have therefore borne the brunt of income tax payments" (Marois 2011:18-19).

While by the mid-1980s it took 4.8 minimum wages for a family of four to meet essential needs, 80 percent of households now had to get by on an income of 2.5 minimum wages or less. As a result, a wave of malnutrition spread among the poor (*ibid.*). World Bank chief economist Stanley Fischer (1989:363) recognized that "most of the burden has been borne by wage earners in the debtor countries." An internal study assessing the World Bank's stated objective of poverty reduction concluded that "poverty issues have seldom featured significantly in such dialogues, and the analysis of structural adjustment programs rarely considered who will carry the heaviest burdens of adjustment" (World Bank 1983).

At the same time, the crisis – as costly as it was for Mexico's poor – turned out to be a boon for the rich. The failed bank nationalization of 1982 had effectively socialized the bankers' liabilities, while the top 10 percent of income earners managed to move between $64 and $80 billion (or more) out of the country by 1988, much of it returning a profit in foreign investments (stocks, bonds, interest and so on). This allowed wealthy Mexican elites to "utilize income from these assets to advantage by transferring funds back into pesos whenever frequent devaluations allowed the elite to maximize its buying power" (Cypher 1990:155). According to one estimate, the interest on capital flight returned to wealthy local elites amounted to roughly 40 percent of total debt payments – private profits that could not be taxed by the Mexican government (Pastor 1989:98). Far from helping to stem capital flight, the IMF actually made matters worse by insisting on capital account liberalization as a precondition for its loans. With wages down, private profits were up across the board, while control over the foreign exchange houses and the anomalous mid-crisis stock market boom provided the rich with ample opportunity for rent-seeking. In the end, the head of UNICEF (1989:11) concluded that "it is hardly too brutal an oversimplification to say that the rich got the loans but the poor got the debts."

Conclusion and Possible Alternative Interpretations

This chapter has presented the evidence in favor of the structural power hypothesis and finds it to be more convincing than the evidence in favor of the traditional explanations revolving around reputation, sanctions or democratic advantage. But what about possible alternative interpretations? The political economy literature offers at least two additional explanations to the ones explored here. An instrumentalist view of business power would suggest that foreign creditors and domestic elites managed to get their way through more traditional political channels like corporate lobbying, revolving doors between business and government and the effective "colonization" of key administrative positions by financial elites. This chapter does not deny that such direct pressure may have played a role; indeed, it has shown how a group of technocrats aligned with foreign creditors and domestic elites managed to occupy important government positions during the crisis. One of the central points of the analysis, however, has been to show that there is more at play than a mere "colonization" of the state apparatus. The bankers' alliance grew in strength precisely because of the state's structural dependence on capital and the elites' own position in the Mexican political economy, marked by their close relations with international creditors.

In a word, the victory of Mexico's bankers' alliance was both cause and consequence of the growing power of the international creditors' cartel. It was a *consequence* in the sense that Mexico's technocrats and elites, by providing a bridge to foreign creditors, were much more capable than the radicals of attracting foreign credit at affordable terms and thereby seeing to the state's structural dependence on capital. This in turn strengthened their hand in internal power struggles within the ruling party PRI. It should therefore be stressed that the bankers' alliance was not powerful because it took over the state; rather it was able to

take over the state *because it was powerful*. At the same time, the rise of the technocrats was a *cause* in the sense that the bankers' ultimate victory under Presidents De la Madrid and Salinas helped to further cement creditor interests and internalize fiscal discipline into the Mexican state apparatus. Again, the point is that there were certain structural forces at play that systematically strengthened the hand of one social group against another. The growing power of the Mexican bankers' alliance cannot simply be reduced to its superior resources or strategies; it rested on the state's structural dependence on credit and the structural constraints imposed by the nature of international lending.

A further interpretation could be derived from the constructivist emphasis on the centrality of norms, narratives, ideas and interpretations. Again, the point of this chapter has not been to deny the importance of such factors. Indeed, the evidence presented above shows very clearly how the norm of debt repayment in the 1980s contrasted sharply to the norm of the 1930s, when the imposition of a unilateral moratorium was still considered "normal and part of the rules of the game" (Ocampo 2013). The chapter has also shown how a particular interpretation of the crisis as a problem of short-term liquidity, combined with a creditor-friendly narrative that placed the blame for the debt crisis squarely on the fiscal profligacy and economic mismanagement of the borrowing governments, was closely connected to the prevailing policy response of short-term fiscal adjustment and case-by-case treatment. The chapter even shows how the orthodox economic ideas of Mexican financial officials became increasingly influential as the crisis deepened, culminating in the rise of an army of US-trained technocrats under President De la Madrid. At one level, this evidence is therefore not incongruent with more constructivist explanations, like the one presented by Teichman (2001), who has convincingly shown that the debt crisis of the 1980s marked a period of dramatic neoliberal transformation across the continent.

The main objective of the chapter, however, has not so much been to explain the rise or role of these norms and ideas, on which we already have a number of very insightful studies, but rather *how they were enforced*. The conclusion is that the neoliberal norm of debt repayment – along with dominant interpretations about the causes of the crisis, hegemonic narratives identifying the blame, and orthodox ideas about the appropriate policy response – were backed by three highly effective disciplinary mechanisms that had the capacity to inflict considerable material costs on the governments that proposed alternative interpretations, pursued different ideas, or transgressed the norm of debt repayment. This shows that, while ideas certainly played a very important role (especially in relation to the internalization of debtor discipline through the third enforcement mechanism), they cannot be divorced from the underlying material interests, social conflicts and power dynamics. This observation appears to be confirmed by the handful of cases where leaders with more heterodox ideas *did* question established norms and neoliberal policy proscriptions. The governments of López Portillo in Mexico, Alfolsín in Argentina and García in Peru were all punished for their non-compliance with dominant norms and ideas. Short-term credit lines were cut off and investors withdrew their capital. The resulting spillovers forced all three of these governments to recant and fall back in line. Ideas were therefore powerful insofar as they stood in relation to specific material interests and structural forces that systematically favored one set of norms and ideas over all others. Those pursuing heterodox alternatives found it more difficult to obtain foreign credit, diminishing the power of their ideas in the process. Pastor (1989:103-104) was right, then, to point out that "none of the more radical proposals – full or partial repudiation, debt service limits, or mobilizing the foreign wealth of local elites – will be adopted without a redistribution of political power." It is for that reason that we now turn to a case in which such a redistribution apparently did take place.

CHAPTER V:

The Great Default

Argentina (1999-'05)

Introduction

On December 23, 2001, Argentina declared a unilateral suspension of payments on over $80 billion in public debt, triggering the largest sovereign default in history. The scale of the default was staggering: as Latin America's biggest debtor, Argentina's bonds made up a quarter of all emerging market debt traded globally (Mortimore and Stanley 2006:16). The outcome constitutes a remarkable contrast to the widespread compliance of the 1980s and poses an interesting puzzle. By the turn of the century, as globalization continued apace, many argued that the power of multinational corporations – and of global finance in particular – was rapidly on the rise (e.g., Friedman 1995; Pauly 1997; Strange 1998; Klein 1999; Hardt and Negri 2000; Stiglitz 2002). Argentina's unilateral default, followed by its coercive restructuring and President Kirchner's rhetorical interventions against foreign creditors and the IMF, seemed to challenge these presumptions. Suddenly the "bond vigilantes" did not appear to be so omnipotent after all: apparently, even a crisis-ridden peripheral country like

Argentina was capable of challenging its foreign creditors and reneging on its debts. For this reason, some scholars have posited the Argentine case as a challenge to the structural power hypothesis. Cooper and Momani (2005:306), for instance, have argued that "the notion of structural discipline sets the 'reach of coercion' at a level that, at least in the Argentine case, failed to match realities ... The power of international creditors' discipline appears to be far more elusive in practice than might be expected."

Such interpretations, however, largely pass over a crucial observation: Argentina's puzzling *over*-compliance in the months and years leading up to the default. Up until late 2001, Argentina was considered a model debtor and largely resembled Mexico in terms of its commitment to repay. In the late 1990s, in particular, the country was widely considered to be an IMF "poster child" and a darling of global capital markets. Presidents Menem (1989-'99) and De la Rúa (1999-'01) stubbornly insisted on full repayment throughout their terms – even when the country entered into stormy waters following contagion from the Mexican peso crisis of 1995, the East-Asian crisis of 1997-'98, the Russian default of 1998 and the Brazilian devaluation of 1999. Between 1999 and 2001 Argentina went into a deep recession that saw unemployment rates climb sharply from 14 percent to over 25 percent. During this time, President De la Rúa steadfastly refused to pursue a default strategy even as his approval rates fell to historic lows and Wall Street, the IMF and the US government actively pressed him to face up to the inevitable and simply restructure the debt. Finally, in December 2001 there was a rupture. After De la Rúa was forced out of office, his interim successor immediately declared a unilateral suspension of all payments.[33] What explains this

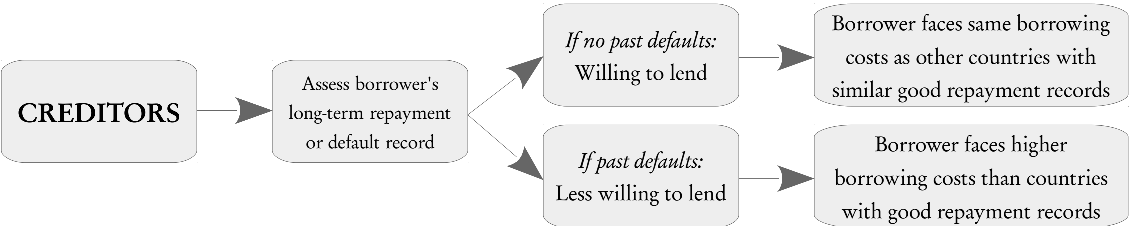
33 This moratorium was upheld by President Duhalde in early 2002 and overcome through a successful debt restructuring by President Kirchner in 2005, which saw 76 percent of bondholders accepting a 75 percent haircut on the value of their old claims. The remaining 24 percent of "holdouts" saw their claims repudiated. When Argentina temporarily re-opened the deal in 2010, participation went up to 91 percent. Some of the remaining holdouts have continued to pursue legal action for full repayment – unsuccessfully so far.

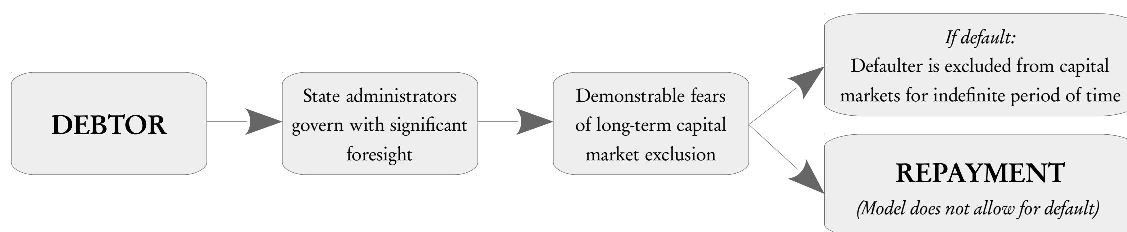
sudden switch from compliance to defiance? Clearly, a full account of Argentina's crisis should be able to explain not only the default itself but also the earlier *refusal* to default; in other words, both the country's over-compliance in the first three years of the crisis and the breakdown of compliance in the final days of 2001. This chapter shows that posing the question this way leads to a very different answer than that reached by critics of the structural power hypothesis. Indeed, rather than challenging this hypothesis, the absence of default in the first three years of the crisis and the process through which it eventually came about actually appear to *confirm* it. Argentina is the exception that proves the rule.

This chapter is structured like the previous one. The first part weighs the evidence in favor of the conventional hypotheses – reputation, sanctions and democratic advantage – and finds the case for them to be unconvincing. The evidence for the spillover costs hypothesis is again more convincing, but it cannot account for the crucial switch from compliance to default. The second part investigates the enforcement mechanisms of the structural power hypothesis and shows how they eventually broke down, leading to default. The third part connects these mechanisms to the outcomes of the crisis, while the conclusion briefly discusses the possible alternative interpretations for the evidence presented.

Reputation Hypothesis

Figure 5.1 – reputational mechanism:





In its original formulation, the reputation hypothesis would lead us to expect no default at all. Because Eaton and Gersovitz presented a static model of reputation, there is no way to properly account for Argentina's switch from compliance to default. But even if we were to relax these theoretical assumptions somewhat and allow for a change in a debtor country's policy preferences, we should still expect investors to recall Argentina's long-standing reputation as a recalcitrant borrower and a "debt intolerant" serial defaulter, which should reduce their willingness to lend (Reinhart, Rogoff and Savastano 2003). The reality was different. As in the 1980s, investors turned out to be remarkably myopic, driven more by "irrational exuberance" and the prospect of short-term profits than by any historically-informed assessment of reputation and risk. By 1997, for instance, in a telling sign of the times, investment banks J.P. Morgan and Merrill Lynch managed to sell some $2 billion in 20-year Argentine bonds in a single month. "Every time we finished a meeting [with investors], the orders would come," Argentine undersecretary of finance Miguel Kiguel recalled. "People were *desperate* to buy Argentina" (cited in Blustein 2005:30-31). Argentina had been the most recalcitrant debtor in the 1980s, yet it managed to quickly re-establish itself as an investor favorite in the 1990s, attracting more credit than any other emerging market. As in previous lending cycles, far from being determined by reputational factors, Argentina's debt dynamics were driven by the eternal ebb and flow of the global credit supply.

Argentine policymakers displayed a similar lack of foresight as their creditors. As in the Mexican case, this study has not found any evidence of Argentine officials being moved

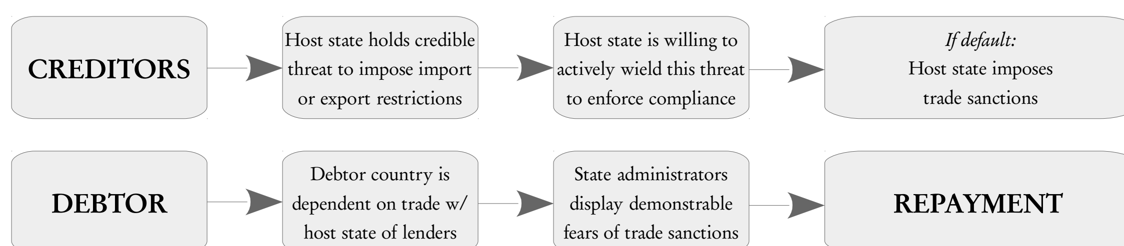
primarily by concerns over their country's long-term access to capital markets. Rather, the Argentine debt strategy hinged exclusively on a desperate attempt to ignore long-term debt dynamics and double down on short-term bets in order to avert the immediate costs of default. Economy Minister Domingo Cavallo, in particular, made a number of decisions that seemed very irrational from the point of view of long-term debt sustainability; but he made them because he feared the *immediate* consequences of default. As Setser and Gelpern (2006:31) have pointed out, "continued support for the status quo reflected a key economic reality: all other policy options carried higher short-term costs than trying to muddle through." Domingo Cavallo himself expressed his concerns that "seeking meaningful debt relief meant losing access to domestic and external credit and *immediately* moving into fiscal and external balance" (Setser and Gelpern 2006:475, emphasis added).

A more important piece of evidence, however, would be the actual consequences of Argentina's default. The reputation hypothesis would lead us to expect complete exclusion from foreign credit after December 2001. We do find that after the default the government briefly lost access to foreign sources of credit. But no sooner than the restructuring deal had been completed in 2005, foreign money started flowing in again (Gelpern 2005:1). Critics of Argentina's default often point out that the country remains locked out of the international capital markets, which – while true – ignores the fact that the country has still been able to raise significant sums of foreign credit through domestic bond auctions. Given the benefits of the commodity boom of the 2000s, the country's phenomenal post-default growth rates, and the vast amount of liquidity flowing through the global financial system, investors were more than happy to take the additional risk of buying locally issued bonds. In the BONAR V and VI auctions, 70 and 80 percent of bonds, respectively, were sold to international investors. Despite the default, demand for Argentine bonds was so strong that in 2005 the

riesgo país – the risk spread compared to US Treasury bills – converged with Brazil's, which did not default on its debts (Datz 2009:470). In fact, as soon as the debt restructuring was completed, the *riesgo país* that had plagued Argentina throughout its crisis returned to the same level it had been at at the peak of the financial euphoria in 1997. Investors were clearly much more myopic than the reputation hypothesis would lead us to expect.[34]

Sanctions Hypothesis

Figure 5.2a – trade mechanism:

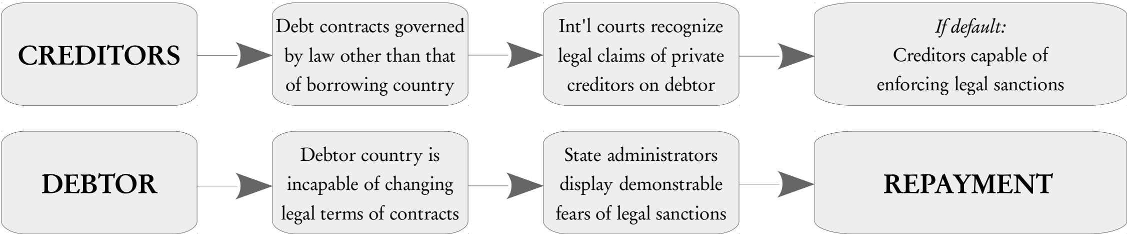


The sanctions hypothesis also does not hold up against the empirical evidence. First, the lenient, even supportive position taken by the Bush administration both in anticipation of and in reaction to the Argentine default shows that there was never any risk of the US imposing trade sanctions in retaliation for Argentina's non-compliance. Insofar as the US government took a stance at all, it actually pushed for default and later pro-actively sided with Kirchner in his wrestling matches with the private creditors and the IMF during the restructuring; a stance that was made possible by the fact that the big US investors had by this point already shed most of their exposure anyway. Helleiner (2005b) has identified a number of reasons – including ideological opposition to the IMF among US officials and

34 "[T]he amount of credit declined dramatically in 2001 and reached a low point in 2005 ... Credit began to flow in again in 2005 and by 2006 reaching the levels of 1994-5. Thus these type of sanctions were of short duration and one can conclude that the evidence shows a myopic view of the default" (Baer *et al.* 2010:13).

arch-conservatives in Congress, as well as geopolitical distractions in the wake of 9/11 and concerns over the emergence of a radical axis from Venezuela to Argentina – that motivated the Bush administration to be supportive of an aggressive Argentine debt restructuring. In sum, Argentina never suffered trade sanctions and this investigation has not uncovered any evidence that De la Rúa's or Kirchner's governments feared such trade sanctions either.

Figure 5.2b – legal mechanism:

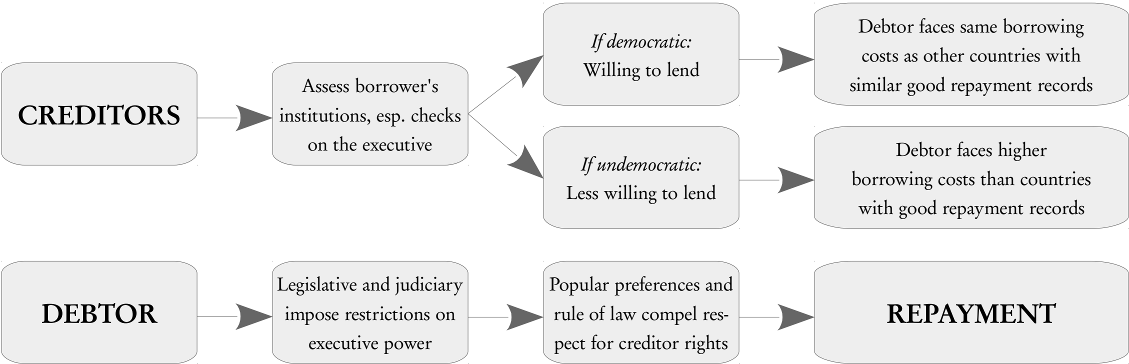


Legal sanctions are a different story altogether. Unlike trade sanctions, legal action has certainly been pursued in response to Argentina's default. But even though hundreds of lawsuits have been brought forth and are still dragging on at the time of writing, creditors have failed to enforce these rulings, while the Kirchners have been content to either ignore or scoff the "vultures" who continue to demand full repayment. A New York judge put it succinctly: "not only have the [lawsuits] not yielded a hundred cents on the dollar, they have not even yielded one cent on the dollar" (cited in Gelpern 2005:4). In the past years there have been a number of high-profile US rulings, including one allowing a subsidiary of Paul Singer's Elliott Management, NML Capital, to briefly attach Argentina's flagship navy vessel *La Libertad* off the coast of Ghana, but the ship was quickly released after the UN Tribunal on the Law of the Sea unanimously upheld its sovereign immunity. More recently, a landmark ruling by Judge Griesa of the US District Court of Southern New York barred Argentina from transferring funds to its exchange bondholders (the ones who did accept the 2005 and 2010 restructuring) if it does not first reach an agreement with the holdouts (the

ones who did not). Nevertheless, the ruling – which has been strongly opposed by Wall Street and the Obama administration – has failed to extract any concessions from President Fernández de Kirchner (outgoing at the time of writing). In July 2014, Argentina tried to make a payment to its exchange bondholders, but its US trustee, the Bank of New York Mellon, was unable to process the transfer as it would have been held in contempt of court. Faced with the false choice to either repay the holdouts in full or defy Judge Griesa and default a second time, Argentina chose the latter. This episode clearly shows that, in the Argentine case at least, legal sanctions have not been an effective enforcement mechanism. While Judge Griesa's ruling has rocked the jurisprudence of sovereign debt – with potentially far-reaching consequences for future debt restructuring deals – it has not been able to reverse Argentina's original default. In fact, it actually triggered another.

Democratic Advantage Hypothesis

Figure 5.3 – institutional mechanism:



What about the role of domestic institutions in securing credible commitment? As we saw in the previous chapter, Schultz and Weingast's democratic advantage hypothesis would lead us to expect a mechanism whereby the institutions of liberal democracy limit the ability of the executive to abrogate its financial contracts: through significant checks and

balances, most importantly a powerful legislative and independent courts. Moreover, we should be able to observe a breakdown of these mechanisms in the switch from compliance to default, with a move towards more authoritarian and less responsive political institutions providing the executive with greater leeway to renounce its contractual obligations. This investigation once again finds the exact opposite to be the case. Argentina complied at a time when democratic checks and balances were rapidly eroding as a result of international financial pressures and precarious economic circumstances; it finally defaulted in response to intense democratic contestation from below. Insofar as political institutions can be said to have played a role in shaping the outcome of the crisis, it was precisely their relatively *un*democratic nature that shielded the executive from popular pressures and that ensured repayment – just as had been the case in the non-democratic Mexico of the 1980s. Unlike in Mexico, however, this lack of responsiveness eventually became politically untenable as the crisis deepened and half the population fell into poverty, giving rise to a deep legitimation crisis and provoking a citizens' revolt that shook the political system to its very core.

The origins of this erosion of democratic responsiveness in Argentina can be traced back to the resolution of the crisis of the 1980s, which had ended with the resignation of President Alfolsín following a bout of hyperinflation and intense riots. When Menem won the elections in 1989, he "soon realised that emergency management of the economy would demand concentration of power in the executive. So he tried and enlarged his authority by means of congressional delegation and by the use of NUDs [necessity and urgency decrees]" (Ferreira Rubio and Goretti 2000:2). At this point, Menem's Justicialist Party controlled both Houses of Congress, most provincial administrations and the Supreme Court. This control over the executive, legislative and judicial branches allowed Menem to decisively abandon the left-Peronist platform on which he had run (which included debt repudiation),

eradicate the national-popular sensibilities of Alfolsín and the Radicals, and carry out an ambitious program of neoliberal reform and privatizations that eventually gained Argentina its status as an IMF poster child. In 1994, coinciding with his embrace of the Washington Consensus, Menem successfully pushed through a constitutional reform that enshrined the NUDs upon which he had increasingly come to rely into law, expanding the discretionary powers of the presidency in the process (Ferreira Rubio and Goretti 1995:89). Before 1994, lawmaking authority had been reserved to Congress, but after the institutionalization of the *decretazo* the executive was able to bypass Congress and create laws by decree, giving the president great "agenda-setting power" and giving rise to a "hyper-presidentialist" regime in which the head of state, according to some scholars, effectively assumed the role of an "elected dictator" (Rose-Ackerman, Desierto and Volosin 2010; Stinga 2009).[35]

Despite the moderate style of his successor, the dynamics of hyper-presidentialism established under Menem further intensified with the onset of the economic crisis after 1999. When De la Rúa re-appointed Menem's old Economy Minister in a desperate bid to restore investor confidence in 2001, "the technocratic Cavallo demanded vast discretionary powers over economic policy, just as he had done under Menem. This only ... reinforced a policymaking process already heavily dependent on executive degrees, marginalized Congress, and devalued the overall process of representation" (Schamis 2002a:87). Rose-Ackerman, Desierto and Volosin (2010:1) stress how "emergency powers, arising from poor economic conditions ... have enhanced presidential power. Presidents seek to enhance their power by taking unilateral actions, especially in times of crisis, and then assert that the constitutional separation of powers is a shield that protects them from scrutiny and that

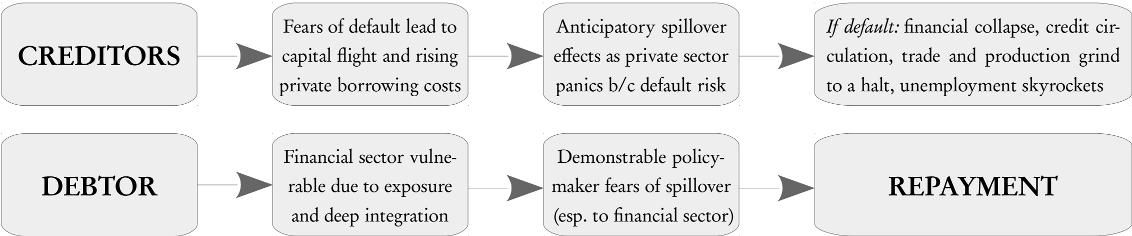
35 Stinga (2009) shows that the use of law-making NUDs (as compared to simple presidential decrees) increased sharply after 1994 to 30% of total decrees issued (up from 13% before 1994). He moreover notes how this "confirm[s] the important role of institutional veto powers exclusively in favor of the President."

undermines others' claims to exercise checks and balances." The authors conclude that in Argentina "presidential power is difficult to control through formal institutional checks." Interestingly, this growing power of the executive and the erosion of democratic checks and balances over the course of the country's neoliberalization seemed to *strengthen* Argentina's credible commitment by insulating economic policy from popular pressures.

As we will see later in this chapter, Argentina only defaulted after a citizens' revolt forced the political establishment to become less subservient to wealthy domestic elites and foreign financial interests and more responsive to the concerns of the general population at home. For this reason, Tomz (2002) categorizes Argentina's moratorium as a "democratic default," emphasizing the widespread public support and voter preference for a unilateral suspension of payments. Noting that "voters may favor noncompliance as the best way to promote the national interest or their personal welfare," Tomz argues that, insofar as those people who stand to benefit from default are represented politically, democratic institutions may actually *increase* the likelihood of non-compliance. Only by shielding economic policy from such popular pressures could investors be convinced of Argentina's commitment to repay. The democratic advantage hypothesis has the world standing on its head.

Spillover Costs Hypothesis

Figure 5.4 – spillover mechanism:



The fourth hypothesis proposed in the literature – spillover costs – once again seems to be the most credible in light of the available evidence. This explanation would lead us to expect three things: first, demonstrable fears among policymakers of the impact of a default on the wider economy and the financial sector in particular; second, early signs of such spillovers when the government approached default, as creditors and investors took fright and anticipated the consequences; third, and most important, the actual materialization of debilitating spillover costs following the default of December 2001. As in the Mexican case, there is elementary evidence for each of these propositions. For one, Cavallo (2002:1-2) was deeply concerned about the averse consequences that even a voluntary debt restructuring would have on the wider economy. The Economy Minister declared that, when he was re-appointed by De la Rúa, "I made it clear that I would by no means join the government to devalue the peso and to declare default on the debt because I considered that such measures would create chaos." Specifying the kind of chaos he expected, Cavallo never mentioned his concerns over Argentina's long-term reputation, the threat of legal or trade sanctions, or the limits imposed upon him by democratic institutions. Rather, he explicitly identified the immediate consequences that default would have on economic performance, emphasizing in particular the transmission belt of the country's fragile and over-leveraged financial system: "defaulting on loan repayments would temporarily ease the burden of public debt interests on budgets; however, it would automatically bring about the collapse of the financial system, cause the destruction of pension funds, and adversely affect savers and workers, because over 50 per cent of the bonds issued by the national state and the provincial governments represented the assets of those institutions" (Cavallo 2002:2).

The health of the financial sector thus became the primary concern of government. In his authoritative investigative account of the crisis, Blustein (2005:168) confirms this:

"more worrisome than litigation ... was the concern about the banking system." Cavallo's chief economic advisor, Guillermo Mondino, pointed out that "the population was very much aware of the exposure the banks had to government securities," and hence even the slightest hint of a default would risk triggering a potentially catastrophic bank run (*ibid.*). In November 2001, with the government failing to allay the fears of ordinary Argentinians and the country inching ever closer to default, signs of anticipatory spillover effects openly manifested themselves as a slow-motion bank run that had been brewing for several months escalated into a full-blown financial panic. Worried that an impending default would lead to a collapse of the banking system and that a breakdown of the convertibility regime and a subsequent currency devaluation would eat up their peso-denominated savings, depositors began to withdraw over $1 billion per day, rapidly eroding the banks' deposits (Rambarran 2004:6-7). This came on top of the $10 billion that had already fled the country in the wake of an earlier debt rescheduling in June that year.

When Argentina finally defaulted, the traumatic consequences largely confirmed the fears of policymakers and the general public – but they nevertheless turned out to be short-lived. The default almost immediately led to a breakdown of the convertibility regime and a subsequent devaluation of 30 percent, followed by a government-declared "pesification" of domestic deposits. After the abandonment of its fixed exchange rate with the dollar, the peso began to slide and was to lose 300 percent of its value (Levitsky and Murillo 2003:155). Foreign investors and international financial institutions immediately withheld all further credit and refused to lend to Argentina unless it agreed to "negotiate in good faith" with its private creditors for an orderly restructuring of the defaulted debt – something that was politically unpalatable in the social environment that had given rise to the default. And so, with both private investors and the IMF refusing to lend more money, the government was

effectively cut off from foreign credit (Lewis 2009:147). The domestic banking system froze up and the economy fell into a deep depression.

As the interbank payment system ground to a halt, firms could no longer access the financing they needed to sustain their everyday activities. Sales dropped by 40 percent and over 100.000 companies went bankrupt, leading to at least 280.000 layoffs (Lewis 2009:146). In the first quarter of 2002, Argentina's GDP contracted by 16 percent and manufacturing output by 20 percent, while a classic investor strike undermined any hopes of an immediate recovery. The rate of investment to GDP, which had stood at an already relatively low 19.1 percent in 1999, fell to 11.3 percent (Baer, Margot and Montes-Rojas 2010:8). Meanwhile, firms struggled to obtain export credits – a troubling development about which Foreign Minister Carlos Ruckauf and Enrique Mantilla, head of Argentina's Chamber of Exports, as well as the World Bank explicitly expressed their concern (Weisbrot and Cibils 2002:4; Cibils, Weisbrot and Kar 2002:20). The ongoing bank run also intensified after a much-maligned limit on deposit withdrawals – the *corralito*, which had been one of the immediate triggers for the December uprising – was lifted. Total bank deposits collapsed from $70 billion at the start of 2002 to a mere $2.9 billion by October. With their capital base rapidly depleting, the banks closed 210 branches and fired 9,500 workers (Lewis 2009:145-6).

The social consequences were devastating. Unemployment hit 25 percent, the share of the population living in poverty reached 57.5 percent and extreme poverty doubled to 27 percent (Grugel and Riggirozzi 2007:10). Klein (2004:4) wrote that, when he took power in early 2002, “the Argentine economy threatened to disintegrate before Duhalde's eyes.” The dramatic collapse in output was the worst to hit any capitalist economy since World War II (Llach 2004). In a country that less than a century ago had ranked among the ten richest in

the world, one in four citizens now "could no longer afford sufficient food" (Rock 2002:56). Still, the economic trauma quickly subsided once Argentina returned to very high levels of growth in 2003; an observation that is in line with the spillover costs hypothesis, which stresses the *short-term* consequences of default on the financial system and its dramatic knock-on effects on overall economic performance.

Still, the spillover costs hypothesis fails to explain why Argentina suddenly switched from repayment to default. If it was really the prospect of economic collapse that forced De la Rúa's government to comply, why did the same prospect not also bind its successors? To understand Argentina's dramatic shift in policy preference, we need to take into account a number of changes in the power dynamics and political conflicts at the heart of the crisis. By focusing on the way in which the enforcement mechanisms that compelled De la Rúa to repay gradually "broke down" over the course of 2001, the structural power hypothesis is capable of providing a more dynamic account of Argentina's policy preferences and a more faithful interpretation of the actual outcome of the crisis – which, as we will see, once again saw global finance turn an economic catastrophe decisively in its favor.

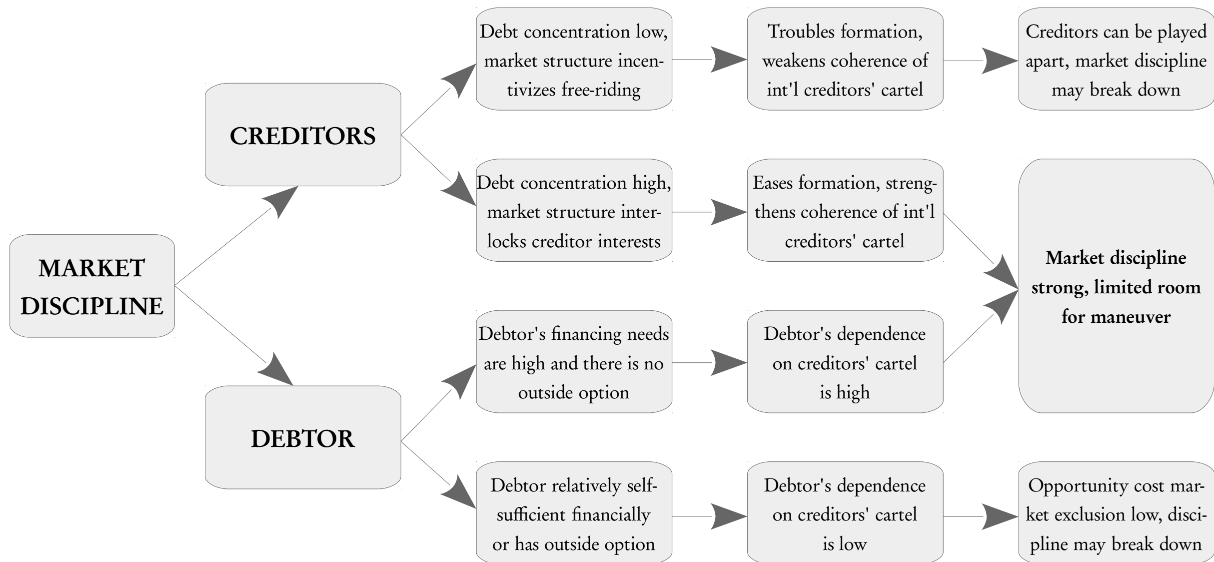
Enforcement Mechanisms

As has been stressed before, a proper explanation of Argentina's default should be able to account both for the government's remarkable compliance in the first years of the crisis *and* for its equally remarkable defiance in the wake of the events of December 2001. In this respect, we can observe a number of important contrasts with the crisis of the 1980s. Again, three stand out in particular. First, at the level of international lending, the return of bond finance in the 1990s made it possible for the big institutional investors to sell their

bonds on secondary markets and thus reduce their overall exposure. In practice, the effect was to disperse the holdings of Argentine bonds among a large group of small investors – mostly pensioners in Europe and Japan – who failed to hold together a creditors' cartel in the way that the US investment banks and institutional investors had. Second, at the level of the international lender of last resort, the IMF had overextended itself in the crises of the 1990s, unleashing a wave of criticism from across the political spectrum. Heavily over-exposed to developing country debt and with the Republicans in US Congress refusing to replenish its reserves, the IMF found itself less capable of enforcing policy conditionality and eventually withdrew its financial support altogether. Third, unlike in Mexico in the 1980s, the decreasing responsiveness of political institutions to popular concerns led to a proliferation of contestation in the streets. While Argentina's bankers' alliance – referred to as the *patria financiera* – was strengthened from above as a result of the state's growing dependence on foreign credit, it was simultaneously weakened from below as popular opposition to austerity and repayment manifested itself in the form of a deep crisis of representation. This crisis gave rise to mass protests that eventually culminated into a popular uprising, ousting the *patria financiera* from office and forcing the Peronist establishment to make sweeping concessions to the population at large, the first of which was a unilateral suspension of payments. In sum, the evidence suggests that the hypothesized enforcement mechanisms – while initially fully operative – eventually broke down, opening a window of opportunity that, with a decisive push from below, finally tipped Argentina into default.

The Return to Bond Finance and the Collective Action Problem

Figure 5.5 – market discipline mechanism:



The conclusion of the Brady deal in the early 1990s led to a crucial change in the structure of international lending, marking the end of the syndicated bank loans of the 1970s and 1980s and giving rise to the return of bond finance. This in turn had important consequences for the ability of creditors to organize collective action amongst themselves. While syndicated bank lending had interlocked creditor interests and eased the internal coordination of a unified international creditors' cartel, bond finance rests heavily on secondary markets, which tend to disperse holdings among a wider and more diverse range of small investors. As we already saw with respect to the crisis of the 1930s, the incapacity of geographically scattered bondholders to act monolithically in threatening to withhold short-term credit tends to lead to a breakdown of market discipline. Anne Krueger, IMF Deputy Managing Director during the Argentine crisis, observed a clear contrast between the "generally orderly" crisis management of the 1980s and the chaotic and unpredictable crises of the 1990s and 2000s, in which investors "were increasingly numerous, anonymous, and difficult to coordinate" (cited in Cooper and Momani 2005:316).

The return to bond finance, however, does raise an important puzzle. If creditors are really more difficult to coordinate in a lending structure based on bond finance than in a structure based on syndicated lending, then why did the deep crises of the 1990s not lead to more widespread default? During the peso crisis of 1995 and the East-Asian financial crisis of 1997-'98, debtor countries and international financial institutions gained notoriety for their orthodox policy responses, and we have already seen that Argentina itself was very subservient in its first crisis years. What explains this compliance under bond finance? The answer, this investigation suggests, lies in the *ownership structure* of the debt, and specifically the high concentration of Argentina's bonds in the first phase of the crisis. When holdings are highly concentrated in a number of systemically important financial institutions in the dominant creditor country, in this case the US, these institutional bondholders – assisted by the international lender of last resort and financial authorities in their host country – will tend to take the lead in forming an international creditors' cartel to prevent default, thereby helping to overcome the collective action problem that would otherwise have plagued small and decentralized bondholders. Highly concentrated bond finance in this respect resembles syndicated bank lending; the major difference being that bonds can be sold on secondary markets, providing institutional investors with an exit option and the ability to reduce their exposure in anticipation of default. This is exactly what appears to have happened in the Argentine case. As long as Argentina's debt remained highly concentrated and institutional investors and Wall Street investment banks stood to gain from repeated debt rescheduling arrangements, the bondholders did not encounter any difficulties in maintaining a coherent international creditors' cartel. The very moment this creditors' cartel began to shed its holdings in order to reduce its exposure, dumping the bonds on hundreds of thousands of scattered small retail investors in Europe, market discipline quickly broke down.

The decisive turning point, in this respect, was an obscure rescheduling arrangement agreed to by Cavallo in mid-2001. In May that year, Crédit Suisse-First Boston and seven other international banks had joined together in a consortium and had taken the initiative to sell the Economy Minister a notorious scheme that became known as the *mega-canje*, or "mega-swap." The deal would exchange old maturing bonds with new ones carrying much higher interest rates, so as to effectively wipe out $15 billion in payments falling due in 2001 and push the moment of reckoning back until after the next presidential elections. While the deal bought Cavallo much-needed time, it provided US institutional investors with a unique opportunity to shed their exposure to risky Argentine bonds. The result was a dramatic change in creditor composition (debt ownership structure), the importance of which is difficult to overstate. As Economy Minister under Menem in the 1990s, Cavallo had dealt with a small group of Wall Street investment banks – brokerage firms like Goldman Sachs, Morgan Stanley and Crédit Suisse-First Boston – which had acted as intermediaries between Argentina and the buyers of its bonds, mostly large pension funds and mutual funds in the United States. As the Menem era drew to a close, however, and as the first signs of crisis became apparent, US institutional investors became increasingly wary of holding Argentine debt, so the big Wall Street investment banks "turned to Europe, where regulations protecting small investors were less strict" (Lewis 2009:133). In countries like Italy and Germany, small investors bought stocks and bonds through their local banks or pension funds. Since European pension funds could not afford the kind of large and well-trained research units that steered the investment decisions of the wealthy US funds, they were easily tricked into purchasing risky Argentine bonds and selling them on to unsuspecting small savers and pensioners. In the process, the risk of default was "atomized" and dispersed overseas.

As a result of this process, hundreds of thousands of small savers, including some 400,000 Italians, ended up holding over $24 billion in claims on an all but bankrupt foreign government. According to an emerging market bond manager, “that's what kept Argentina going. Those poor suckers didn't have a clue as to what they were buying” (cited in Lewis 2009:133). The mega-swap allowed the Wall Street investment banks to dump Argentina's worthless bonds onto a dispersed panoply of unsuspecting European retail investors, while setting Argentina up with an ever growing long-term debt load. Blustein (2005:125) argues that the swap “ranks among the most infamous deals that Wall Street has ever peddled to a government – and with good reason: for [Crédit Suisse-First Boston] and a half dozen other Wall Street firms, the megaswap would be a bonanza ... For Argentina, it would be a bust, rendering the country's solvency even more questionable than it was already.” At the same time, by dispersing Argentina's creditors, the swap had very negative consequences for the ability of the new bondholders to maintain a unified creditors' cartel as the banks had.

The breakdown of the international creditors' cartel – or rather, the existing cartel's success in passing on the risks and losses of a future default to a less organized third party – in turn helped to disarm the enforcement mechanism of market discipline that had been so effective in the 1980s and 1990s and that had, up to that point, served to enforce the compliance of the De la Rúa government. After the mega-swap, however, Argentina was for all practical purposes excluded from international capital markets. The institutional investors refused to extend further credit unless there was a debt restructuring to make Argentina's debts sustainable again. The big US investment banks – knowing that a default was coming – started hedging their bets. By September 2001, it was clear that the government had “all but lost access to credit markets,” bringing the country “to the brink of default” (Rambarran 2004:6). With its exposure greatly reduced and the risk of contagion effectively defused,

Wall Street saw the dark clouds gathering on the horizon and dramatically changed tack, suddenly embracing the inevitability of an Argentine default.

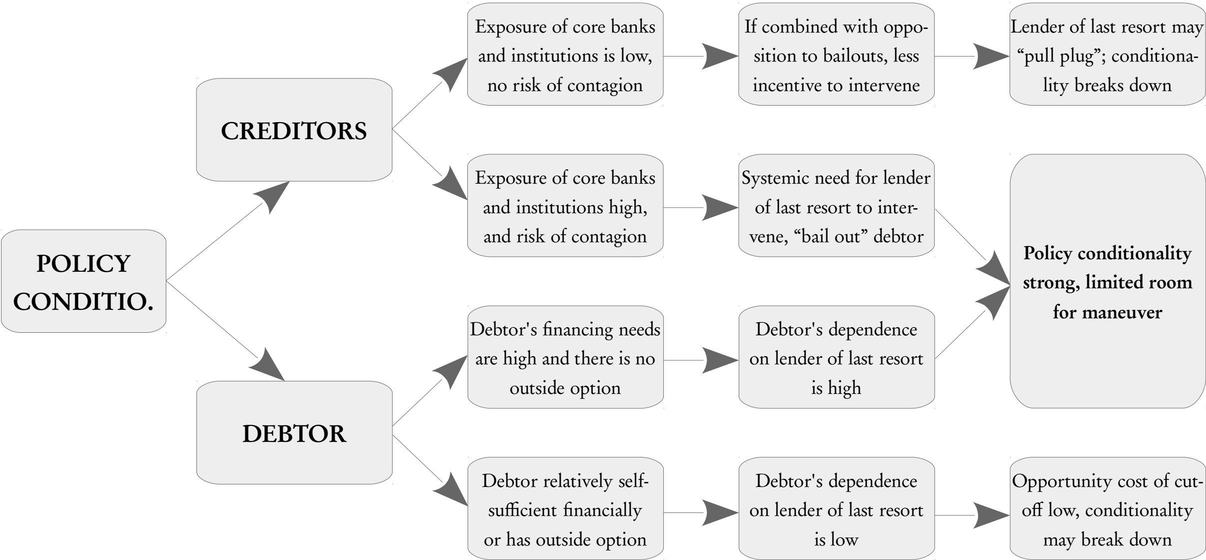
In October 2001, a meeting took place between IMF Managing Director Horst Köhler and the senior executives from some of the biggest US-based investment banks and institutional investors, including J.P. Morgan, Goldman Sachs, Citigroup, Crédit Suisse-First Boston and AIG. According to Lewis (2009:157), the bankers assembled at the meeting concluded that "Argentina was going to collapse and that nothing could be done to save it. A default was inevitable, and the best that the creditors could do would be to approve a restructuring under which they would voluntarily accept less than the face value of their claims." As Blustein (2005:162) emphasizes, "this was a remarkable moment. The major creditors of a country were effectively saying that the government should pay them less than they were owed, on involuntary terms." But while the bankers' position may seem puzzling at first sight, their dogged insistence on the necessity of a default had little to do with altruism. Rather, they were hoping to restore Argentina's creditworthiness, keep the country in the lending game, and thus allow its government to come crawling back to the banks for further high interest loans. The losses from a haircut, even a large and involuntary one, would be bearable as most of the costs had already been passed on anyway.

The Weakening of the IMF and Policy Conditionality

A second major observation in the Argentine case relates to the role of the IMF, which had been so crucial in cementing the creditors' cartel and preventing default in the 1980s. Together with the US Treasury, the Fund played an even more important role in the crises of the late 1990s. Echoing the main lessons from the last Latin American debt crisis,

Cibils, Weisbrot and Kar (2002:6) noted that "the role of the IMF is important, not so much because of its own resources or expertise, but because of its power – together with the US Treasury Department – as head of a creditors' cartel that can deny Argentina access to sources of credit." Why, then, did the Fund not manage to prevent Argentina's default in 2001? Was it unable to prevent it? Or did it not want to? The answer is probably a combination of both.

Figure 5.6 – policy conditionality mechanism:



First, at the turn of the century the IMF was severely weakened, having dramatically overextended itself in the East-Asian crisis of 1997-'98 and facing scathing criticism – and growing opposition – from across the political spectrum in response (Bhagwati 1998; Wade and Veneroso 1998; Stiglitz 2002; Eichengreen 2005; Johnson and Kwak 2010). Second, after the (non-)election of George W. Bush, the US government grew increasingly hostile to the type of international bailouts pursued by the Clinton administration, especially in light of the reduction of US bank exposure to Argentine bonds discussed in the previous section. The first point led to a growing *inability* of the IMF in the period leading up to mid-2001 to

compel De la Rúa to stick to his fiscal targets. The second led to a growing *unwillingness* among the IMF's main sponsors in Congress and the White House to keep Argentina afloat in the face of a default that was now widely considered to be inevitable anyway. The two conspired in November 2001 to lead to the withholding of a critical IMF credit tranche on grounds that Argentina had failed to live up to the conditions of its Standby Agreement. The severing of the Fund's official credit line set in motion a sequence of events that three weeks later finally led to default.

The IMF's approach to Argentina thus underwent a change at least as dramatic as – and very much in line with – the change in debt concentration and creditor composition addressed in the previous section. We can identify three distinct phases in this respect. The first, which covered Menem's presidency from 1989 until 1999, was marked by very close and cooperative relations between Argentina and the Fund. Throughout the 1990s, the international financial community enthusiastically sponsored the neoliberal agenda pursued by Menem and Cavallo, which "matched perfectly with the reigning economic ideology" of the IMF, World Bank and US Treasury (Lewis 2009:56). As late as 1998, Menem was invited to address the IMF annual meeting in Washington, D.C. to share his views on responsible financial management. At this point, the representatives of Argentina's *patria financiera* resembled the technocratic allies of Mexico's bankers' alliance of the 1980s, working closely with US and IMF officials to establish "a high degree of agreement on the economic policies to be implemented" (Cibils and LoVuolo 2012:755). In the late 1990s, the IMF's Managing Director Michel Camdessus exclaimed that "in many respects the experience of Argentina in recent years has been exemplary ... clearly, Argentina has a story to tell the world: a story which is about the importance of fiscal discipline, of structural change, and of monetary policy rigorously maintained" (cited in Blustein 2005:58).

The second phase, which covered the first part of De la Rúa's presidency and the lame duck phase of the Clinton administration, was marked by continued attempts to stave off an Argentine default but at the same time also by the waning influence of the IMF and its growing inability to enforce policy conditionality on the Argentine government. In the US, conservative opposition to international bailouts gathered steam in the wake of the unprecedented US-led rescue operations in Mexico, East Asia, Russia and Brazil. From 1998 onwards, influential voices were going up for the abolition of the Fund and the Clinton administration struggled to convince Congress to replenish its reserves. As a result, the IMF became severely over-exposed to emerging market debt, with Turkey, Brazil and Argentina accounting for 73 percent of its outstanding liabilities at the end of the decade (Cooper and Momani 2005:313). By 2001, the Fund's reserves of $8.7 billion paled in comparison to the $16 billion in exposure it had to Argentina alone (Helleiner 2005b:963). All of this gave the IMF significantly less leverage over the Argentine government than it had had with respect to the Latin American debtors of the 1980s and the East Asian governments in the 1990s.

In this phase, the IMF nevertheless remained determined to avoid default. Setser and Gelpern (2006:474) write that "Cavallo's core accomplishment [as Economy Minister] was to draw on his considerable reputation to secure a series of additional injections of IMF liquidity to finance what turned out to be a classic gamble for resurrection." The IMF disbursed several of the largest augmentations in IMF history, but even this failed to stem the investor stampede for the exits. Meanwhile, IMF managers, who had not been informed about the mega-swap, grew increasingly frustrated with President De la Rúa. Cooper and Momani (2005:308) write that relations between Argentina and the IMF "soured during this time as the Fund watched Argentina continue to announce policies that the IMF deemed 'misguided', although these initiatives were overtly approved out of fear of a systemic col-

lapse." As late as September, the IMF came to the rescue again by adding another $8 billion lifeline to its Standby Agreement from the previous year; the third such augmentation in less than a year, bringing the total of extra credit to $22 billion. There is a broad consensus, including among the IMF's economists, that these loan extensions constituted "the most contentious decisions regarding the IMF's involvement in the Argentine crisis" (e.g. Mussa 2002). Not only did the augmentations triple the Fund's exposure to Argentina and turn the IMF into the country's single biggest creditor, but they were also held responsible by IMF economists for "delaying the inevitable, postponing the default and amplifying the dislocation caused by the crisis" (Cassou, Erce-Domínguez and Vázquez-Zamora 2008:16).

This period of muddling through finally gave way to the third phase, which covered the first years of the Bush administration and the final months of De la Rúa's presidency. At this point, Washington's pent-up frustrations with Argentina turned to outright, full-blown hostility. First, as the economic performance of its former poster child grew from bad to worse, the IMF notably shifted its narrative. Whereas it had previously praised the fiscal discipline of the profligate Menem, it now began to blame the relatively compliant technocrat De la Rúa for his fiscal ineptitude. This in turn reflected a change at the helm of the IMF and the US Treasury. When the Mexican, East-Asian, Russian and Brazilian crises struck during the Clinton administration in the 1990s, the Treasury and the IMF had prioritized emergency lending over all other priorities. However, from Clinton's last Treasury Secretary Larry Summers on, the United States' financial leadership position was gradually undermined from within by conservative forces. In 1998, Republicans lawmakers had put up stiff resistance to a proposed $18 billion increase in IMF reserves to protest against Clinton's Asian bailouts. The increase eventually passed under the condition that Congress establish a commission to review the IMF's role in international crisis management. This

gave rise to the Meltzer commission, chaired by free-market economist Allan Meltzer, an influential advocate for the abolition of the Fund (Helleiner 2005b:362). In its final report, the commission urged a radical downsizing of IMF activities. Faced with this increasingly isolationist climate, it is no surprise that Bush's response to the Argentine crisis amounted to little more than "a placeholder with relatively modest upfront financial commitments that deferred hard decisions" (Setser and Gelpern 2006:474).

After the Bush administration took office in January 2001 and a new management took over at the Treasury and IMF, the international stance hardened. The new Treasury Secretary, Paul O'Neill, expressed his opposition to further international bailouts while his undersecretary for international affairs John Taylor even advocated abolishing the IMF altogether (Blustein 2005:117). Bush's chief economic advisor, Lawrence Lindsey, was also on record for his staunch free-market convictions; views that weighed heavily on the administration's response to the Argentine crisis, which on the one hand became ever more *laissez-faire* in its approach to emergency lending and on the other much tougher in terms of the conditionality it imposed on the debtor (Cibils, Weisbrot and Kar 2002; Helleiner 2005b). Corrales (2002:35) writes that "the first sign of hard-line posturing came when Secretary of the Treasury O'Neill, shortly after taking office in 2001, chided Argentina publicly for getting in trouble because it never did its homework, essentially ignoring Argentina's reform record of the past decade and the role of external crises."

Moreover, by mid-2001 – following the mega-swap discussed above – the Fund had decided that "the fire in Argentina would not spread, mostly because bondholders had protected themselves (more specifically, most major U.S. bondholders had already sold much of their Argentine debt)" (Corrales 2002:35-36). Carmen Reinhart, the Fund's deputy chief

economist, tried to ease the contagion fears of her colleagues by reassuring them that an Argentine default would probably have only limited repercussions. As she co-wrote in a staff memo of the IMF research department on August 15, "a 'credit event' in Argentina is widely anticipated and has been (partly) discounted by the markets for some time. The possibility that a default by Argentina triggers a sharp reversal of capital flows to other countries in South America is therefore relatively small" (cited in Blustein 2005:142). Another internal IMF report showed that, while a few Spanish banks might take a hit, the risk of contagion and the overall threat posed to the international financial system were low (Blustein 2005:175). At the same time, drawing on its experience with devaluations in East Asia, the IMF had become convinced that Argentina's inflexible exchange rate had to go, which would in turn require a restructuring of the debt. None of this meant that Argentina would be granted any leeway though: as the American stance hardened, loan conditionality was further ramped up (Corrales 2002:36).

By now, influential economic commentators and leading figures in the US financial establishment had already been openly expressing the need of a default for quite some time. Back in March 2001, Columbia economist Charles Calomiris and a group of Wall Street bankers had proposed that "Argentina declare itself bankrupt, request debt forgiveness, and start over with new policies intended to reward creditors only if its economy improved" (Wucker 2003:50). Calomiris was by no means a left-wing populist or Jubilee campaigner. Well-known in conservative circles as a long-time champion of financial deregulation who kept the interests of Wall Street close at heart, he was convinced that there was only one way to keep Argentina in the lending game: by writing off a significant chunk of the debt. It has been noted that "devaluation and default were openly discussed (particularly in financial and academic settings in the United States) and there was a widespread opinion that the

debt and the convertibility regime were not sustainable" (Damill, Frenkel and Rapetti 2005: 74). With the IMF itself heavily over-exposed, Horst Köhler, the Fund's new chief, began to investigate the possibility of private sector involvement in the burden sharing. Blustein (2005:98) notes that Köhler "raised the possibility that the IMF and the Argentine authorities should consider something like Calomiris's 'haircut' proposal for forcing creditors to accept reduced payment of their claims." And so the IMF actively began to prepare default scenarios, a so-called 'Plan Gamma', as a possible resolution to the crisis.

In April 2001, Calomiris went public with his default proposal in a *Wall Street Journal* article entitled 'Argentina Can't Pay What It Owes'. In the piece, he specifically argued that most US institutional investors had already sold off their Argentine bonds and therefore US policymakers did not need to fear a default. Calomiris highlighted the fact that "U.S. institutions are already 'underweight' on Argentine debt," and pointed out that while Argentina accounted for some 25 percent of emerging market bonds in circulation worldwide, it only made up 10-15 percent of the portfolios of the large US-based mutual funds and pension funds (note that this was *before* the mega-swap; these ratios were even further reduced as institutional investors offloaded their Argentine bonds in the swap). The opinion piece elicited a strong rebuke from Cavallo, who shot back that "I have thought a lot as to why honest people may dare to write a recommendation as to how Argentina may default. Who could conceive such a destructive idea for a country, and be bold enough to propose it? ... There is a complete misunderstanding (almost omission) of the costs that a compulsory restructuring of our debt would have" (cited in Blustein 2005:122).

By October 2001, Schamis (2002a:87) writes, "it was obvious to most analysts that Argentina would have to default on its debt, but Cavallo – some said with an eye on his ties

to Wall Street – stubbornly refused to admit it." The perceived inevitability of default, however, was already turning into a self-fulfilling prophecy. On December 5, the IMF dryly announced that it would be withholding its next $1.24 billion loan installment out of frustration with the government's failure to keep its budget under control. With the lender of last resort simply pulling the plug on its financial life-support, there was very little the Argentine government could do to prevent the downward spiral that, three weeks later, would force the country to declare the largest unilateral default in world history.

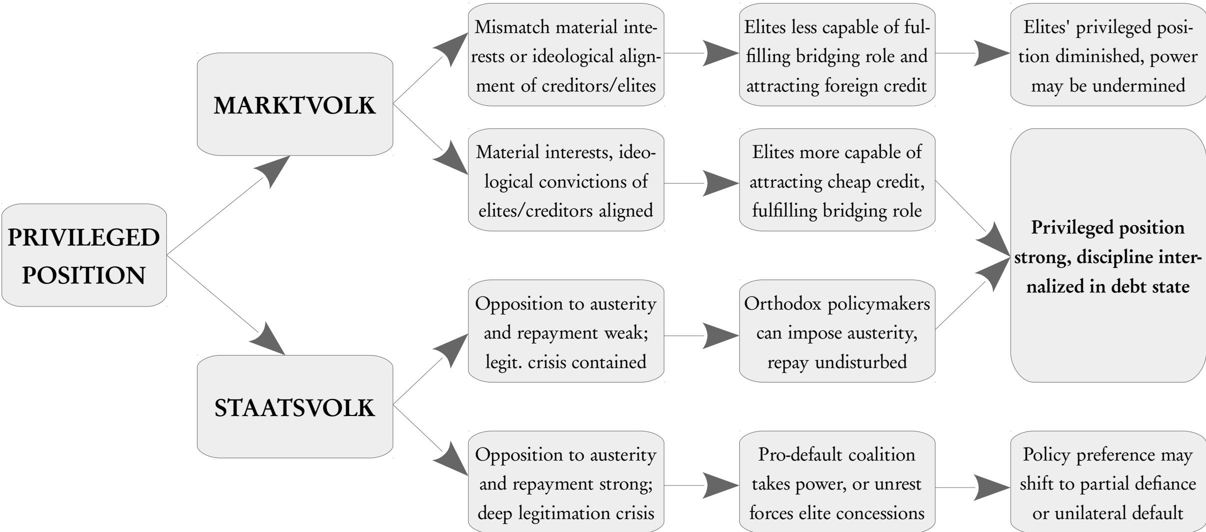
In a final act of desperation, Cavallo seized the country's pension funds and transferred the contents to the Treasury, allowing the government to keep paying its bills and to once more extend the moment of reckoning. In a meeting with IMF officials on December 7, when it was clear to everyone involved that Argentina had no other option but to declare a default and exit the convertibility regime, Cavallo refused to even discuss the option with Fund officials (Setser and Gelpern 2006:475). And so the US simply kept pushing Argentina further towards the cliff. "As if the message was not clear enough," Cavallo later fumed in indignation, "Allan Meltzer visited Buenos Aires to tell [opposition leader] Eduardo Duhalde and most of the senators that the debt restructuring process which the Argentinian government was engaged in would not generate enough of a haircut and Argentina should simply default on all its debt" (Cavallo 2004:147). Cavallo and De la Rúa would have none of it. In one of the most remarkable cases of over-compliance in recent financial history, the two men continued to defy their foreign creditors precisely by *not* defaulting.

If the entire international financial community was now pushing for Argentina to suspend its payments, why did the country's leaders not just get it over with and default? What drove De la Rúa and Cavallo to repay, and what were the final factors that eventually

brought about the inevitable default? So far, we have explored the gradual breakdown of the *international* enforcement mechanisms; to answer the above questions we will now need to look at the important political and social changes that took place inside Argentina itself.

The Rise and Fall of the Patria Financiera

Figure 5.7 – privileged position mechanism:



As in Mexico, the Argentine political economy underwent a major transformation in the last three decades of the twentieth century. In the 1970s, the most important political cleavage had been the split between the left-wing and right-wing of the Peronist movement. The former advocated a *patria socialista*, a socialist homeland, while the latter advocated a nationalist and corporatist *patria Peronista*. The military coup of 1976 dramatically changed this situation. Like in Chile, the left was brutally persecuted as the *junta* began to liberalize the economy. The result was increasing state dependence on private credit and investment and the growing indebtedness of government, firms and individual households to private banks. Schamis (2002b:129) writes that "Argentines came up with the term *patria financiera* to refer to the main beneficiary of the liberalization process." While this *patria financiera*

was by no means as deeply rooted as Mexico's bankers' alliance (it lacked the organizational and structural ties to domestic industrialists), it nevertheless grew increasingly influential in the debt crisis of the 1980s and finally reached its apogee under Menem and Cavallo in the 1990s. When the crisis of 1999 struck and the state's dependence on foreign credit grew ever more acute, the political allies of the *patria financiera* – who shared creditors' interest and belief in stabilization, privatization, liberalization, deep integration and the "sound money" guaranteed by peso-dollar convertibility – effectively monopolized economic policymaking, especially in the wake of the reappointment of Domingo Cavallo. In this sense, Argentina resembled Mexico in the first years of its crisis.

Unlike in Mexico, however, the rise of the *patria financiera* and Cavallo's policy response to the crisis did not go uncontested. While the labor unions had been largely co-opted by the Peronist establishment and did not put up a very strong resistance, there was significant popular pressure from below to reverse painful austerity measures and fight sky-rocketing poverty and unemployment. As we will see in this section, the rise of the *patria financiera* thus corresponded closely to the growing dependence of the state on credit, while its fall was a direct result of both the cutting off of foreign financial support (discussed above) and the deepening crisis of representation that grabbed a hold of Argentine society in 2001, as the state's failure to see to its accumulation function increasingly undermined its legitimization function. As a result, the crisis led to a complete loss of public trust in the political establishment and the post-*junta* order, culminating into an uprising in December 2001 that forced out De la Rúa and Menem, finally leading to Argentina's historic default.

Just as in Mexico, the crisis started out with two conflicting positions on the debt question. Unlike in Mexico, these conflicting positions could be openly expressed in free

democratic elections, with the Peronist candidate Eduardo Duhalde of the Justicialist Party openly calling for default in his 1999 campaign and Fernando De la Rúa, who ran on the ticket of the 'Alliance' between his centrist Radical Party and the center-left Frepaso, pledging "to pay the debt under all circumstances" (cited in Schamis 2002a:82). However, as international financial pressures grew stronger in the wake of the elections, the victorious De la Rúa found himself stuck between a rock and a hard place. On the one hand, the markets and IMF demanded far-reaching austerity, while on the other popular opposition to such measures was growing stronger. As Argentina entered into a vicious cycle of rising risk premiums, deeper budget cuts, a worsening economic downturn and widening social unrest, there seemed to be little the President could do to rectify the situation: pleasing investors deeply angered voters, and pleasing voters scared away investors. Still, investors clearly had the upper hand, eroding De la Rúa's standing at home. By 2000, even fellow party members began to openly air their opposition to the president's policies; De la Rúa's predecessor and party leader Raúl Alfolsín, for instance, lambasted the president for his orthodoxy and called for a debt moratorium.

Increasingly incapable of sticking to the IMF's fiscal targets and desperate to strengthen his weakening grip on power in the wake of a corruption scandal that had left him politically isolated, De la Rúa decided to replace his Economy Minister with Ricardo López Murphy, a fiscal hawk and former IMF economist who he hoped could help restore private sector confidence. But when the $4.45 billion austerity package he announced upon taking office triggered violent student protests, 'The Bulldog', as López Murphy was known to the media, was forced to retreat with his tail between his legs. As a result, research staff at the IMF rapidly lost faith in Argentina's ability to pay its debt (Cooper and Momani 2005:308). Chief economist Michael Mussa believed López Murphy was the only one who could have

credibly reigned in government spending – and he had just been mowed down by popular protest (Mussa 2002). Meanwhile, as wealthy citizens started withdrawing or expatriating their savings and a slow-motion bank run quietly gained pace, it began to dawn on more and more people that "default was only a matter of time" (Lewis 2009:130). But De la Rúa, determined to avoid that outcome, continued to gamble for resurrection and pledged once more that he would honor Argentina's obligations in full. To add force to that pledge, the president did something remarkable: he turned to his political opponent Domingo Cavallo, against whom he had squared off in the presidential elections of 1999, and reappointed the former Economy Minister back to the position he had held under President Menem.

The economic motivations behind Cavallo's appointment were clear. With his close ties to domestic and international investors as well as the US government and the IMF, "the Wizard", as Cavallo was known, was the man deemed most capable of providing a bridging role towards foreign creditors. In fact, Cavallo was so loved by investors that, when Menem had announced on January 29, 1991 that he would be appointing him as Economy Minister the first time around, the Buenos Aires stock exchange instantly shot up 30 percent in a single day (Blustein 2005:13; Rock 2002). As Schamis (2002a:87) noted, the main reason De la Rúa now reinstated his one-time rival was because "he was hoping thereby to gather political support from economic and financial elites, as well as to put in place a man whom he could trust to attack the deficit aggressively, foster growth, and service the debt." As had been the case with Silva Herzog in Mexico before, the combination of Cavallo's reputation as a savior and his bridging role to foreign creditors provided the Economy Minister with vast political leverage. Setser and Gelpern (2006:472) point out that "the institutional power of the economy ministry in particular hinged in no small part on its ability to deliver external financing." As the earlier discussion about the discretionary powers of the executive

showed, Cavallo – in a desperate bid to steer the economy around – wielded this leverage to near-autocratic effect, with remarkable frankness about the purpose of his second coming: "it was perfectly clear that President De la Rúa intended to appoint me as his Economy Minister in order to avert a default on the debt and to pre-serve the convertibility regime."

Why, then, were De la Rúa and Cavallo so adamant on preventing default? Setser and Gelpern (2006:475-6) have pointed out that, since half of the country's $90 billion debt was in the hands of domestic constituents and financial institutions, a default "would [have] reduce[d] the financial wealth of those Argentines who had invested in the debt – banks and pension funds as well as wealthy Argentines with offshore accounts." It would also have led to the collapse of the country's financial system and would have forced the government to come to the rescue of private banks and the large pension and insurance funds. The vast capital injections this would have required were impossible to undertake in the fiscal and monetary straitjacket of the convertibility regime. A default would therefore automatically force the government to abandon convertibility. This in turn risked reviving the specter of inflation that so haunted not only the lower and middle classes – who always bore the brunt of price increases – but especially the investor class (since inflation cancels out real interest). Moreover, the convertibility regime cemented Argentina's integration into the US financial system, enabling wealthy Argentines to invest and safely deposit their savings abroad. A default was therefore clearly not in the interest of Argentina's political and financial elite – and De la Rúa and Cavallo, as representatives of the embattled *patria financiera*, were determined to avoid harming this key constituency at all costs.

The problem was that three years of crisis and over a decade of relentless austerity and neoliberal restructuring had left an indelible mark on the already-fraught relationship

between the government and its voters, and between the political establishment and citizens more generally. De la Rúa's failure to do anything about the economic collapse, combined with his embarrassing corruption scandals and his seeming indifference to the suffering of ordinary people, caused presidential approval ratings to drop to unprecedented lows. While his popularity stood at 70 percent when he took office in 1999, by October 2000 it had dropped to 32 percent and by June 2001 it had was down to 15 percent, easily making De la Rúa the country's most unpopular and most despised democratically-elected President ever (Epstein and Pion-Berlin 2006:7). In fact, a Gallup poll in November 2000 found that only 11 percent of voters believed the government was doing a good job economically, while nearly half saw no difference between the policies of De la Rúa and those of the thoroughly corrupt crony-capitalist *caudillo* Carlos Menem, from whom the President had so desperately tried to distance himself all these years (Epstein and Pion-Berlin 2006:8).

But the anger ran deeper than that: citizens had begun to question the legitimacy of the post-*junta* order as a whole. As one observer put it, "there was a widespread feeling, if an ill-defined one, that the people had been let down by the entire political class" (Klein 2004:3). As the government grew ever more committed to its obligations towards foreign bondholders and ever less responsive to its own citizenry, a deep crisis of representation took hold that saw public trust in the political establishment and in democratic institutions collapse. Several Graciela Römer polls during Menem's presidency had already indicated a slide in public confidence in political parties: while only 24 percent of those questioned expressed some or much confidence in 1993, this fell to a mere 10 percent in 1999, while confidence in Congress as a political institution fell from 31 percent to 13 percent (Epstein and Pion-Berlin 2006:9). These dynamics were further aggravated by the financial crisis, and in particular by Cavallo's erratic and autocratic approach to crisis management.

The majority of people simply lost their faith in democratic institutions. Protests, strikes and occupations were on the rise, and incensed citizens took to physically attacking officials spotted in public. Social tensions reached a point where most politicians were too afraid to even go out for dinner or cross the street on foot. Senator Eduardo Menem, the former President's brother, was assaulted on an airplane; others were yelled and spat at in restaurants. According to a Graciela Römer poll taken around the congressional elections of October 2001, 70 percent of respondents were dissatisfied with political institutions.[36] The midterm elections themselves were widely seen as a referendum on the government's economic policies. As Tomz (2002:14-15) recounts, "all major parties addressed the default in their manifestoes, with some clinging to the status quo policy of payment and others seeking an immediate suspension of payments." Duhalde, representing the national-popular center-left of the Justicialist Party, restated the same default pledge he had made in the 1999 elections, and members of De la Rúa's Radical Party – including ex-President Alfolsín and De la Rúa's former cabinet chief Rodolfo Terragno – publicly distanced themselves from De la Rúa by pledging a default on the external debt. Terragno even claimed to have made default "the leitmotif of my campaign" (*ibid.*).

The outcome of the mid-term elections was the clearest manifestation of the crisis of representation to date. Despite the fact that voting was obligatory, more than 26 percent of the electorate did not show up at the polls. Of those who did vote, an unprecedented 22 percent cast blank or spoilt ballots (the so-called *voto bronca*) in protest against the political class (Lewis 2009:134). "Public frustration," Levitsky and Murillo (2003:154) wrote, had "reached a boiling point." One observer noted that "the cumulative social disillusionment with the [Radical Party] of Alfolsín, the [Justicialist Party] of Menem and the Alliance of

36 'El 70% está insatisfecho con las instituciones políticas', *La Nación,* October 28, 2001

De la Rúa gave rise to the idea that there was no place within the structure of the Argentine political system for the representation of broad and diverse social demands" (Schuster 2008:165). The leading newspaper *La Nación* simply headlined that "the people do not feel represented." In addition to the widespread abstention and the large *voto bronca*, Tomz (2002:15) shows that those who did cast a positive vote "overwhelmingly favored candidates who did not want to repay the foreign debt." Thus the pro-default Peronists, the Justicialist Party, became the biggest group in the Lower House while retaining its control over the Senate. Federico Storani, a leading figure in the ruling Radical Party, admitted defeat and called it a "plebiscite against the government's economic policy" (*ibid.*).

Meanwhile, polls revealed that public opinion had largely turned in favor of default. According to one poll in the city and greater metropolitan area of Buenos Aires, only 28 percent of Argentines wanted their government to stay current on its debt obligations, while 63 preferred to impose a unilateral moratorium (Tomz 2002:15). Another found that only 5 percent considered repayment to be a priority, while support for a total repudiation of the debt more than doubled from 11 to 27 percent compared to the last elections of 1999 (*ibid.*). But De la Rúa refused to give in. In fact, he decided to swim right against the current of public opinion by insisting on even more austerity to prevent what he considered to be a "catastrophic" default. The president declared that "I am going to give over my life to this struggle. We discard the idea of a devaluation or default." Despite losing his Congressional majority and witnessing his party disintegrate before his eyes, President De la Rúa stood firm in his insistence on the full and timely repayment of the national debt. In a televised address he euphemistically stated that "I know that many are not content with the government or with the form of my management and style, [but] it is time to face reality... Argentina will not fall into a cessation of payments" (cited in Tomz 2002:15).

The obstinance of the president and the complete disqualification of the political class as a whole left many Argentines hungry for change. Strikes and protests became not only more frequent but also more militant. In the period between July and December 2001, the amount of strikes per month tripled compared to the same months of the previous year. Tomz (2002:13-14) remarks that "the jump, sparked by a major new round of budget cuts and a 'zero deficit' plan ... confirms that workers were becoming less tolerant of the austerity needed to continue servicing the debt." Meanwhile, protesters blocked highways and major intersections, attacked government buildings and on a number of occasions temporarily took officials "hostage" to demand social jobs or unemployment benefits. As the government continued to lay off civil servants and cut salaries, pensions and social security benefits, new forms of popular protest began to bubble up from below. Hausman and Velasco (2003:11) recount that "the new poor realised that their social collapse was unstoppable. They were going to carry on falling. It was at that point that new political actors appeared." Notably, these were "not the historical leaders of the working class because, when the labor market collapsed, the unions, as the political representatives of the working class, went with it." Schuster (2008:167) writes that the "new forms of political construction [were] built from within society rather than the political system, [and] emerged on the Argentine scene with unusual force."[37]

At the end of November 2001, these dramatic changes from below coincided with equally dramatic changes from above: the *riesgo país* shot up to 5,000 basis points, leaving

37 Emphasizing democratic principles and stressing their autonomy from parties, unions and the state, these "new social protagonists" began to craft alternative forms of self-organization that touched upon the lives of millions. Given their widespread popular appeal and innovative grassroots practices – which included the blocking of roads and the mass occupation of closed factories and other workplaces – the traditional political actors largely failed to connect to these burgeoning social movements, let alone come up with a convincing political response (Colectivo Situaciones 2002; Zibechi 2003; Sitrin 2012).

Argentina with no external sources of financing. On November 30, amid growing fears of a breakdown of the convertibility regime and a consequent devaluation of the *peso*, a bank run took off, leading Cavallo to shut down the country's banks and declare the *corralito* on December 1, freezing bank deposits, outlawing deposit transfers abroad and imposing a withdrawal limit of 1,000 pesos per week. As one banker put it, "the *corralito* trapped the *perejiles,*" the little guys. "The big players already knew what was going to happen and got out ahead of time" (cited in Ariso and Jacobo 2002:159). The *corralito* backfired, prompting dramatic social unrest and setting in motion a vicious cycle that would eventually culminate in Cavallo's own political demise. A few days later, on December 5, against the backdrop of intensifying opposition in the streets, the IMF announced its decision to withhold the next installment of its bailout program in response to the government's inability to stick to the conditions of its loans. Now the government found itself under immense pressure from all sides to simply get it over with and default.

The popular outrage that had been building all throughout the year came to a head on December 19 when the streets exploded in furious anger. As Rambarran (2004:6-7) puts it, "the social fabric unraveled." Food riots and violent looting first broke out in Rosario and within hours spread through the country to Santa Fe, Córdoba, La Plata and Mendoza, and from there via the suburbs of Buenos Aires to the heart of the capital (Lewis 2009:135-6). Violent clashes broke out between protesters and police. Groups of rioters and looters stormed banks and supermarkets. In a poorly calculated attempt to quell the uprising, De la Rúa went on national television to announce a suspension of constitutional rights and to declare a 30-day state of exception, deploying the federal police, border guard and naval prefecture to restore order. Given the severity of the social unrest and the speed at which the riots spread across the country, the president briefly entertained the idea of shutting down

all private radio and TV stations and mobilizing the army to put down the rebellion, but both options were rejected by his cabinet. With the experience of the *junta* still fresh in the country's mind, even the army leadership turned out to be unwilling to leave the barracks without express approval from Congress and so long as there remained a chance, however slim, that conventional political solutions might save the day.

Like Cavallo's *corralito*, the president's televised address backfired in the worst way imaginable. According to Malamud (2006:13), "De la Rúa looked distant and insensitive to what was taking place. Some of his aides even qualified his speech as 'autistic'." Citizens felt that their legitimate expressions of indignation were not being taken seriously and so they defied the curfew and descended from their homes in the hundreds of thousands. As protesters marched on the Plaza de Mayo and amassed in front of the presidential palace, clashes broke out and police violently cracked down on the protests, killing 17 people nationwide, five of them right in front of the presidential palace (Malamud 2006:13-14). That night, De la Rúa – looking for a scapegoat – forced a publicly humiliated Cavallo to resign.

The rage, however, could no longer be contained so easily. In the morning of the next day, December 20, renewed protests broke out as thousands returned to the Plaza de Mayo to defy the curfew again. When it had become clear that violent repression would not diminish the people's resolve, De la Rúa again went on national television in the afternoon to invite the Peronists to join him in a "government of national salvation" and help restore "peace and order" to the country. The Peronist leadership refused. Even De la Rúa's own cabinet members later declared that, watching the President's performance on TV, they could not escape the feeling that De la Rúa was on another planet, far removed from what was truly going on "out there" (Malamud 2006:14). As his Ministers and Senators began to

abandon him and as the protesters only seemed to grow stronger in numbers and resolve, the politically isolated De la Rúa finally tendered his resignation. Security forces considered it too dangerous to evacuate him from the presidential palace by car, and so – in an image that would come to define Argentina's deepest political crisis since the fall of the *junta* – De la Rúa was forced to escape the palace by helicopter. As he was airlifted from the roof of the building, the crowds below roared: "All of them must go!" As Tomz (2002:15-16) put it, the protesters "had just removed from power the most significant obstacle to default."

Since the vacant position of vice-president had never been filled, the role of interim-president fell to Ramon Puerta, the Peronist leader of the Senate, until Congress elected Adolfo Rodríguez Saá as the new head of state. The first thing Rodríquez Saá did upon taking office was to declare a unilateral moratorium on Argentina's entire outstanding debt to private creditors. In his inaugural address on December 24, he declared that "I believe in an Argentina without unemployment, without misery. I will govern for the most humble and for those who suffer. I call for the suspension of payments on the foreign debt until all Argentines have jobs" (cited in Tomz 2002:15-16). Rodríquez Saá lamented that "the gravest thing that has happened here is that priority has been given to foreign debt while the state has an internal obligation with its own people."

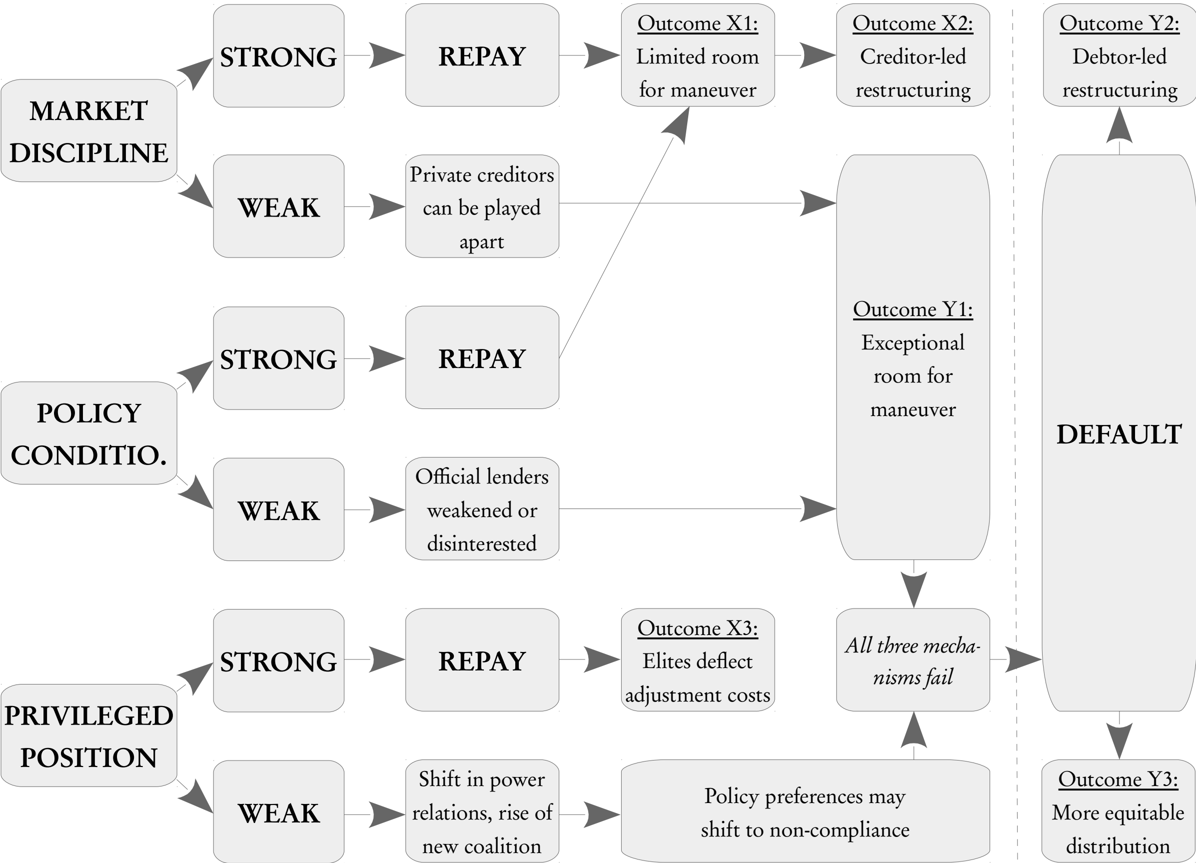
But while Argentina entered into default on over $80 billion in debt (half of which owed to foreign private creditors and half to domestic creditors), the new President almost immediately fell foul of his other pledges. As fresh protests took off, the most important Peronist governors came together and decided that Rodríguez Saá had to go. On December 30, Congress voted to replace him with Ramón Puerta, who resigned immediately. From there, the hot potato of the presidency passed to Eduardo Oscar Camaño, chairman of the

Chamber of Deputies, who was a known supporter of Eduardo Duhalde, the former vice-president under Menem and De la Rúa's main opponent in the 1999 elections. On January 1, 2002, the power vacuum was finally filled when Camaño arranged for Duhalde to take over and complete the remainder of De la Rúa's term, with new elections set for December 2003. Duhalde acceded to power as the country's fifth president in just ten days' time.

In analyzing this incredible sequence of events, unprecedented and still unequaled in Argentina's post-war history, the conventional explanations of debtor compliance appear to hold little explanatory power. Between Argentina's exceptional over-compliance of October 2001 and its record-shattering default of December 2001, nothing truly changed in terms of its reputation, the credible threat of sanctions, or the nature of its political institutions. If these variables remained constant, they cannot account for the change in outcome. After the institutional investors had dumped their bonds in the mega-swap and the IMF had cut off its credit line, the only thing that truly changed in the intervening period was that the *patria financiera* – represented by De la Rúa and Cavallo – was ousted from office, and sustained mass pressure from below forced the Peronist establishment that inherited the presidency to make serious concessions to the population at large. These concessions took the form of a unilateral moratorium, which had been advocated by the national-popular wing of the Peronist opposition from 1999 onwards, which was strongly supported by a majority of voters, and which was already widely expected, desired and actively pursued by the US, IMF and Wall Street. Since the other two enforcement mechanisms of market discipline and policy conditionality had earlier been been deactivated from above by the mega-swap and the IMF's refusal to release the next credit tranche, the ouster of De la Rúa finally made the inevitable unstoppable.

Outcomes of the Crisis

Figure 5.8 – outcomes according to structural power hypothesis:



The above discussion shows how the three enforcement mechanisms – as in Mexico – were initially fully operative in the Argentine case, compelling the government to comply and repay its debts. But at the same time it also shows how these mechanisms – unlike in Mexico – ended up breaking down, ultimately leading to default. If the structural power hypothesis is correct, then, we should observe a number of contradictory outcomes in the Argentine crisis that on the one hand reveal an unexpected similarity to the Mexican case while on the other presenting a sharp contrast. First, given the fact that its private creditors were scattered, the Bush administration disinterested and the IMF incapacitated, we should observe exceptional room for maneuver in Argentina post-default. At the same time, given

the uniqueness of the Argentine case we would expect this room for maneuver to remain a quite limited phenomenon that did not necessarily apply to its neighbors. Second, given the greater room for maneuver Argentina experienced, we should expect it to take the lead in pursuing a debt resolution process in its own national interests. At the same time, however, we would expect global finance – whose structural power remains undiminished, according to this thesis – to have escaped from the crisis relatively unscathed, even with profits (after all, as we have seen, US institutional investors had already shed their Argentine exposure by the time of the default). Third, given the relative strength of Argentina's social movements and the country's rupture with global finance following the default, we should expect the privileged position of the *patria financiera* to be eroded – since its bridging function broke down the moment Argentina lost access to capital markets – and a new coalition to emerge in which national-popular interests would play a more central role, with important consequences for the distribution of adjustment costs. At the same time, however, given the state dependence on national capitalists for an economic recovery, we would expect the redistributive post-default measures to be conciliatory rather than emancipatory and the defiance of investors to be rhetorical rather than truly transformative. Once again, we find evidence for each of these propositions, lending further support to the structural power hypothesis.

Argentina's Exceptional Room for Maneuver

Perhaps the most remarkable outcome of Argentina's crisis is the exceptional room for maneuver the country enjoyed following its default. While Eduardo Duhalde struggled in 2002 to balance the contradictory needs to restart private accumulation on the one hand and restore popular legitimacy on the other, Néstor Kirchner upon assuming office in 2003

found himself presented with a political and economic opportunity structure for much more confrontational action, opening space for an aggressive debt restructuring where no such space had existed before. In early 2005, after a long and arduous negotiation process, Argentina reached a deal with its creditors that saw 76 percent of bondholders accept new bonds worth 25 percent of the original defaulted ones. The remaining 24 percent, a Baptist-Bootlegger coalition of European pensioners and American vulture funds, saw their claims repudiated (Baer, Margot and Montes-Rojas 2010:12). When Argentina briefly reopened the restructuring deal in 2010, more bondholders subscribed, reducing the “holdouts” to a mere 9 percent. This is a remarkably high degree of participation given the size of the haircut and the aggressive posturing of the government. How was Kirchner able to get his way?

There were a number of factors that played to Argentina's advantage. First, as has been discussed already, Argentina's bondholders were greatly atomized after the creditor-led mega-swap of mid-2001, and mostly made up of so-called “financially illiterate” small savers and pensioners. This had important consequences for creditors' bargaining power *vis-à-vis* the Argentine government in the debt negotiations. As Lewis (2009:158) puts it, “most of the bondholders were 'small fry' and scattered geographically, making it difficult for them to coordinate any strategy.” The collective action problem of 1930s bond finance returned with a vengeance. “True to atomistic stereotype,” Gelpern (2005:3) observes, “bondholders could not hold a coalition. Each acted in its own self-interest.” Furthermore, Gelpern (*ibid.*) has importantly noted that “these [small] investors generally were not repeat players and knew little about emerging-market debt.” Mortimore and Stanley (2006:20) also affirm that “the lack of cohesion among the different organizations representing the creditors worked to the advantage of the government.” Kirchner made strategic use of these factors to play his creditors apart. For one, when bondholders set up the Global Committee of Argentina

Bondholders in an attempt to present a united front at the debt negotiations, he simply refused to talk to the group or even to recognize its existence (Gelpern 2005:3). He was able to do this because he did not depend on these dispersed bondholders for future credit – even if he restructured the debt on extraordinarily good term for the creditors, most bondholders had made a one-off investment and were unlikely to ever lend to Argentina again.

Argentina's unilateral suspension of payments also contributed to reversing the debtor-creditor power dynamic – just as it had done in the wake of the defaults of the 1930s (Ocampo 2013). Before Argentina's moratorium, bondholders had been receiving 100 cents on the dollar and any reduction in the face value of their claims would have undoubtedly been considered an unacceptable loss. Now, some two years after the default, creditors were receiving 0 cents on the dollar, and – barring moral concerns over the violation of creditor rights – any form of restructuring, even an unusually harsh one, would at least allow them to mark their holdings to market and continue to profit from restructured bonds and new deals in the future. The moratorium, in other words, restored the initiative to the debtor and allowed it to wield the prospect of a restructuring as a carrot instead of a stick, creating an incentive structure for creditors to sign up to an aggressive debt restructuring that they would otherwise never have agreed to. As Datz (2013:474) succinctly put it, "investors were not looking at losses taken in 2001, but at a scenario of gains in 2005." Economy Minister Roberto Lavagna seemed to be under a similar impression when just a month before the conclusion of the deal he rhetorically asked why – despite the destruction of numerous debt contracts in 2001 – investors were still so eager to buy Argentine bonds. His simple answer: "because today clearly they can get a very good rate of return" (cited in Datz 2013:465).

The benefits of Argentina's restructuring accrued especially to the financially literate repeat players: the international banks and institutional investors, who had a direct interest in keeping Argentina in the lending game. But they were not immediately clear to the small European retail investors, who were unlikely to lend to Argentina again and who would have preferred a higher payout. Kirchner was acutely aware of these conflicting interests in the creditor base and exploited the fissure to full effect. By negotiating individually with the big international banks while at the same time denying the very existence of the dispersed bondholders, his government successfully drove a wedge in the (non-existent) international creditors' cartel – to the detriment of pensioners and other small investors in Europe.

The second factor playing to Argentina's advantage was that its dispersed creditors received little or no support from their own governments, the IMF or the United States (Lewis 2009:158). In its negotiations with private bondholders, Helleiner (2005b:956) notes, "the USA was ... quite sympathetic to the position taken by the Argentine government." When Bush met Kirchner at the Summit of the Americas on January 13, 2004, Bush "quite significantly did not echo Koehler's request that he consider paying more than just 25 percent to holders of bonds." As Quarles of the US Treasury put it: "it's not the IMF's role to impose any particular terms of the deal. ... How much can Argentina repay? ... I think that's something that the IMF and the US, as a shareholder in the IMF, should not have a view on." Treasury Secretary Taylor echoed the same sentiment: "the idea here is to allow negotiations but not to be in the middle, or choose sides. That's for the creditors and Argentina to work out" (all cited in Helleiner 2005b). Mortimore and Stanley (2006:20) conclude that "the non-intervention of the IMF together with the lack of cohesion within the G7 ultimately benefited the debtor." It also greatly frustrated the small bondholders. As an Italian lawyer representing a group of pensioners who lost their life's savings in the

default put it: “Argentina doesn't want to pay its debt, and Washington doesn't want to force it to pay. So the easiest thing is to send the bill to the bondholders in Europe, little people no one will ever see” (cited in Moffett 2004). Another Italian lawyer pointed out to the *Wall Street Journal* that “with what's happening in Iraq and Afghanistan, you can be sure that Mr. Bush didn't want to start a battle with Argentina, just to defend some retirees in Europe” (*ibid.* 2004).

But the role of the US government was not just characterized by disinterest. In fact, the Bush administration took an active stance in favor of Argentina's aggressive approach to the private creditors and the IMF. When Kirchner missed a $2.9 billion payment to the IMF on September 9, 2003, President Bush personally supported the move, further reducing the IMF's ability to defend bondholder interests in the debt negotiations (Lewis 2009:157). A group of Argentine economists has noted that, “because there was a real risk of Argentina defaulting on its large obligations to international financial institutions, the Fund's leverage to influence the outcome of the private debt restructuring was much weakened all through the post-default phase of the crisis” (Cassou, Erce-Domínguez and Vázquez 2008:15). When Kirchner finally reached an agreement with the IMF that was uncharacteristically beneficial to Argentina, Bush personally called up his Argentine counterpart to congratulate him and express his satisfaction with the deal, while Treasury Secretary John Snow was reportedly very pleased with the agreement as well. Randal Quarles, Assistant Treasury Secretary for International Affairs, claimed that the administration had “deliberately pushed for the budget surplus targets [in the IMF Standby Agreement] to be left undefined in the second and third years – over IMF objections – because it wanted the IMF not to take a stance in the debt negotiations with private creditors,” stating that “it's not the IMF's role to take a stance to impose any particular terms of a deal” (cited in Helleiner 2005b:954).

This active support from the Bush administration in turn allowed Argentina to segment not just its small bondholders and large institutional investors, but also its official and private creditors. By negotiating on two different tables at once, Kirchner effectively removed IMF conditionality from the equation when it came to his government's arm-twisting with private creditors. And indeed, when Kirchner made his final "take it or leave it" offer to foreign private bondholders, the US government "raised no objections to the Argentine offer" (Helleiner 2005b:955). In fact, the day after the final offer was made, Bush briefly met Kirchner at the sidelines of the UN General Assembly where the US President "seemed to endorse" the deal. According to Kirchner's spokesperson, Bush told him the following words: "congratulations again for the agreement with the IMF; now you must keep negotiating firmly with private creditors." When Kirchner approached him later that day, Bush even had the wit to crack a joke about the deal to a group of assembled world leaders: "here comes the conqueror of the IMF!" (all cited in Helleiner 2005b:955).

The third factor playing to Argentina's advantage were the "extraordinarily good international conditions" it found itself faced with post-default, most importantly a boom in commodity prices generated by rapid Chinese growth and the wave of liquidity sloshing through international financial markets thanks to the Fed's historically low interest rates in the wake of 9/11 and the collapse of the dotcom bubble (Baer, Margot and Montes-Rojas 2010:12; Mortimore and Stanley 2006). These beneficial external conditions combined with Argentina's own relative insulation from the world economy. Cibils *et al.* write that "one of the great advantages that Argentina has over other countries confronting the creditors' cartel ... in terms of recovering on its own is that the country is running large surpluses on both its trade and current accounts" (Cibils, Weisbrot and Kar 2002:21). Between 1999 and 2002, the government actually managed to run a sizable primary budget surplus, leaving it

much less dependent on external financing than most other peripheral countries facing balance-of-payments crises (Weisbrot and Cibils 2002:3). Unlike Mexico, Argentina was also self-sufficient in food production and a net exporter of commodities, while its large current account surplus greatly reduced its dependence on hard currency for the import of basic necessities. As a result, Argentina's currency reserves never fell below four months' worth of imports, compared to two weeks' in Mexico in 1982 (World Bank 2015). Meanwhile, the government could count on the support of an important regional ally: during and after the negotiations, the Socialist government of Hugo Chávez came to the rescue by reinvesting parts of Venezuela's oil revenue surplus in special Argentine bonds. In 2005, the Venezuelan government lent a total of $3.1 billion and the two countries set up a special investment fund, the Fund for the South, whose mission "was to free South America from dependence on the United States and the IMF" (Lewis 2009:162; Datz 2013:472). Chávez purchased $3.6 billion in bonds in 2006 and a further $1 billion in 2007. Venezuela's assistance contributed to Argentina's insulation from market discipline and IMF conditionality (Scott 2006:6).

With the commodity boom boosting exports and alternative sources of financing reducing dependence on global finance, Argentina experienced high growth rates averaging 7.5 percent in the post-default years. The recovery began under the presidency of Duhalde in mid-2002 and continued right up until the global financial crisis of 2008. These factors combined to boost Kirchner's standing at home and his self-confidence abroad, feeding his fiery anti-creditor rhetoric. As Mortimore and Stanley have observed, "the short-term cost [of Kirchner's defiant stance] to the country was minimal, since Argentina clearly had no possibility of obtaining external financing in the international financial markets anyway" (Mortimore and Stanley 2006:20). With the prospect of high growth and the possibility of raising cheap credit through domestic bond auctions, confrontation with powerless small

bondholders and unpopular international financial institutions seemed like a sensible path to pursue. All of this goes to show that Argentina had considerably more room for maneuver in the wake of its default than it had had under Alfonsín in the 1980s.

Still, it would be overly hasty to conclude on the basis of these observations that all sovereign borrowers therefore enjoy similar opportunities and that the structural power of finance somehow does not hold up in reality. Argentina's opportunity structure was highly idiosyncratic, as were the circumstances in which it found itself; a fact that is confirmed by the observation that the country's unilateral moratorium and aggressive debt restructuring remain isolated and exceptional phenomena in the global political economy. As Roubini (2005) has emphasized, "the lesson of Argentina is that crisis and default are very costly and painful, not that they are costless. Otherwise, if default is so costless, how come we do not see dozens of highly indebted countries following Argentina and defaulting?"

The Brazilian experience presents a particularly interesting contrast in this respect. In 2002, as Brazil prepared for presidential elections, it found itself facing similar pressures as Argentina had since 1999; pressures that were exacerbated by the prospect of a victory for Lula's Workers' Party. As a devout left-wing activist and outspoken labor leader, Lula gained a negative reputation among investors in the 1980s debt crisis for his vocal advocacy of a debt moratorium and an outright repudiation of the international obligations incurred by the military dictatorship. In its December 2001 electoral program, the Workers' Party still "spoke of denouncing the existing agreement with the IMF and auditing and re-negotiating the external debt," and mentioned "a complete revision of the policy of giving priority to the payment of the debt service" (Williamson 2002:12). So when Lula began to advance in the polls, investors took fright. Every time a new poll indicated a Lula lead, the

"Brazil risk" shot up (*ibid.* 2002:11). Unlike Argentina, foreign banks still carried significant exposure to Brazil in 2002. As they withheld their lending fearing a default, Brazil's spreads shot up, widening from 7 percent in March 2002 to 20 percent in September, as Lula rose from 30 to 40 percent in the polls (Miller, Thampanishvong and Zhang 2004:3-4).

In response to this market pressure, Lula decided to tone down his rhetoric over the course of the campaign. By January 2003, *The Economist* reported that, "since the final weeks of the election campaign, Lula has worked hard to turn investor panic into mere wariness. He has stressed that Brazil means to pay its debt and has chosen ministers who seem ready to carry that promise through" (*Economist* 2003). After Lula's victory, economist Arminio Fraga, a former investment banker who had served as Central Bank Director under the previous conservative government, noted that "the biggest event when Lula came to office in 2003 is that nothing happened" (cited in Miller, Thampanishvong and Zhang 2004:24). Roubini (2005) writes that, "Lula, as soon as he was elected, looked across the border and saw what default – even an unavoidable one like Argentina's – causes as its by-product, i.e., massive crisis and pain. And he rightly decided to do even more fiscal adjustment and try to avoid default." Argentina's default thus remained the exception.

US Hedge Funds as Big Winners of the Debt Restructuring

Given the unilateral nature of Argentina's default and the aggressive restructuring it pursued, perhaps the most surprising outcome of the entire episode was the fact that certain elements of global finance still managed to somehow turn the crisis to their advantage. In this sense, Argentina's policy choices may have been diametrically opposed to those of Mexico in the 1980s, but for Wall Street the outcome was more or less the same – if not

better. As we have seen, by the time of the default in 2001 the big US-based institutional investors had already dumped most of their bonds on a scattered group of European retail investors, meaning they largely emerged unscathed from the initial default. But by the time of the 2005 restructuring, some of these retail investors – including many pensioners who were terrified at the prospect of losing their life savings – despaired at Argentina's refusal to recognize their representatives in the debt negotiations and sold back the same bonds, for mere cents on the dollar, to an eager army of traders at the big Wall Street hedge funds. The opposition to the eventual deal came mostly from Italian pensioners; the US hedge funds hardly put up a fight and signed up by an overwhelming 90 percent (Roubini 2005).

Why would the hedge funds be so eager to jump on Kirchner's offer if they thought they were receiving such a bad deal? The answer is that they were, in fact, not receiving a bad deal at all. As Datz (2013:474) shows, "some hedge funds bought these bonds at 17 cents in 2002 and were happy to swap them for nearly double that amount in 2005." This, in turn, greatly eased the restructuring process for the government, "because instead of dealing with private international creditors who bought the bonds at 90 cents on the dollar, the government was dealing with those who paid around 20 cents" (*ibid.*). In short, when the debt restructuring finally came around, Wall Street had basically already won the battle by dumping most of its worthless bonds on powerless European pensioners and then buying them back up at greatly discounted prices to restructure them at a profit. European retail investors ended up as the losers, while Wall Street hedge funds emerged as the big winners.

While the opaque nature of bond finance means that exact numbers are impossible to verify, the *Wall Street Journal* reported that by the time of the 2005 restructuring small European and Japanese investors (including 450,000 Italians, 35,000 Japanese and 15,000

Germans and Central Europeans) held around 44 percent of Argentina's defaulted bonds, with local Argentines holding another 38 percent (Moffett 2004). Given these numbers, it is not surprising that the main opposition to the restructuring came from the European retail investors. But as Roubini (2005) has angrily pointed out, even the opposition of these retail investors was designed to serve narrow Wall Street interests. In what probably amounts to the greatest scandal of all, the retail investors who had already been defrauded by the Wall Street investment banks in the mega-swap were now lured back by these same investment banks who offered to represent them in negotiations with the Argentine government. In Roubini's view, the banks feared being sued by these retail investors and refused to sign a deal with the Argentine government simply to avoid such litigation (Roubini 2005).

Moreover, the eventual debt reduction for Argentina is nowhere near as large as the 75 percent nominal haircut would lead one to expect. The reason is that the government added an obscure and rare "sweetener bonus" to the deal – a so-called GDP warrant – which paid bondholders an annual dividend in case Argentina's economic growth rates were to exceed a certain threshold. Since its GDP had contracted by almost 20 percent between 1998-'02, and since the country encountered such a favorable external environment after its default, it was to be expected that Argentina would grow rapidly and that investors stood to gain lavishly from these clauses. Since Argentina's average annual growth rates shot up to 7.5 percent after the default, the government actually found itself confronted with higher rather than lower debt servicing costs as it emerged from the crisis. At the same time, the banks made big profits from the intermediation fees they could charge for the restructuring itself. Santiso (2003:193) reports that "almost all the investment arms of leading Wall Street firms made lucrative deals" with the Argentine government (cited in Datz 2013:474). In the end, it is clear that Kirchner's scathing rhetoric outshone the actual losses he managed to

impose on powerful international financiers. As the *Economist* (2005) dryly noted after the conclusion of the restructuring deal: "even in a default, there is money to be made."

A Rearrangement of Domestic Power Relations

The third important outcome of the Argentine crisis – and a point on which the contrast to the Mexican case could not be sharper – is the rearrangement of *domestic* power relations following the default and the consequences this had for the relative redistribution of the costs of adjustment. Up until the default, the burden of adjustment had largely been borne by the seemingly powerless popular sector; the imposition of the *corralito* was the clearest manifestation of this. Argentine financial authorities deliberately left a loophole in the *corralito* that allowed their main constituency – wealthy elites – to pull their money out of the banks anyway. Through a mechanism very similar the one used by Mexicans elites in the wake of López Portillo's bank nationalization, rich Argentines were able to move their savings and investments to the stock exchange. Dominguez and Tesar (2004:15-16) explain that "restrictions in the *corralito* ... allowed investors to use their frozen bank deposits to purchase Argentine stocks, and, in so doing, provided a legal mechanism for transferring funds abroad." As a result, the lucky Argentines who still had real savings in the bank could simply buy stocks that were cross-listed in the US to legally convert their Argentine shares (purchased with pesos) into American Depository Receipts (ADR), which could then be sold for dollars and deposited in a US bank account (Dominguez and Tesar 2004:15). Only this loophole can explain the idiosyncratic 50 percent increase in Argentine stock exchange valuations in December 2001, at a time when the national economy was effectively in a state of collapse: the rich were pouring their money into shares to get it out of the country.

The strength of the popular resistance to such privileges for the wealthy eventually forced the political and financial establishment to make a number of concessions to the domestic population, leading not only to the unilateral moratorium but also to new set of redistributive policies and anti-poverty measures. This is why Schuster (2008:168) argues that "the power of protest has been perhaps one of the most important lessons derived from the events of December 2001." As Argentine historian Ezequiel Adamovsky put it, "it was the constant threat of looting, targeting of politicians, of rebellion, of occupations, of road-blocks, and assemblies that disciplined both management and local and international financial sectors, opening an unimagined space for politics" (cited in Fiorentini 2012).

In the immediate wake of the December uprising, President Duhalde struggled to restore a semblance of legitimacy to the state apparatus and was constantly forced onto the defensive by a restive population. Upon taking office, Duhalde's approval rating stood at a mere 10 percent (Rock 2002:56), and Levitsky and Murillo (2003:155) write that the initial wave of protests had "grown into a massive civic rebellion against the entire political elite." A Gallup poll showed that 84 percent of respondents did not feel represented, while 87 percent rejected all parties outright (Turner and Carballo 2005:175-6). Duhalde was therefore acutely aware of the need for some kind of shift in policy and rhetoric to outmaneuver the country's burgeoning social movements and restore political legitimacy. He embarked upon a populist campaign to shore up national support for the political system by pursuing a different distribution of adjustment costs. Publicly railing against "the destructive alliance of 'political power and financial might' that had sold the nation out to foreign creditors and international financial institutions at the expense of internal production and consumption," the President tried to portray himself as a real man of the people (Epstein and Pion-Berlin 2006:12). He restored the yearly extra months' pay for public sector workers and earmarked

$350 million for soup kitchens. In an address to Congress in March 2002, he for the first time publicly recognized the "formidable crisis of representation" that had undermined the public's trust in the institutions. Despite the acute fiscal crisis of the state, he announced the implementation of the *Plan Jefes y Jefas de Hogar Desocupados*, a $1 billion household support program targeted at the unemployed, in a move that was widely interpreted as an attempt "to combat militant opposition by the *piquetero* movement" (Féliz 2012:5).

But even these moves failed to subdue the people's vexation with the authorities. The government remained trapped between the social unrest at home and the total loss of credit from abroad. Duhalde, in a word, struggled to bridge the contradiction between the state's dependence on capital on the one hand, and its need to restore popular legitimacy on the other. One observer identified the president's approach as profoundly "schizophrenic": while he embraced the radical rhetoric of the movements, Duhalde "began (gradually and almost secretly) to do as the IMF advised, not only devaluing the currency, but also securing an agreement with the provinces to cut spending, unifying the exchange rate, and changing a bankruptcy law to match international standards" (Corrales 2002:38-9). While at home he complained endlessly about the crimes and national betrayal of Argentina's *patria financiera*, he simultaneously sought to placate his other audience – international investors – by exuding a market-friendly pragmatism abroad. As he failed to reconcile the state's two most basic functions, street protests resumed and Duhalde was forced by intensifying social unrest to call early elections for April 2003.

These were the conditions that Néstor Kirchner inherited when he assumed the presidency in May 2003, elected with just 22 percent of the vote after his contender withdrew from the race. To boost his standing, Kirchner, known as a moderate and pragmatic center-

left Peronist, immediately announced an economic program that prioritized growth and job creation and refused to resume payment of the debt at the expense of social and economic recovery. In a return to the classical national-popular blend of left-Peronism, Kirchner praised the virtues of "national capitalism" as an alternative to the Washington Consensus that had led to the country's collapse. "It's not that we want not to comply, not to pay," he declared, echoing the words of Alfolsín and García in the 1980s, "but neither can we pay at the expense of seeing more and more Argentines postponing their access to proper housing, a safe job, education for the children, and health services" (cited in Helleiner 2005b:954).

In an attempt to restore the legitimacy of the political system and the dominant position of the traditional Peronist establishment, Kirchner set out to build a corporatist coalition constituted by an alliance between national capitalists and leaders of the labor and unemployed workers' movements. In a meeting with a group of Buenos Aires bankers on September 29, 2003, Kirchner declared that "it is crucial that national capital partakes in the process of the reconstruction of society. It is impossible to build a national project if we do not consolidate a national bourgeoisie." This followed an earlier statement by Alberto Alvarez Gaiani, President of the Industrial Union, who had argued that – with Argentina now cut off from foreign credit – the only way to see to the state's structural dependence on capital would be to resume domestic investment by strengthening the government's ties to Argentine business. "There is a need for a national bourgeoisie," he declared. "A country is stronger when you have the owners of the most important companies in the country sitting around the decision-making table. Nobody is going to invest a single penny in this country for a long time" (both cited in Zibechi 2003). At the same time as opening up government to national capital, Kirchner pursued a classical Peronist strategy of co-optation with regard to labor and the popular sector. Now that the trade unions had practically imploded, the

main opposition came from the various factions of the *piquetero* movement. By incorporating the leaders of some of its more traditional and hierarchically organized groups into his government, Kirchner hoped to isolate the more radical autonomous wing of the *piqueteros*, demobilize opposition to the political system, and at the same time obtain a powerful ally in his political maneuvers against opponents (Schuster 2008:176). Luis D'Elia, leader of the *Federación Tierra y Vivienda*, one of the more visible *piquetero* groups, was appointed undersecretary for Land and Housing. D'Elia's followers, called *piqueteros-K*, became a crucial support base for Kirchner and a powerful weapon in the government's public confrontations with foreign companies (Lewis 2009:156).

This rearrangement of the dominant class coalition – away from Menem's neoliberal alliance between national capital and the *patria financiera* and towards a typical Peronist alliance between national capital and elements of the popular sector – went hand-in-hand with the embrace of an alternative economic model that has often been referred to as "neo-developmentalist" or "neo-extractivist." The embrace of this model was made possible by the advantageous external conditions mentioned before – ample liquidity and a commodity boom – and saw a massive transformation of Argentina's economy and agricultural sector, with a soy boom changing the face of the countryside. This shows that the events of 2001 and 2002 marked more than a change in government; they marked a profound rupture in the development of the Argentine political economy and a transformation (however partial) in the state-capital relation. The reduced dependence on foreign credit weakened the *patria financiera* and allowed for the emergence of a new class coalition that subordinated financial interests to the interests of extractive and exporting industries on the one hand, and of co-opted elements of the popular sector on the other.

Recent years have clearly revealed the vulnerability of the national-popular coalition and its accompanying state-led neo-extractivist model to changing external conditions. The end of the commodity boom in the wake of a Chinese slowdown and the end of cheap credit after the Federal Reserve's decision to raise interest rates for the first time in nearly a decade increased the external constraints on commodity exporters like Argentina, especially on those with left-leaning governments. Faced with inflationary pressures and skyrocketing borrowing costs, the left-Peronist coalition lost popular support and eventually faltered in the 2015 presidential elections, as Fernández de Kirchner's appointed successor lost out to the right-wing candidate Mauricio Macri, the former mayor of Buenos Aires and a scion of one of the country's wealthiest families, who at the time of writing was widely expected to begin a renegotiation of the defaulted debt with Argentina's holdout creditors, bringing the country's protracted and acrimonious standoff with its foreign creditors to a long-awaited end. In the capital-scarce environment that now lies ahead, the *patria financiera* – with its superior capacity to attract credit and investment – is likely to stage a vindictive comeback.

Conclusion and Possible Alternative Interpretations

The above discussion has shown that the three classical explanations of debtor compliance – reputation, sanctions and democratic advantage – are all unconvincing in the case of Argentina. None of these variables changed in the expected direction in the lead-up to default, so none of them can truly explain the switch from compliance to non-compliance. And while there is elementary evidence of debilitating spillover costs following the default, an explanation based purely on spillover costs cannot explain why Argentina changed its policy preferences from repayment to default. The structural power hypothesis, with its

emphasis on the three enforcement mechanisms of market discipline, policy conditionality and the privileged position of domestic elites does appear to be supported by the prevailing evidence and is able to provide a more dynamic account of the shift in policy outcome. The chapter showed how the three mechanisms gradually broke down over the course of 2001, eventually making the inevitable default unstoppable. As in the Mexican case, however, we could imagine at least two possible alternative interpretations for the main observations made in this chapter: the instrumentalist explanation and the constructivist explanation.

The instrumentalist view would emphasize interpersonal relations, elite control of government and direct forms of political pressure. Again, the findings in this chapter show that all of these factors may have played a role in swaying the government in specific directions. Cavallo, for instance, was known to be close to Wall Street and the *patria financiera*, and it was essentially the backdoor deal between the Economy Minister and a number of powerful international investment banks that sealed the envelope on the mega-swap, which set Argentina up with even greater debts while allowing institutional bondholders to divest of their Argentine exposure. In this sense, the instrumental power of creditors continued to play a role behind the scenes. Nevertheless, it should be emphasized that these more direct forms of power occurred against the backdrop of Cavallo's growing desperation about the government's acute fiscal crisis and the vulnerabilities of the financial system. With Argentina acutely dependent on foreign credit, Cavallo was willing to go to any extremes to keep liquidity circulating through the domestic economy. To paraphrase Lindblom, the bankers could not simply be left knocking on the doors of the Economy Ministry – they had to be invited in. The same goes for Cavallo's re-appointment: as this chapter clearly showed, both De la Rúa and Cavallo were very clear about the reasons he was asked to take over the Economy Ministry: to restore fiscal order, attract foreign credit and prevent a default on the

national debt. The *patria financiera* did not simply "colonize" key government positions, as an instrumentalist reading of the crisis might have it. Finance was powerful not because it controlled government; it controlled government *because it was powerful*. The state acutely depended on Argentine bankers and the elite to refinance the domestic debt and to provide a bridging role towards foreign lenders. There is no doubt that more direct forms of power continued to be exercised throughout the crisis, but they always occurred against the backdrop of the state's structural dependence on credit and hence the structural power of creditors and the privileged position of those with close ties to these creditors.

The policy preference eventually shifted from compliance to default not because a pro-default coalition suddenly managed to exert greater direct pressure or mobilize superior resources to defeat the anti-default coalition, but because the three enforcement mechanism of the creditors' structural power broke down: market discipline was dysfunctional in the absence of a coherent creditors' cartel and in the face of Argentina's relatively high self-sufficiency in food, fuel and financing; policy conditionality did not work with a hostile US Congress opposing further international bailouts and with the IMF eventually pulling the plug on Argentina's Standby Program; and the privileged position of domestic elites was thoroughly hollowed out by the deep legitimation crisis that took hold over the course of the crisis and that eventually exploded in the rebellion of December 2001. Insofar as any real pressure was exercised it was therefore the *structural* pressure of a withdrawal of foreign financing and the *popular* pressure of a withdrawal of loyalty from the government and the state. Both were manifestations of the collective agency of different social forces, more than the instrumental power of specific interest groups.

A similar response could be made to the constructivist view, which would emphasize the importance of norms, narratives and ideas about the crisis, its causes and possible solutions. Again, the chapter has not sought to dispel the importance of such factors; it has actually shown how, as in Mexico, there were different ideas on how to resolve the crisis from the very start. From the elections of 1999 onwards, Duhalde's narrative, for instance, always revolved around the idea that ordinary citizens were not to blame for the government's fiscal problems and should not be made to pay for the irresponsible lending of US investors. Advocating the idea of a unilateral cessation of payments, Duhalde clearly broke with the prevailing international norm of debtor compliance – and he paid for it dearly, as voters were swayed by De la Rúa's and Cavallo's argument that such a default would have catastrophic consequences for the Argentine economy. Still, the battle of ideas continued to rage throughout the crisis, with social movements stepping up their struggle against orthodoxy and proposing their own heterodox or radical alternatives. In the background, there was always a belief among large sections of society and parts of the political establishment that a more heterodox and national-popular exit from the crisis, in the form of a unilateral moratorium on debt payments, would be a preferable option.

Yet, as the chapter has also tried to show, these ideas did not hover in a vacuum. In the early years of the crisis, orthodox ideas about fiscal policy and market reform gained the upper-hand because these were the same ideas that foreign investors had. These investors, in turn, did not just have an abstract intellectual attachment to these ideas; they believed in them because they had a vested material interest in them: "responsible" fiscal policies freed up resources for debt payment while convertibility, liberalization and privatization allowed for much greater foreign penetration into domestic markets. Given the growing dependence on foreign credit and investment, it was precisely those who shared the investors' material

interests and ideological predilections for austerity, reform and debt repayment who found themselves strengthened in the immediate lead-up to the eventual default; once again, the appointment of Cavallo is a clear case in point. It was not until the rupture of December 2001 that more heterodox ideas made their way into the mainstream – the reason being that these less conventional ideas were much better suited at pacifying an increasingly restless population and providing material concessions and rhetorical distractions to restore a sense of political stability in the midst of a deep legitimation crisis. Again, as in the Mexican case, ideas played an important role, but not in isolation from the underlying power relations and the social and political struggles over who was to bear the costs of adjustment.

Argentina's default proved to be the explosive conclusion to the second major international lending cycle of the postwar period. It was followed almost immediately by a third lending cycle, spurred on by historically low US interest rates in the wake of 9/11 and the dotcom bust, and a commodity boom emanating from China. As with the preceding cycles of the 1970s and 1990s, this third credit expansion quickly turned to bust, provoking a bout of major market turmoil. Unlike in previous crises, however, the financial crisis of 2008-'09 was centered on the advanced capitalist core – initially the US subprime mortgage market – and spread from there to Europe, where by 2010 it unleashed the most severe international debt and currency crisis since the Great Depression – except this time without the wave of unilateral defaults. It is to this most recent episode that we turn next.

CHAPTER VI:

The Specter of Solon

Greece (2010-'15)

Introduction

The European debt crisis of 2010-'15 has rekindled long-standing debates about the power of creditors and the quality of national democracy under conditions of financialization and European integration. Centered on a small country representing just 2 percent of the EU's total economic output, the crisis nevertheless roiled global financial markets over fears that a Greek default could undermine the stability of the European banking system and call into question the country's place within the single currency, thereby threatening to unravel the very fabric of the monetary union. As the debt crisis deepened, the EU creditor states – together with the ECB and the IMF – organized the largest international emergency loans in history, including three successive bailouts for Greece (in 2010, 2012 and 2015), in order to ensure continued repayment. Yet in spite of these bailouts, or precisely because of the onerous conditions attached to them, the Greek economy went into free-fall and the country entered a deep depression from which it has yet to recover. Losing a third of its

economic output and with a quarter of its population out of work, Greece has experienced one of the most severe contractions of any advanced capitalist economy during peacetime – with all the attendant social and political consequences.

Yet despite these high costs of austerity and debt repayment, successive governments of different political orientations have consistently rejected unilateral action on the debt and have pursued orthodox structural adjustments instead. Even the election of the leftist Syriza party, the formation of an anti-austerity government and the resounding rejection of the creditors' terms in a 2015 referendum did nothing to change policy outcomes. What, then, explains this remarkable degree of debtor compliance? Much of the debate has centered on the question of Greece's euro membership, which certainly appears to be a crucial factor. Still, as this chapter aims to show, a narrow focus on the euro risks obscuring some of the more fundamental power dynamics at the heart of the debtor-creditor relation; something past debt crises in the Global South have done much to elucidate. The following case study builds on the insights derived from the previous two case studies and demonstrates how Greece has been confronted with remarkably similar enforcement mechanisms as Mexico and Argentina. Eurozone membership, far from setting the Greek crisis apart from past international debt crises, has served to both *entrench* and *amplify* existing structural power relations by removing monetary policy autonomy and rendering Greece acutely dependent on a "foreign" central bank for liquidity provision to its domestic banking system.

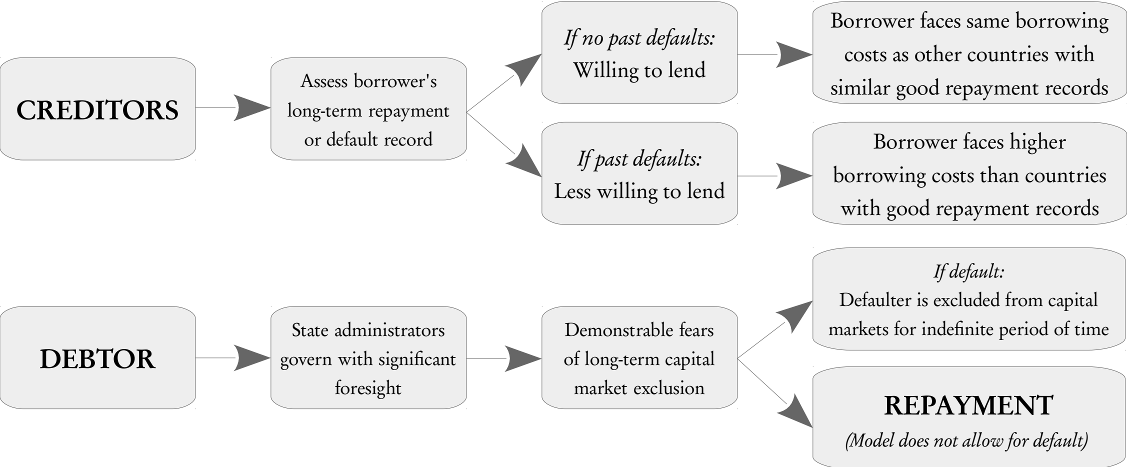
A unilateral default was therefore systematically disincentivized not just because it would immediately bring about an exit from the Eurozone, but because it was likely to result in Greece's official lenders pulling the plug on further credit and liquidity provision, thereby unleashing debilitating short-term spillover costs that would ripple throughout the

financial system and wider economy. Since these spillover costs would disproportionately affect wealthy elites – and since they scared whatever remained of the middle class – there was a concerted effort on the part of the Greek establishment, whose interests and ideology were closely aligned with those of foreign creditors, to prevent a default from taking place. Despite the uniqueness of its Eurozone membership, then, the Greek case displays a remarkable degree of similarity to other post-1982 debt crises. The main puzzle this chapter seeks to address is what sets Greece apart from Argentina: why did the latter default while the former did not? Both countries experienced deep legitimation crises and large anti-austerity protests, and both eventually witnessed the ouster of pro-austerity establishment politicians and the rise of an anti-austerity coalition. So why did Greece not default?

This chapter is structured like the previous ones. The first part weighs the evidence for the conventional hypotheses of debtor discipline; the second looks at the hypothesized enforcement mechanisms; and the third considers the actual outcomes of the crisis, concluding with a short word on possible alternative interpretations of the evidence.

Reputation Hypothesis

Figure 6.1 – reputational mechanism:



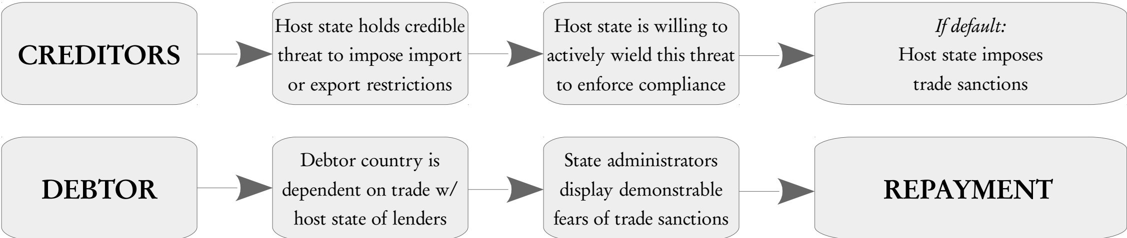
As in the Mexican and the Argentine cases, the original reputation hypothesis would lead us to expect two things. First, given Greece's history of default, we should observe a significantly higher risk premium in Greece than in other European countries without such a history of default.[38] Second, we should observe concerns among policymakers of the long-term consequences of default for the country's access to foreign credit, which would in turn require Greek officials to govern with considerable foresight. On both counts, the evidence suggests the opposite to be the case. First, despite having spent about half of its existence as an independent country in a state of default, Greece notably borrowed on almost the exact same terms as Germany as late as 2008, its spread only rising above 1 percent following the collapse of Lehman Brothers and the Wall Street meltdown. It was not until the rescheduling of Dubai World's debts in November 2009, and after incoming Prime Minister George Papandreou announced that the previous government had cooked the books – with the help of Goldman Sachs – and that Greece's deficit and debt load were in fact much higher than previously thought, that the German-Greek risk spread began to widen dramatically (Gibson, Hall and Tavlas 2011:9-10). This appears to indicate that lenders did not take into account Greece's reputation as a “debt intolerant” serial defaulter that has spent a total of 90 years in default; rather, they based their investment decisions on short-term risk assessment. In fact, for years investors appeared to reason that all debt in the Eurozone carried more or less the same default risk. As a result, Greece, with its perceived high growth potential, developed into an investor favorite, just like Mexico and Argentina had before it, and began to attract large amounts of cheap credit in spite of its poor repayment record – which is the exact opposite of what the reputation hypothesis would lead us to expect.

38 After contracting its first loan during its war of independence, Greece instantly defaulted. It contracted a new set of loans in the 1880s, but defaulted again after the Greco-Turkish war of 1897, leading to financial control by the Great Powers. It defaulted again during the Great Depression (see Borchard 1951).

Second, it was not just the lenders who were myopic and exuberant with respect to the risks involved; Greek officials were just as shortsighted when it came to the long-term sustainability of the debts they were taking on. As the crisis deepened, IMF staff began to quietly sound the alarm bells about Greece's ability to repay its debts, but the government did not heed their warnings. Former Deputy Director of the IMF's European Department Susan Schadler (2013:11) recounts that "Greek officials perceived the [IMF's] doubts [about debt sustainability], but their attention was focused almost solely on whether the near-term amortization schedule would be met, not on whether the debt trajectory would be compatible with renewed market access a few years out." This observation similarly contradicts the reputation hypothesis and fits with the theme of investor and policymaker myopia that emerged from the previous case studies. The creditors, narrowly concerned with short-term bond yields, lent without taking into account Greece's past repayment record, while Greek officials repaid not because of long-term considerations about their country's future creditworthiness but due to fears over the immediate consequences of default.

Sanctions Hypothesis

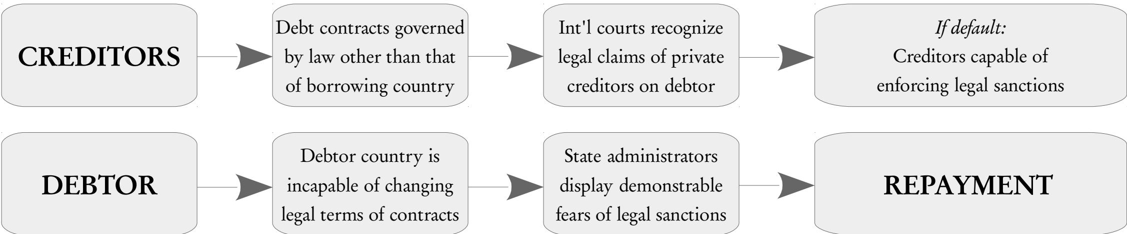
Figure 6.2a – trade mechanism:



The sanctions hypothesis would lead us to expect explicit or implicit threats of trade or legal sanctions, as well as a demonstrable concern among policymakers of such sanctions

being imposed. Yet trade sanctions are unlawful under EU treaties on the free movement of goods within the single market, and this investigation did not uncover evidence that the Greek government feared their imposition by the other European creditor countries. When Greece briefly went into arrears on the IMF, no such sanctions materialized, and it is highly unlikely they would have materialized even in the event of a full default.

Figure 6.2b – legal mechanism:



In terms of legal sanctions, the evidence also points in the opposite direction. As Buchheit and Gulati (2010:2) pointed out early on in the crisis, "from the legal standpoint, the salient feature of Greece's bond debt is that approximately 90% of the total is governed by Greek law." This means that, if Greece had wanted to default, legal sanctions would not have been able to stop it from doing so: it could have simply changed the laws governing the majority of its bonds, leaving bondholders unable to sue the government in any court – Greek or foreign. For this reason, an Allen & Overy (2012:11) report points out that, from a legal point of view, Greece held "quite a good card" when the debt crisis first broke out. Faced with unaffordable interest rates, it could "ultimately impose a unilateral rescheduling on its creditors simply by passing a statute. This statute would, subject to various qualifications, be recognised in the courts of most developed countries since creditors who contract under local law take that system of law as it is from time to time." If legal sanctions had truly been the decisive enforcement mechanism of Greece's compliance as a debtor, the abi-

lity of the Greek government to disarm this mechanism simply by changing its laws would lead us to expect a Greek default, which did not materialize.

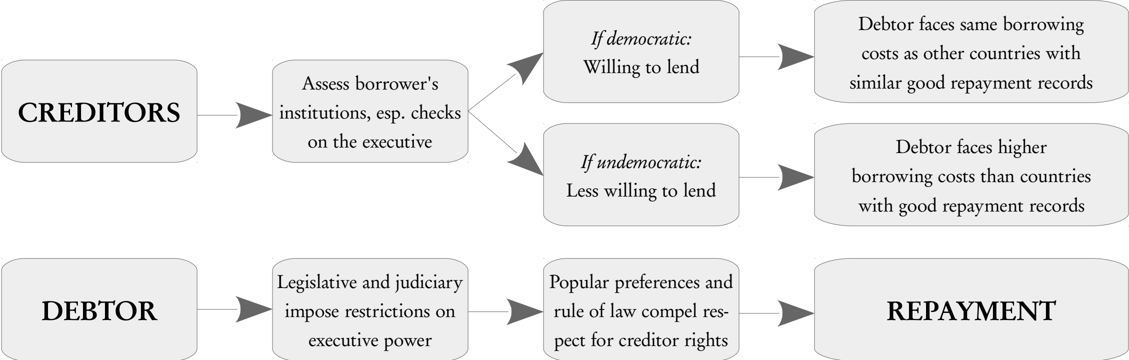
Another type of sanctions that is never brought up in the sovereign debt literature but that nonetheless could be argued to have played an important role in the Greek debt crisis is *monetary* sanctions – or more specifically, the credible threat by official European creditors to expel Greece from the Eurozone (see Kirshner 2005). It should be emphasized that there are no formal provisions allowing Eurozone leaders to remove another member state, but there are ways in which a disorderly Greek exit (or "Grexit") from the Eurozone could have been forced by the European Central Bank simply by withholding much-needed liquidity from the banking system. This would have led to a collapse of Greece's four systemic banks and the need to recapitalize them, followed by an injection of fresh liquidity into the domestic economy – a set of measures that the Greek government would not have been able to undertake without reasserting control over its central bank and introducing its own parallel currency (initially in the form of scrip or IOUs, later in proper coin and notes) that would eventually come to replace the euro as *de facto* means of payment. A convincing case could therefore be made that Greek policymakers feared the implicit threat of monetary sanctions throughout the crisis, even before the game of brinkmanship between Syriza and the Eurogroup made such threats explicit in 2015. Given the lack of legal provisions for expulsion, however, the execution of this threat – whether implicit or explicit – would by necessity have to operate through *informal processes* of liquidity asphyxiation; a mechanism that lies firmly within the domain of the structural power hypothesis. After all, the only way for the European lenders to pursue their ultimate monetary sanction of a forced Grexit would have been through the *strategic use* of their systemic privilege,[39] namely their capacity

39 For a theoretical clarification on the *strategic use* of structural power, see Culpepper and Reinke (2014).

to deny further credit to the Greek government and withhold liquidity from Greek banks, thereby indirectly forcing an outcome they could not pursue in a more overt manner. The reason Greece would fear such an "ejection by stealth" has little to do with the instrumental power of monetary sanctions *per se* and everything with the structural power of the ECB, whose capacity to withhold emergency liquidity assistance from Greek banks and cut the Bank of Greece off from the TARGET2 interbank payment system would instantly leave Greece incapable of attracting foreign financing, thus triggering debilitating spillover costs.

Democratic Advantage Hypothesis

Figure 6.3 – institutional mechanism:



As in the previous two cases, the democratic advantage hypothesis would lead us to expect Greece's compliance to be the result of significant legislative and judicial checks on the executive, limiting the latter's ability to act unilaterally and compelling it to credibly commit to "creditor rights." As in Argentina, however, the evidence suggests the opposite, with the credibility of Greece's commitments strengthened not by limits on the executive but by "an extension of autocratic executive power" (Watkins 2014:14). Indeed, as the crisis deepened, subsequent Greek governments increasingly resorted to emergency decrees and executive edicts to bypass parliament and neutralize widespread opposition to austerity and

reform. Prior to the 2015 elections, Dalakoglou (2014) remarked that "for the last two years Greece has been governed almost exclusively with decrees that were designed to be emergency provisions for use in extreme cases such as war or natural disasters. Since June 2012, twenty-five [such decrees] have been issued. Hardly any of the major structural adjustment measures were approved by the normal parliamentary process." This tendency intensified with the deepening of the social and economic crisis, which led to an increasingly unilateral approach by the executive. In 2013, the *New York Times* reported that Prime Minister Samaras "stepped up his use of emergency decrees and edicts to impose changes that other political parties and Greece's unions have a long history of trying to thwart," including edicts to prevent and end strike actions by schoolteachers, seamen and metro workers, as well as executive decrees "imposing stricter supervision on ministries and state bodies."

At the same time, many long-standing constitutional provisions – especially those guaranteeing labor and pension rights, the minimum wage and collective bargaining – were aggressively dismantled at the orders of the Troika and the behest of private creditors, who at times openly expressed their opposition to the legal protections afforded by the post-dictatorship settlement. In one report, J.P. Morgan (2013) complained that the constitutions of the Southern European countries display too much of a "socialist influence," with "weak executives; weak central states relative to regions; constitutional protection of labor rights; consensus building systems that foster clientelism; and the right to protest if unwelcome changes are made to the political status quo." Many of these provisions were important checks and balances introduced to reduce the power of the executive after the dictatorship; rather than asking for these limits on the executive to be strengthened in order to improve Greece's ability to credibly commit to its obligations, the creditors wanted such provisions weakened. As a result, the legislative increasingly became sidelined as the crisis deepened.

Douzinas (2013) has noted that "the loan and memorandum agreements imposed taxation increases and savage pension and salary cuts before they reached Parliament, which was reduced to the role of rubber-stamping a *fait accompli*." To give some concrete examples: an emergency act passed along with the first memorandum of understanding in 2010 (s.1.4 law 3845/2010) provides government ministers with a "*carte blanche*" to "issue executive decrees which can cover all aspects of economic and social policy, repeal pre-existing laws and sign further binding agreements giving away parts of national sovereignty without Parliamentary approval." Another act (s.1.9 law 3847/2010) states that memorandums and agreements with foreign creditors become binding upon their signing and "are introduced in Parliament later just for 'debate and information'" (both cited in Douzinas 2013).

A further challenge to Greece's democratic institutions arose in the wake of two fateful announcements – the first by Prime Minister Papandreou on October 31, 2011, the second by Prime Minister Tsipras on June 27, 2015 – that they would be holding referenda on the terms of the second and third bailout agreements, respectively. Both were met with fierce opposition from the European creditors, who first tried to prevent the plebiscite from taking place, then tried to impose the question, and finally – in the 2015 referendum – tried to influence the vote by threatening Grexit in the event voters chose the "wrong" outcome. After the announcement of the first referendum in 2011, European Commission President Manuel Barroso reportedly told Greek Finance Minister Venizelos that "we have to kill this referendum," to which the latter "agreed almost immediately." The response to the second referendum in 2015 was to instantly limit the amount of emergency liquidity assistance (or ELA) available to Greek banks, forcing the government to close the banks and impose far-reaching capital controls in the face of an incipient bank run. In both cases, yields on Greek bond spiked dramatically following the announcement of the plebiscite – on the Monday

after Tsipras' announcement in June 2015, two-year bond yields shot up 14 percentage points to 34 percent (Jolly and Bradsher 2015). Investors clearly feared that voters might object to the terms of the memorandum of understanding with the Troika, thereby undermining the executive's capacity to credibly commit to its international obligations. Better, in other words, to keep the executive shielded from democratic pressures, especially since the loan conditions determined in the memoranda were deeply unpopular with voters.

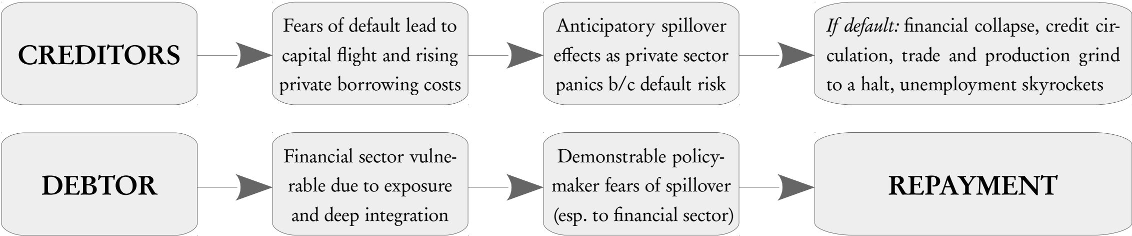
In 2012, the creditors' direct interventions in domestic politics were cemented with a set of institutional changes at the European level. As Watkins (2014:14) writes, "with debt restructuring off the table, the burden fell on 'control'." The European Fiscal Compact, in particular, was unambiguously intended to impose budgetary discipline on the deficit states of the periphery and to limit the national sovereignty of individual Eurozone members in determining budgetary priorities. Bugaric (2013:25) has observed that the treaty "basically entrenches a certain economic theory at the level of constitutional law" and notes that, "while it elevates the austerity paradigm ... to the status of 'unbreakable law', it basically outlaws Keynesianism and its counter-cyclical economic policies." Loïc Azoulai, who holds the Chair of Law at the European University Institute, has referred to the pact as a "legal monster" for its far-reaching encroachment on national sovereignty and fundamental constitutional provisions (cited in Kocharov 2012). An editorial in the *European Constitutional Law Review*, the leading journal in the field, declared that the fiscal compact "strikes at the heart of the institutions of parliamentary democracy by dislocating as a matter of constitutional principle the budgetary autonomy of the member states" (ECLR 2012:5-6). Debtor states like Greece would have to abide by the rules laid down by the creditor states. As the German Finance Minister Wolfgang Schäuble candidly put it, the Greek people "can vote however they want, but whatever election result we have will change nothing about the

actual situation in the country" (cited in Donadio and Erlanger 2012). With democracy suspended, political leaders could carry on with the more urgent task of repaying their debts.

The evidence is therefore clear on this point: Greece's creditors – both private and official – had remarkably little faith in the ability of democratic processes and institutions to ensure credible commitment. Insofar as Greece's political system, its political culture and its post-dictatorship constitution were to be reformed to ensure continued repayment, the creditors' priority was not to limit executive power but to elevate it; not to strengthen the role of parliament but to sideline it; not to defend hard-fought labor rights but to upend them; not to increase national ownership over the reform effort but to eliminate it; not to force Greek leaders to respect the popular will but to insulate them from it. And just as in Argentina, the lenders' generalized disregard for democratic processes and institutions gave rise to a deep crisis of representation inside the country, with public trust in the political system all but collapsing, a massive wave of protests, strikes and riots rocking the country, and anti-establishment parties rising rapidly in the polls. By early 2012, public trust in the government had fallen to around 7 percent and trust in parliament to around 12 percent; down from roughly 57 and 43 percent, respectively, in 2005-'06 (Exadactylos and Zahariadis 2013). Democratic legitimacy was sacrificed at the altar of the European bond market.

Spillover Costs Hypothesis

Figure 6.4 – spillover mechanism:



If the three conventional hypotheses once again fail to explain the compliance of a major debtor country in distress, then what about the spillover costs hypothesis? As in the previous two cases, the fourth explanation appears to be backed most convincingly by the available evidence. If the spillover costs hypothesis is correct, we should find demonstrable policymaker concerns over the debilitating consequences of unilateral default on the wider economy. We should also witness the materialization of anticipatory spillover effects whenever the perceived default risk rose. Given the difficulty of gaining access to policymakers' considerations, the first point is impossible to verify with certainty – yet there seems to be evidence that Greek officials genuinely feared the spillover costs of default. Greece's high degree of commercial, financial and monetary integration into the wider Eurozone made it particularly vulnerable in this respect. Like Mexico in the 1980s, Greece remains heavily dependent on imports of important goods like oil and pharmaceuticals: "It was pointed out that the hospitals would have no medicines and the lights of Athens might go out" in the event of default, as the loss of access to trade credit and the lack of foreign currency reserves would leave the country unable to pay for fuel and drugs (Allen & Overy 2012:8). At the same time, as in Argentina, Greek government officials were particularly concerned about preserving the financial system and the currency regime. After all, prior to the 2012 debt restructuring, Greek banks were exposed to government bonds to the tune of €30 billion euros and "would immediately go bankrupt" if the state defaulted (Aglietta 2012:27). The country's elite and upper-middle class were also strongly tied to euro membership, making them strongly opposed to default as this would likely result in Grexit.

We can identify at least three specific episodes during which a chaotic Greek default was widely feared by Greek officials and foreign creditors alike, allowing us to test whether anticipatory spill-over effects did in fact materialize in the face of high default risk, as the

spillover costs hypothesis would lead us to expect. In the first episode, following Papandreou's announcement on October 31, 2011 that he would be holding a referendum on the latest bailout agreement, it was reported that "world leaders fear that if Greece failed to sign on to a bailout plan that was worked out late last month, it would trigger a bank run and market panic" (Birnbaum 2011). In September and October 2011, a "bank jog" had gotten underway, with Greeks withdrawing up to €14 billion in savings and time deposits. This slow-motion bank run intensified after Papandreou's referendum announcement. George Provopoulos, Governor of the Bank of Greece, informed the Parliament's economic affairs committee that "in the first 10 days of November the decline [in deposits] continued on a large scale," bringing total savings to €170 billion by the end of 2011, down 30 percent from €237.7 at the start of 2010. When the referendum was cancelled, under intense financial and political pressure, Finance Minister Venizelos defended the U-turn by explaining it would have led to total panic: "Imagine the reaction of the markets. In three days we would have collapsed. We would never have got to the referendum because there would have been a run on the banks" (cited in Smith 2014). Deposit flight stabilized after the appointment of the technocrat Papademos, as the perceived default risk subsided (Weeks and Ziotis 2012).

A similar pattern developed in the second episode, following the inconclusive elections of May 6, 2012. New Democracy and Syriza finished the first round neck-and-neck, and when both failed to form a governing coalition, new elections were called for June 17. With Syriza polling first until mere days before the vote and the leftists openly calling for a moratorium, fear of an impending default and Grexit motivated depositors to pull out their money *en masse*. "We are talking about June 2011," one Troika official said, "when Greeks were taking about one to two billion euros a day from the banking system. And the Greeks had to send military planes to Italy to get banknotes. It got to that point" (cited in Islam

2013:4). As deposits fell to €159 billion, demand for paper money tripled, causing total cash in circulation to reach €48 billion, or 24.8 percent of GDP – an extraordinary figure given the 4-7 percent average for developed economies (*ibid.*). George Provopoulos later said that "in a matter of a few days [after a possible Syriza victory], a full-blown banking crisis could have erupted" (Spiegel 2014a). A Troika official predicted "there would have been complete and immediate panic" (cited in Islam 2013:4). In another interview, Provopoulos said that "I was much more afraid because I knew everything; I had the data in front of me. If this phenomenon had gone on, there would have been no reason but to go into a full bank run. That would have resulted in the exit of the country from the euro area" (cited in Reguly 2013). Prime Minister Papademos was so concerned about the possibility of a Syriza victory "that he remained in his office on the Sunday night of the elections to prepare for the market shock," fearing "that the constellation of election results would not allow the formation of a government supportive of the new economic programme" (Spiegel 2014a).

In the end, New Democracy won the elections and formed an uneasy coalition with PASOK, causing the risk of default to recede and depositor fears to subside. More recently, however, Greece has been going through an intensified replay of these dramatic events, this time under radically different political conditions. In anticipation of Syriza's eventual electoral victory in January 2015, deposit flight and capital flight returned with a vengeance. The economist Theodore Pelagidis relayed that "the rich and affluent have been telling their private bankers to transfer funds, and that reflects the mounting concern over how Syriza will behave after the election" (cited in Smith 2015a). In the lead-up to the snap elections, €14 billion was withdrawn from the banks, with deposits falling to their lowest level in 10 years at €155.4 billion (Chrysoloras, Ziotis and Bensasson 2015; Chrysoloras and Bensasson 2015). Capital flight continued apace as well. *The Guardian* reported that "Greek investors,

led by shipowners and other industrialists, have stepped up transfers of funds. One insider said bankers were being instructed to make multimillion-euro transfers daily" (Smith 2015). The four systemic Greek banks were forced to re-apply for the ECB's emergency liquidity assistance, with a senior banker in Athens explaining that ELA "is seen as a buffer against a growing liquidity squeeze on the banks, caused by political uncertainty over the election outcome" (cited in Hope and Wagsty 2015). In the week of the elections, the biggest four banks – Alpha, Piraeus, Eurobank and National Bank – each lost over 20 percent in market capitalization. As another Athens banker put it, "This is a massacre. Markets are panicking ... They're trying to preempt a crisis on banks' liquidity. They know the crisis will be centered around the banks" (cited in Thompson 2015).

And it was. The moment Syriza was elected, the bank jog intensified while the stock market lost a further 41.5 percent in the first quarter (Chrysoloras and Bensasson 2015). By April, total deposits had fallen to €133.7 billion, €100 billion below their 2009 peak (*ibid.*). The financial panic finally came to a head in June, when the Syriza-led government stepped up its brinkmanship ahead of a crucial cut-off date on June 30 when the previous bailout program was set to expire and an important IMF payment was due. When the bailout talks broke down on June 26 and Tsipras announced the referendum in the early hours of June 27, the slow-motion bank jog turned into a full-blown ATM run overnight. Just two days later, the ECB announced that it would not be increasing its ELA ceiling – having disbursed €89 billion in emergency loans up to that point – and the Greek government was forced to shut down the stock exchange and banks and impose far-reaching capital controls, including an ATM withdrawal limit of €60 per day and an outright ban on bank transfers abroad. On June 30, the second bailout program expired and Greece missed a €1.5 billion payment to the IMF, becoming the first developed country to ever go into arrears on the Fund.

As a result, and just as the spillover cost hypothesis would lead us to expect, Syriza's game of brinkmanship – and the lenders' aggressive decision to withhold further credit and liquidity – led to a situation in which the economy effectively ground to a halt. On July 11, the head of the Hellenic Chamber of Commerce said that "there is no system in place for Greek companies to transfer money abroad. Our life-blood has been shut off. People are depleting their stocks. We are going to start seeing shortages of meat by the end of the week ... The ferry operators are demanding cash up front to bring in fuel and supplies" (cited in Evans-Pritchard 2015a). With firms unable to pay their foreign suppliers, imports dropped and domestic production collapsed. The Purchasing Managers' Index (PMI), a key indicator of the health of the manufacturing sector, fell from 46.9 to 30.2 in July (its lowest point on record) while new orders fell from 43.2 to 17.9.[40] An economist at Markit, the private firm compiling PMI data, explained that "factories faced a record drop in new orders and were often unable to acquire the inputs they needed, particularly from abroad, as bank closures and capital restrictions badly hampered normal business activity" (cited in Hannon 2015). While the Greek economy had been projected to emerge from its depression in 2015, the European Commission estimated that it would now contract up to 4 percent as a result of the capital controls and the collapse in business confidence (European Commission 2015a; Strupczewski 2015). Still, it should be emphasized that these spillover effects were not just the result of an "apolitical" market reaction to Syriza's "irresponsible" policies; they were the ultimate political weapon in the arsenal of Greece's lenders, who – as we will see in the remainder of this chapter – wielded its power to full effect.

40 Any value over 50.00 marks an expansion of output and anything below 50.00 marks a contraction.

Enforcement Mechanisms

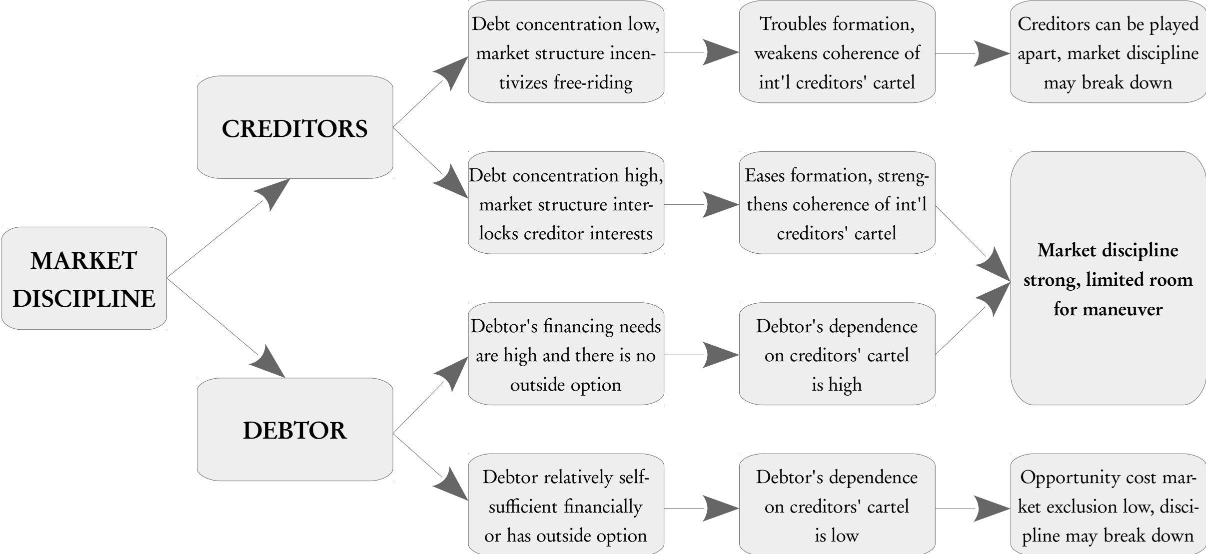
The spillover costs hypothesis is well-positioned to explain policymakers' hesitance to default. Pronunciations by Alexis Tsipras that a default and Grexit would have unleashed "catastrophe" and constituted "suicide" may have been improvident and exaggerated in view of the likely consequences of endless austerity, but they do hint at the fact that Greek officials encountered an impermeable *material barrier* to unilateral action: the barrier of severe short-term spillover costs. The ability of the left-led government and of society as a whole to breach this barrier by withstanding the economic, social and political consequences of liquidity asphyxiation depend entirely on their internal resilience and their capacity for self-reproduction under conditions of temporary autarky; a capacity that could be considered very low in Greece's case, given its dependence on key imports, foreign credit and external liquidity assistance for its banks, as well as the absence of foreign currency reserves. While certain elements in Greek society, within Syriza and even in the governing coalition itself may nevertheless have been willing to pursue a rupture with creditors, the balance of forces within Syriza, within the government and between Greece and its lenders did not appear to be in favor of these pro-default and pro-Grexit voices. It can therefore be surmised that the spillover costs hypothesis falls short by ignoring the *political* nature of crisis management as an asymmetric power struggle over the distribution of the costs of adjustment. The next section aims to bring this power struggle into closer focus.

First, at the level of international lending, we will see how Greece's debt at the start of the crisis was highly concentrated in a number of systemic and over-exposed French and German banks, whose unified creditors' cartel helped to enforce strict market discipline. Second, at the level of the international lender(s) of last resort, fears of a European banking

crisis, peripheral contagion and a catastrophic collapse of the Eurozone led EU leaders and the ECB to undertake an aggressive bailout under strict policy conditionality, with the IMF partaking as a "junior partner" to assist in monitoring and surveillance efforts and the ECB performing a crucial role as fiscal disciplinarian. Finally, we will see how Greece was extra vulnerable to the consequences of default because of the exposure of its own banks and its Eurozone membership. Combined with its reliance on EU credit, especially its dependence on ECB liquidity, this vulnerability strengthened the hand of domestic elites whose anti-Grexit interests and pro-EU ideology were aligned with those of the creditors. The combination of these factors served to enforce compliance in relatively smooth fashion up until early 2015, when a deep legitimation crisis led to the rise of Syriza's anti-austerity coalition, producing a brief breakdown of the third enforcement mechanism and forcing official lenders to strategically resort to their structural power, eventually compelling Tsipras to capitulate by refusing to disburse further credit and withholding liquidity from Greek banks.

The Financial Markets as "Global Supra-Government"?

Figure 6.5 – market discipline mechanism:



In the dark hours of the European debt crisis in late 2011, it became somewhat of a fashion among commentators from across the political spectrum to highlight the growing power of financial markets. When leaders in Greece and Italy were toppled and replaced by unelected technocrats, the *New York Times* wrote that "the power of financial markets has upended traditional democratic processes." A later piece in the same newspaper observed that "the bond market has emerged as a mighty protagonist in Europe's economic crisis, representing a seminal shift in power from politicians to investors and a relatively obscure cohort of bankers." Martin Wolf (2012) of the *Financial Times* noted that "in a big crisis, creditors rule," while investment banker Roger Altman (2011) dramatically declared in the same pages that "financial markets [are] acting like a global supra-government":

> *They oust entrenched regimes where normal political processes could not do so. They force austerity, banking bail-outs and other major policy changes. Their influence dwarfs multilateral institutions such as the International Monetary Fund. Indeed, leaving aside unusable nuclear weapons, they have become the most powerful force on earth.*

But who are these abstract "markets"? And how did they become so powerful? This section argues that, just as in the debt crisis of the 1980s, the rule of the creditors in Europe was a product of the *highly concentrated ownership structure* of peripheral debt. Research by Barclays Capital (2011) revealed that Altman's "omnipotent financial markets" were in fact made up of a small number of very powerful actors, with the ten biggest holders of Greek bonds accounting for more than half the country's debt in mid-2011, and the top-30 bond-holders accounting for over over two-thirds. The immense strength of market discipline in the European debt crisis thus appears to be a result not of efficient, self-regulating market dynamics but of the oligopolistic nature of sovereign lending. As in Mexico and Argentina, the high concentration of the debt in a number of systemically important institutions eased the formation and coherence of a creditors' cartel that could credibly threaten "a sudden

stop," or an immediate withholding of credit, thereby unleashing debilitating spillover costs with potentially dramatic consequences for the wider economy and society as a whole.[41]

So who held the debt? As in Mexico in the 1980s, at the start of the crisis in 2010-'11 Greece's debt was heavily concentrated among a handful of international banks in the main creditor countries, especially France and Germany. Greek banks and pension funds held a large share as well, while a variety of foreign institutional investors (including mutual funds, pension funds and hedge funds) also had some exposure. Crucially, unlike Argentina after its mega-swap and prior to its default, and unlike the debt crisis of the 1930s, the extent of retail (non-institutional) ownership of Greek debt was and remains small (Buchheit and Gulati 2010; Fontevecchia 2011; Moore and Hope 2014). Yet this observation still leaves us with an important puzzle: if international lending in the build-up to the European debt crisis took the form of bond finance, as it had in the 1990s and in the case of Argentina, then why did the ownership structure of the Greek debt end up resembling the highly concentrated bank loans of the 1980s more than the dispersed holdings of the 1990s? There are two possible explanations. First, the discrepancy appears to be the result of the peculiar structure of the continental European financial system, which like the Euromarkets of the 1970-'80s remains heavily bank-centered (Merler and Pisani-Ferry 2012). Second, there is the perverse incentive structure of the regulatory regime inside the Eurozone, which "does not require banks to have equity capital funding for sovereign debt – there is no capital requirement, in banking jargon – so banks accumulated these debts over many years under the assumption no additional capital would be needed" (Boone and Johnson 2012:4).

41 For the concept of "sudden stops" in the context of the Eurozone, see Merler and Pisani-Ferry (2012).

There were a number of other factors that structurally interlocked creditor interests and thereby eased the formation of a coherent international creditors' cartel. The first and most important factor concerns the exceptionally deep integration of EU capital markets, which opened up an additional line of systemic vulnerability: banks of the core were not only heavily exposed to peripheral governments but also to peripheral *banks and businesses.* As Ardagna and Caselli (2014:25) write, "due to the close links among the financial markets of advanced economies, distress of one sovereign can spill over to other sovereigns and banks. Key channels – in addition to banks' direct holdings of foreign sovereign debt – are banks' cross-border interbank exposures and banks' claims on non-financial entities in countries affected by sovereign tensions." Since the latter actors would have been the first to fold in the event of a sovereign default, European bankers and officials had every interest in the stability not just of the governments but also of the banking sectors in the periphery. The interests of European creditors were therefore intertwined across the board, making it much less likely that individual creditors would decide to free-ride against the others.

Another important factor that eased creditor coordination and strengthened market discipline was the rise of credit rating agencies and their central role as monitors of debtors' policies and creditors' assets. In recent decades, rating agencies have assumed a number of functions that had previously been firmly within the domain of the IMF. Throughout the 1980s, the Fund had fulfilled the task of a surveillance agency and a gatekeeper of private market access; only with an IMF stamp of approval – in the form of a Standby Agreement – could debtors expect to tap capital markets, and a debtor could only expect to obtain such a stamp of approval if it carried out "responsible" policies geared towards the freeing up of foreign exchange with which to service its debts. This not only gave the IMF considerable leverage over the debtors' policies; it also helped the Fund coordinate creditor action by

providing important "extra-market" signals beyond mere risk-based pricing. With the rise of the rating oligopoly from the 1990s onwards, these key functions have since been privatized by the "Big Three" agencies, whose entire business model is based on monitoring debtors and assessing their risk of default. The credit reports released by these rating agencies now serve as a private stamp of approval for continued market access. As before, a debtor will have to be seen pursuing "responsible" (creditor-friendly) policies to tap capital markets.[42]

Two developments cemented the agencies' disciplinary power: first, the fact that the ratings of the Big Three began to be actively used by central banks – including the ECB – in defining the eligibility of collateral; and second, the fact that "credit ratings were 'hard-wired' into the wider financial system through their use in financial market regulations and supervision" under Basel II and III rules (Dyson 2014:391). It is again worth noting that the process of determining market access (the force of market discipline) is not reached through "free" self-adjusting market dynamics. Unlike adherents of the Efficient Markets Hypothesis have long liked to believe, the means of determining creditworthiness is not a product of abstract price mechanisms but rather of a highly centralized and state-supported system of risk assessment that depends to a large extent on the subjective and often flawed judgments of a handful of supposedly neutral experts, in combination with the continued willingness of regulators to keep accepting these judgments as objective and meaningful.

Like the market for government bonds more generally, the credit rating industry is a highly concentrated business, with S&P's, Moody's and Fitch together accounting for 95 percent of total world market share between them. This extremely high concentration gives

42 As Dyson (2014:391) argues, "the disciplinary power of the credit rating agencies derives from the way in which the ratings that they choose to assign to states provide the signals that prompt bond and foreign exchange markets to discriminate fiscal saints from sinners."

these companies considerable pricing power and vast leverage over the governments whose various debt instruments they rate. While an agency like Standard & Poor's cannot prevent default in a direct sense, its ratings do serve to shape the incentive structure for the buying and selling of government bonds, thus providing trusted non-price signals to coordinate creditor action and prevent free-riding in the event of default, as the average investor would not want to be seen holding junk bonds. Since both investors and regulators rely on private ratings to assess default risk and determine whether a government's bonds are investment grade and can be used as collateral, a downgrade by a single agency can have far-reaching consequences for an investor's ability to hold on to these bonds and for a government's ability to access international capital markets. This dynamic of centralized monitoring and gatekeeping therefore creates a powerful additional constraint on debtors, compelling them to continuously impress “the markets” on the credibility of their commitments.

Various structural factors thus contributed to the formation of a coherent creditors' cartel that could enforce market discipline onto the peripheral debtors and compel them to pursue strict austerity measures and repay their debts. Later on in the crisis, this creditor coherence in turn found its organizational expression in the important innovation of the bondholders' steering committee that was formed ahead of the 2012 PSI debt restructuring, along with the renewed centrality of the Institute of International Finance (IIF), which had been formed in the crisis of the 1980s to defend the interests of the commercial banks and to coordinate creditor action. Together, the IIF and the steering committee helped bond-holders present a unified creditor front in negotiations with the Troika and Greek officials. A report by law firm Allen & Overy (2012:9) notes that this “was a remarkable innovation since it is believed that there has been no major steering committee for bondholders since perhaps the 19th century, although there have been steering committees for bank lenders.”

Interestingly, the steering committee explicitly "took [its] cue from the last great steering committees of international banks established in the 1980s to deal with the bankruptcy of Mexico in 1982 and many other emerging countries" (*ibid*). A direct connection can therefore be established between concentrated lending and coordinated creditor action in Mexico and in Greece. In both cases, the banks managed to prevent a unilateral default, buy crucial time to reduce exposure and build up capital, and finally coordinate an "orderly" (creditor-led) restructuring that helped them divest of devalued debt without having to accept significant losses. Needless to say, the outcomes in both countries contrast sharply to the highly dispersed holdings and the poorly coordinated creditor action in Argentina after mid-2001, which ended in unilateral default and a forceful debtor-led restructuring.[43]

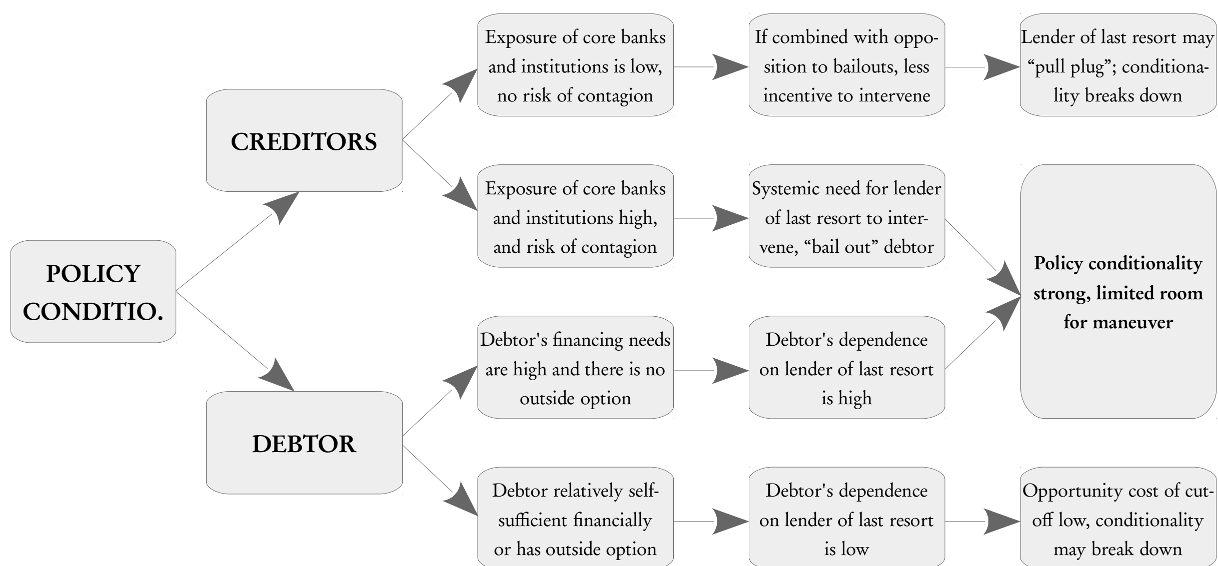
As in Mexico and Argentina, the enforcement mechanism of market discipline was most clearly on display at the start of the crisis, when Greece still had a degree of access to the bond market and greatly depended on it to make up for its widening budget shortfall. In assessing the different options that Greece had at the beginning of the crisis, Ardagna and Caselli (2014:6) point out that an early default would have necessitated even more extreme austerity than that demanded by official lenders, as the Greek government was running a deficit of over 10 percent of GDP in 2009 and of 4 percent in 2010. This meant that, in the absence of access to fresh credit, the government would have been compelled to move into primary balance immediately following a default, which made a suspension of payments a remarkably unattractive option in the first phase of the crisis. Still, a series of downgrades between 2009 and 2011 caused investors to panic, leading to rising yield spreads and forcing

43 "In the 1980s, it was possible to organise bank creditors because typically the number of really major banks involved was not more than a couple of dozen. With the re-opening of the bond market for emerging countries in the 1990s, there was no mechanism whereby bondholders were sufficiently organised to form a representative group. There were too many bondholders and some were not subject to official pressures." (Allen & Overy 2012:9).

the PASOK government to further cut spending in the vain hope of reassuring the markets. Similar patterns unfolded in Portugal and Ireland and to a lesser extent in Spain and Italy, irrespective of the partisan affiliations of those in power or the institutional specificities of the country in question. De Grauwe and Ji (2013:3) have observed that this growing market panic resulted in the imposition of "excessive austerity" on the peripheral countries, and they provide important evidence showing that "the higher the spreads in 2011, the more intense were the austerity measures." In fact, they find that "the intensity of the austerity can be explained almost uniquely *by the size of the spreads*" (emphasis original). This finding highlights the disciplinary force of highly concentrated finance not just in Greece but across Europe, and confirms the lessons learned from Mexico and Argentina. Just as in these previous crises, however, market discipline eventually risked undermining itself and would have led to default if it were not counterbalanced in time with official intervention. Again, high concentration was a necessary but not a sufficient condition to prevent default.

Troika to the Rescue? Austerity and Financial Control

Figure 6.6 – policy conditionality mechanism:



By early 2010, it had become clear that investor panic was producing a self-fulfilling prophecy, as collapsing credit ratings and skyrocketing borrowing costs effectively excluded Greece from international capital markets. With interest rates on two-year bonds breaching 12 percent in late April, Greece found it impossible to attract sufficiently affordable credit to refinance its outstanding obligations. If it did not immediately secure alternative sources of financing, the largest sovereign debt default in history loomed as early as May 19. This in turn sparked fears across European capitals of a banking crisis in the core, contagion across the periphery, and a disorderly Greek exit from the monetary union; all this in the wake of massive bank bailouts following the Lehman Brothers debacle in the United States, with the international financial system still fragile and investors constantly on edge in anticipation of the next systemic shock. Since Greece's debt stood at €300 billion, "virtually all of it in the hands of private sector creditors," there were fears that a Greek default might turn out to be that next shock (Buchheit and Gulati 2012:2). And since the principal lenders turned out to be a handful of systemic French and German banks, each "dangerously overexposed to peripheral countries," this shock would have instantly led to the collapse of some of Europe's biggest and most powerful financial institutions (Buchheit 2011:4). European leaders were therefore convinced that there could be no Greek default: the creditor governments and the ECB would rather bail out the banks indirectly, by "rescuing" Greece, than allow Greece to fail and be forced to bail out the banks directly for a second time in two years. The bankers themselves clearly shared this policy preference as it helped them avoid both the costs and the blame of another meltdown while shielding shareholders from a dilution of their equity stake that would likely accompany further capital injections by their governments.

The international effort that was eventually set up to prevent a Greek default shows some striking similarities to past crisis management in the Global South, but also a number

of important differences. The Greek “rescue” operation was similar in that it hinged on the tranche-by-tranche disbursement of large official-sector emergency loans under strict policy conditionality, combined with a staunch insistence on full and timely debt repayment and a wholesale rejection of early debt relief. It was different in that the emergency loans and the conditionality were unprecedented in their scope and severity, and in that the US Treasury Department and the US Federal Reserve played only a marginal role in their disbursement and implementation. Instead, the initiative was taken by the French and German governments, the European Commission and the ECB, while the IMF – instead of assuming the leadership function it was used to – ended up participating as a “junior partner” focused on designing the program and monitoring compliance with loan conditionality.

The biggest difference, however, relates to Greece's Eurozone membership. While Argentina had experienced a similar lack of monetary policy autonomy as a result of its convertibility regime, it always retained its own central bank and its own currency. Greece, by contrast, suffered an additional layer of dependence as its banking system relied directly on ECB liquidity provision for its survival. As we will see in subsequent sections, Greece's dependence provided the ECB with an exceptionally strong form of structural power that it wielded strategically in order to enforce compliance with the Troika's loan conditionality.

The following section will consider how these similarities and differences played out in practice. For the purposes of our analysis here, the international response can be divided into three phases. The first covers the preparations for and implementation of the first €110 billion bailout program of May 2010; the second, roughly from from early 2011 on, covers the preparations and implementation of the second €130 billion bailout program, including the PSI debt restructuring of February 2012; the third phase began, after a two-year inter-

lude following the debt restructuring, with the snap elections of January 25, 2015, the rise of an anti-austerity coalition and the six-month stand-off between Greece and its creditors over the terms of further financing and the necessity of debt relief, eventually leading to a third bailout. This section will consider the first and part of the second phase; the 2012 debt restructuring and the 2015 bailout will be considered in the final sections of this chapter.

Phase I: The First Bailout

The first phase began around February 2010, when – after an initial period of denial and insistence on the "no-bailout" clause of the Maastricht Treaty – European leaders began to openly recognize the need for emergency financing to prevent a disorderly Greek default. On February 17, a research note by Société Générale, which carried significant exposure to Greece, explained that "what seems to have galvanized minds is the realization that much of European banking is heavily exposed to Southern Europe and Greece in particular" (cited in Fuhrmans and Moffett 2010). While the opaque nature of bond finance once again makes it difficult to confirm exact numbers for individual banks, it has been estimated that over two-thirds of Greece's €300 billion debt mountain was held abroad. One analyst at Crédit Suisse said that "Greek banks own around €40bn of the total ... implying most Greek debt is sitting on the balance sheets of non-domestic banks" (cited in Treanor 2010). Moreover, as we saw in the previous section, European banks also held very large *indirect* exposures to Greece through their loans to and ownership shares in Greek banks and businesses. It has been estimated that French banks held some €60 billion in consolidated claims on Greece, while German banks held around €35 billion (Bastain 2012). Fears of contagion across the Eurozone periphery added a further element of systemic vulnerability, as major lenders like

Deutsche Bank, Commerzbank, Société Générale, BNP Paribas and Crédit Agricole carried large exposures to Southern Europe as a whole. Buchheit and Gulati (2010:6) point out the remarkable similarities with the 1980s, in this respect, as well as the notable differences with the 1990s: the "sovereign debt crises of the last 10 years or so have affected mostly non-bank creditors – hedge funds, pension funds, other institutional holders of emerging market sovereign debt, sometimes even individuals. Those crises did not threaten the stability of the banking sectors in creditor countries. A restructuring of Greek debt will, [by contrast], rekindle fretful memories of the global debt crisis of the 1980s."

Unlike the 1980s, however, there was to be no rescheduling of debts and no "bail-in" of private creditors. By May 2010, European leaders summarily swept aside the no-bailout clause in the Maastricht Treaty and agreed upon a €110 loan to the Greek government – the largest international bailout in history. The funding, provided by European governments, the ECB and the IMF was intended to cover Greece's external obligations and domestic expenditures for a period of three years, after which the country was expected to be able to return to the markets on its own. Like previous Standby Programs in the Global South, the loan was disbursed in tranches and under strict loan conditionality[44] compelling the Greek government to enact one of the most severe fiscal contractions of any developed country on record, to pursue deeply unpopular market reforms, reduce labor costs, slash pensions and unemployment benefits, lay off civil servants, and dismantle basic workers' rights like job protections and collective bargaining. As in previous programs, the policy conditions were enforced through the tranche-by-tranche disbursement of the bailout loan, always leaving

44 As Trichet put it: "Loans are not transfers, and loans come at a cost. They come not only at a financial cost; they also come with strict conditionality. This conditionality needs to give assurance to lenders, not only that they will be repaid but also that the borrower will be able to stand on its own feet over a multi-year horizon. In the case of Greece, this will require courageous, recognisable and specific actions by the Greek government that will lastingly and credibly consolidate the public budget" (ECB 2010a).

the threat of a refusal of the next loan installment hanging like a Damocles' sword over the government's head. Ardagna and Caselli (2014:13) point out that "this option of 'pulling the plug,' common to all conditionality programmes, would limit the exposure of official lenders" and left the government with little choice but to adhere to the program.

Seen in light of past adjustment programs, the rapid fiscal consolidation demanded of the Greeks was unusually tough.[45] The harsh austerity measures went hand-in-hand with a staunch refusal to consider an early debt restructuring. When Greece's Finance Minister George Papaconstantinou flew to Washington, D.C. on April 24, 2010 for an emergency meeting with IMF chief Dominique Strauss-Kahn, ECB President Jean-Claude Trichet and EU Economic and Monetary Affairs Commissioner Olli Rehn at the sidelines of the annual IMF-World Bank spring meeting, he was told the exact same thing that Jesús Silva Herzog had been told when he made the exact same trip in the fateful Mexican Weekend of 1982. As Blustein (2015:1) writes, "one message was emphatically conveyed in the meeting: there would be no restructuring of Greece's debt." Papaconstantinou himself recounts that it was said "in the most clear terms, aimed at me: 'George, do not open this issue' ... I was not a fool. I would never have opened this issue unilaterally, and then be told, in the media, that it was not an option, and have all the investors running for cover in 24 hours. It was a very delicate situation" (cited in Blustein 2015:1). As in 1982, in other words, intervention was made conditional on Greece rejecting unilateral action and maintaining its debt servicing.

From the very beginning, however, it was clear that the IMF's role in the Troika was going to be different from its role in past debt crises. While in the 1980s and 1990s the Fund

45 "There is only one precedent of a country succeeding in implementing an average annual primary deficit reduction larger than the one Greece was to undertake, and none that has achieved a comparable cumulative reduction over a similar number of years. Recall that the comparison programmes are the most aggressive on record in the OECD in the last 40 years" (Ardagna and Caselli 2014:16-17)

had – with the backing of the US Treasury and Federal Reserve – taken an active leadership role in international crisis management, the Europeans were very uneasy about such direct intervention inside their monetary union. ECB President Trichet was particularly strongly opposed to IMF involvement in the bailout, especially since some IMF officials continued to insist on the need for debt relief, which was unacceptable to the ECB. While Merkel shared Trichet's rejection of debt relief, she eventually managed to convince the ECB chief of the need for IMF participation in the bailout. Merkel insisted on IMF participation because of the Fund's unrivaled expertise in enforcing policy conditionality and monitoring compliance; the Europeans simply lacked the technical knowledge and institutional capacity to administer conditionality.[46] As Finland's Finance Minister Stubb explained after the third bailout in 2015, "we would prefer to have the IMF on board. It's not just because of its approximate €15bn-€20bn input into the [third] programme, but the credibility and tough conditionality the IMF approves in all of this" (cited in Robinson *et al* 2015). In 2010, the compromise that eventually emerged was for the IMF to participate as a "junior partner," provide part of the loan, help design loan conditionality, monitor performance and enforce compliance, but without taking complete control of the Greek economy (Blustein 2015).

This awkward arrangement was to have serious consequences for Greece. The most important was that the early calls for debt restructuring made by a number of high-ranking IMF officials were overruled in the face of staunch European opposition. Certain departments within the Fund had been convinced from the very start that without meaningful debt relief the program had little chance of success, which technically disqualified the IMF from participating. The Strategy, Policy & Review Department, in particular, was adamant

46 Blustein (2015:6) writes that "the German public ... would never accept an emergency loan unless it came with severe conditions, enforced by arbiters with recognized neutrality and competence – and the IMF was the only institution that came close to that description."

that "an IMF loan to Greece must not go simply for payments to bondholders, as it had in Argentina's case [since] giving Athens a big international rescue loan, with no haircut, would shift the burden to taxpayers" (Blustein 2015:6). But despite the misgivings of many of its economists, and despite the fact that the IMF's share of the loan far exceeded Greece's allotted quota, the Fund's management decided to press ahead with the program anyway – to vehement protests of many of its executive directors.[47] In effect, former executive director Miranda Xafa (2014:14) writes, "the debt sustainability criterion was waived based on the systematic concerns arising from spillover risks if the program was not approved."

And so the program went ahead, and – although it lagged behind on its reforms – Greece dutifully carried out the budget cuts and tax hikes demanded by the Troika. In 2010, the Greek government reduced total public spending by 5 percent of GDP. As the OECD (2011) acknowledged, "no other OECD country has achieved such a fiscal improvement in a single year over the past three decades." But the effect of this austerity was an unmitigated social and economic disaster. By 2011, it was clear that the Greek economy was contracting much faster than official IMF prognoses had foreseen (Cline 2013:2). Olivier Blanchard, the IMF's chief economist, later acknowledged that the Fund's unrealistic prognoses had hinged on a set of questionable assumptions about Greece's fiscal multipliers that underestimated the contractionary effects of the harsh austerity the IMF had helped to enforce (Blanchard

47 Brazil's executive director complained that "debt restructuring should have been on the table" and argued that the bailout "may be seen not as a rescue of Greece, which will have to undergo a wrenching adjustment, but as a bailout of Greece's private debt holders, mainly European financial institutions." Rene Weber of Switzerland expressed "considerable doubts about the feasibility of the program," asking: "Why has debt restructuring and the involvement of the private sector not been considered so far?" Executive directors from China, Argentina and several other developing countries expressed similar concerns. The IMF's minutes of the 2010 board meeting mention that "the exceptionally high risks of the program were recognized by staff itself, in particular in its assessment of debt sustainability." The minutes were leaked and published by the *Wall Street Journal* (2013).

and Leigh 2013). These incorrect multipliers were not just a product of innocent presuppositions, however; according to Susan Schadler (2013:12), former deputy director of the IMF's European Department, the multipliers were an outcome of "fundamental political pressures" that compelled IMF staff to paint a much rosier image of Greece's public finances and growth prospects than reality merited in order to be able to keep participating in the bailout program. In its review of the 2010 Standby Agreement, the IMF acknowledged that "in retrospect, the [bailout] program served as a holding operation" allowing private bondholders to reduce exposure and boost their capital ratios, "leaving the official sector on the hook" to bear the brunt of a future default or restructuring (IMF 2013). Between the first quarters of 2010 and 2011, German lenders cut their exposure to Greek government debt by $9 billion and their overall lending by $19.8 billion, while the French reduced theirs by $13.6 billion and $14.16 billion, respectively (Badkar 2011).

Phase II: The Second Bailout

Nevertheless, bank exposures were still significant by early 2011 and the collapse of the Greek economy raised the specter of a disorderly default anew. This marked the start of the second phase of crisis management, in which Greece's official lenders were to double down on their effort to enforce compliance. Despite the failure of the first bailout program to produce a swift return to the markets, the European creditors had a number of reasons to stay the course. Schadler (2013:12) writes how "several interviewees suggested that apart from domestic political considerations, one reason the Europeans did not want to commit openly to absorbing the costs of the crisis and establishing an endgame [i.e., debt relief] was that they felt it necessary to perpetuate uncertainty as a method of holding the feet of the

Greek government to the fire." While many criticized EU leaders for "muddling through" and "kicking the can down the road," in hindsight Europe's indecision appears to have been part of a deliberate strategy to buy time and allow private creditors to escape (Streeck 2014). As Ardagna and Caselli (2014:10) note, "default delayed could conceivably turn into default avoided..., and perhaps more importantly, delaying default ... would give core-country banking sectors time to reduce their own exposure to Greece."

The events of late 2011 made it clear that EU leaders were actually perfectly capable of organizing decisive action when confronted with an episode of non-compliance. When George Papandreou called a referendum on October 31, the lenders immediately responded by flexing their structural power: the disbursement of the sixth loan installment was halted until after the referendum and European officials made it clear "that the entire loan package would become obsolete if the plebiscite were to yield a negative result" (Roth 2013:21). Papandreou was summoned to the G20 summit in Cannes on November 1, where – after being publicly humiliated by his fellow EU leaders – he was told in no uncertain terms that he risked cutting his country off from all foreign credit and thereby being pushed out of the Eurozone. Finance Minister Venizelos recounts Merkel's message as follows: "either you cancel the referendum or you hold one, immediately, that asks: 'yes or no to the euro'. And after that we'll see if we'll go ahead with the [next] installment, the [bailout] program, the hair-cut" (cited in Smith 2014). Faced with this explicit threat of a cut-off of financing and an indirect expulsion from the euro, Papandreou cancelled his referendum just days later.

Beside the increasingly aggressive moves by EU leaders to force Greece back into the fold, the second phase of crisis management was also marked by an increasingly central role for the ECB. While the ECB – as we saw earlier – had already played an important role in

opposing an early IMF-led debt restructuring, its participation in the first bailout mostly took place behind the scenes. But the technocratic veneer rapidly faded as Trichet took off his gloves and the central bank became much more actively involved in managing the crisis. Dyson (2014:384) notes that the years 2011-'12 marked “a tipping point for the ECB. It embraced unlimited, three-year liquidity provisions to euro area banks [and] committed to unlimited, if conditional, intervention in sovereign bond secondary markets, despite the opposition of the German Bundesbank.” In the process, “the euro area sovereign debt crises catapulted the ECB into a broader role in crisis management” (*ibid*). The first clear signs of active ECB interventionism came in the form of a handful of letters from ECB President Jean-Claude Trichet to the finance ministers or heads of state of the peripheral countries in which he explicitly threatened to withdraw various forms of ECB support.[48] During the negotiations on the second Greek bailout in 2011, Trichet sent one such letter to George Papandreou – dated April 7, 2011 – in which he threatened to revoke a suspension of rating requirements for privately-held securities issued or guaranteed by the Greek government. Since this would have disqualified the country's four systemic lenders from using these securities as collateral for ECB loans, Trichet's letter essentially amounted to a threat to destroy the country's banking system, which depended on ECB support to stay afloat. As such, the letter provides an exceptionally incontrovertible piece of evidence highlighting the central bank's willingness to strategically wield its structural power over the Greek banking sector – and hence over the Greek state that depended on it to refinance its internal debt and keep credit circulating through the domestic economy – in order to enforce compliance with the terms of the Troika loan conditions.[49] As Xafa (2014:15) notes, “essentially, Trichet

48 The Irish, Italian and Spanish press have since released Trichet's letters addressed to their respective governments over the course of 2011.

49 Parts of Trichet's letter to Papandreou have since been published in the Greek press (see Palaiologos 2014).

informed the Greek government that even a maturity extension would lead the ECB to pull the plug on Greek banks, since they would lack appropriate collateral as well as the capital adequacy needed to access the ECB discount window. The consequence of such a move would be to force Greece to leave the euro area and print its own money."

In addition to its emergency lending to governments and its emergency liquidity assistance to banks, the ECB also organized what practically amounts to an indirect bailout of private institutional bondholders through the mechanism of its bond-buying scheme. In May 2010, the ECB governing council agreed upon the Securities Market Program (SMP), which revolved around the ECB purchasing the distressed bonds of peripheral governments on secondary markets. Since its statutes officially forbid monetary financing of member states, the ECB could not buy these bonds directly from distressed governments; what it could do, however, was to indirectly depress the interest rates on this debt by entering into secondary markets and offering to buy up the securities held by private bondholders who could not otherwise get rid of them at good prices. The ECB intensified its bond-buying scheme in August 2011, when market pressure on Spanish and Italian debt rose significantly with the escalation of the Greek crisis. Between May 2010 and September 2012, when the SMP was replaced by the Outright Monetary Transactions (OMT) scheme, the ECB purchased €210 billion in peripheral bonds, including half of Greece's outstanding obligations (Truth Committee on Public Debt 2015:24; Dyson 2014:387). The result of the SMP was to concentrate a growing share of Greek bonds on the ECB balance sheet and to turn the ECB into Greece's single biggest creditor in the short-term.[50] More importantly, SMP provided a source of demand, and hence an exit option, for private bondholders who could not other-

50 The European Financial Stability Fund (EFSF) and IMF hold a greater share of Greece's total debt load today, but the maturities of these obligations extend much further into the future.

wise reduce their exposure to Greece without taking major losses. By driving up the prices of these securities, the ECB essentially ended up subsidizing private bondholders.

Like the other ECB programs, the SMP came under strict conditionality for the borrowing governments.[51] The implication of this was that ECB bond purchases could also be *withheld*, which is precisely what happened on a number of occasions during 2011, most importantly in November when the Papandreou government in Greece and the Berlusconi government in Italy were both brought to their knees after the ECB temporarily suspended its bond-buying scheme to signal its displeasure over the inability of both governments to implement the demanded fiscal adjustments. As ECB governing council member Yves Mersch stated: “if we observe that our interventions are undermined by a lack of efforts by national governments then we have to pose ourselves the problem of the incentive effect.” When he was asked if this would involve withdrawing SMP, Mersch said: “If the ECB board reaches the conclusion that the conditions that led it to take a decision no longer exist, it is free to change that decision at any moment. We discuss this all the time” (see Jones 2011).

Combined, the ECB's three threats – to withhold its emergency loans, to withdraw its support for domestic banking systems, and to halt its secondary market bond purchases – constituted the main sticks of the central bank's structural power over peripheral debtor states. At the same time, the ECB also held an important carrot, which it tellingly reserved for its dealings with private banks. When negotiations on a Greek debt restructuring with private sector involvement (PSI) got underway in 2011, the ECB decided “to compensate the damage ... by introducing new measures in favour of the banking sector” (Panico and

51 In Trichet's words: “It is crucial that governments implement rigorously the measures needed to ensure fiscal sustainability. It is in in the context of these commitments only that we have embarked on an intervention programme in the securities markets” (ECB 2010b).

Purificato 2013:5). These took the form of two exceptional Long-Term Refinancing Operations (LTROs), allowing private banks to borrow an unlimited sum from the ECB at a fixed interest rate of 1 percent and with an unusually long three-year maturity. Both operations were heavily subscribed and allowed Eurozone banks to borrow over €1 trillion at negative real interest rates. LTRO constituted a clear indication of the ECB's pro-creditor bias: while it lent to national governments under strict policy conditionality, threatening to cut off all credit in the event of non-compliance, it simultaneously provided banks with unlimited and unconditional liquidity at interest rates so low as to effectively constitute a free handout to private investors, enabling them to engage in a lucrative carry trade between low-interest ECB loans and high-yielding peripheral debt instruments. Moreover, this cheap credit enabled domestic banks in the periphery to increase their exposure to their own governments (Dyson 2014:386). This in turn led to a repatriation of peripheral debt: as banks in the core reduced their exposure to the periphery, the ECB's interventions were loading these toxic bonds onto the balance sheets of the debtor countries' own private banks. This meant that, in the upcoming PSI debt restructuring, Greece's private banks and pension funds were to be left holding the hot potato, while EU banks had already divested of their bond holdings – a point to which we will return in the next section on the outcomes of the crisis.

The ECB's role in crisis management culminated in Draghi's famous statement on July 26, 2012 that the central bank would do "whatever it takes to preserve the euro." This statement was followed on September 6 by a governing council decision to terminate the SMP and replace it with Outright Monetary Transactions (OMT), which never needed to be activated; the sheer force of Draghi's statement and the firewall of the European Stability Mechanism and possible resort to OMT were enough to pacify bond markets and restore at least a semblance of normalcy to the Eurozone – even as the Greek economy continued its

steady decline under the austerity regime. Finally, in January 2015, the ECB announced its expanded assets purchase, or quantitative easing, program. The QE program, which would see the ECB purchase up to €60 billion in assets a month, turned out to be another mechanism for exerting pressure on national governments. Following the election of Syriza in January 2015, Draghi made it very clear that Greece's eligibility for QE would depend on its compliance, stating that "there are obviously some conditions before we can buy Greek bonds" (cited in Bensasson and Chrysoloras 2015). As before, the implicit threat was a withdrawal of ECB support in the event of non-compliance.

Given its important role in enforcing conditionality and providing free money to banks but not to sovereigns, it is perhaps no surprise that the ECB has been widely criticized for narrowly defending the interests of the creditors at the expense of the debtors (e.g., Lapavitsas 2012:3; Mallaby 2012). The question that arises, then, is why the ECB – as a nominally independent and apolitical institution – would display such a strong institutional bias in favor of private-sector creditors.[52] Here, we should insist on the fact that the ECB – regardless of whoever administrates it – is by its nature a highly politicized institution with a strong pro-creditor bias. This bias is due to the fact that its mandate blends the functions of an independent central bank, supposed to guarantee financial stability and keep inflation in check (but never to answer to social concerns about unemployment or deflation), and simultaneously that of a creditor – or a European lender of last resort – charged with enforcing fiscal discipline on its borrowers. This dual mandate directly inserts the monetary policymakers of the ECB into the fiscal policymaking of democratically accountable national governments. While these national governments are never allowed to interfere with the

52 The ECB, of course, would deny that it has such an institutional bias. As Mario Draghi himself put it, the ECB is a "rules-based institution, not a political one" (Draghi 2015).

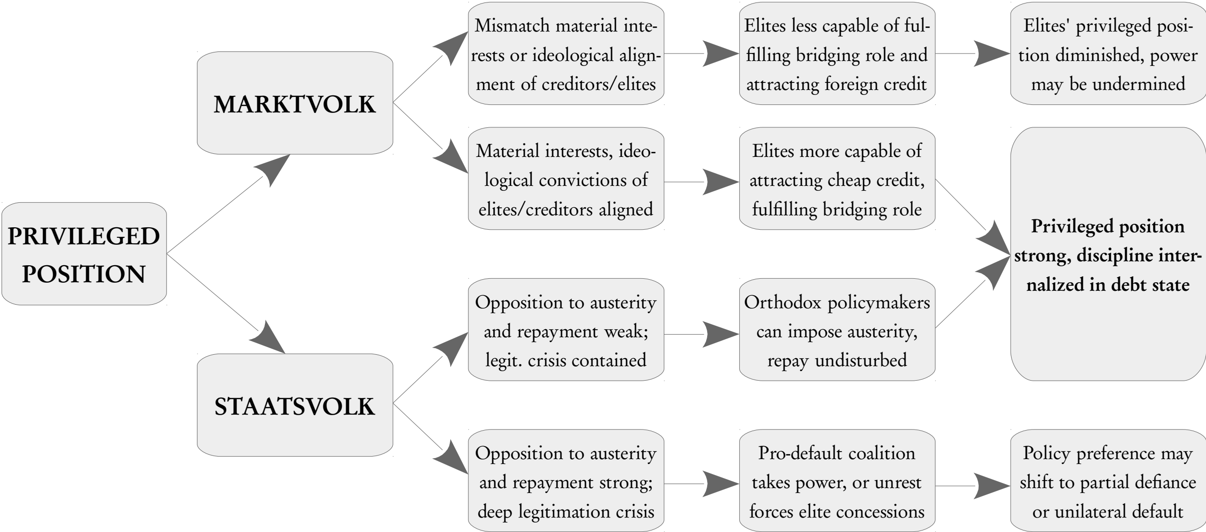
independence of the ECB, the ECB's role of a lender of last resort does frequently compel it to interfere with the independence of these governments. In other words, while the ECB enjoys significant autonomy from “political meddling” by its individual member states, the weaker member states – those that depend on the ECB for emergency financing – do not enjoy similar autonomy from “political meddling” by the ECB (see Varoufakis' discussion on this subject in a teleconference with British investors, OMFIF 2015). This asymmetry in the Eurozone's power structure is profoundly political by definition, regardless of how officials or policymakers seek to administer, justify or obscure the resultant imbalances.

Moreover, as the Eurozone debt crisis escalated and the survival of systemically important banks in the core countries and the existence of the single currency were called into question, the ECB found itself under intense systemic pressure to intervene and rescue the pillars of the Eurozone's highly concentrated financial sector, namely the “too big to fail” banks of the core countries, from the systemic risk of a Greek default. Its creditor-friendly actions and pro-creditor bias in crisis management thus followed logically from its institutional mandate to safeguard stability in a heavily concentrated and imbalanced financial and monetary system. A European Parliament inquiry on the Troika's role in the debt crisis recognized this pro-creditor bias in the subsequent bailout programs when it noted that “the protection of bondholders was seen as an EU necessity in the interests of financial stability.” The Budget Committee of the European Parliament reached a similar conclusion, adding that “we have in fact transferred the wild card from private banks to governments.”[53]

53 See: European Parliament (2014) and Libération (2015), respectively. Both are cited in the preliminary report of June 2015 by the Truth Committee on Public Debt of the Hellenic Parliament.

The "Establishment Triangle": From Compliance to Defiance and Back

Figure 6.7 – privileged position mechanism:



As in the previous two cases, a narrow reading of the first two enforcement mecha-nisms could give the impression that Greece's compliance was purely imposed from abroad. But while private bondholders and the Troika clearly played a crucial role, they could never have been as successful without the help of their allies in the Greek political and financial establishment. In fact, just as in Mexico and Argentina, the crisis resulted in a growing state dependence on credit, boosting the privileged position of those capable of attracting that credit on the best possible terms. And just as in Argentina, the Greek state experienced a deep legitimation crisis as the economic depression deepened and Troika-enforced austerity measures and structural reforms intensified. This legitimation crisis initially expressed itself in the form of fierce popular opposition in the streets, which the Greek political establishment – unlike President De la Rúa in Argentina – was initially able to withstand, although protests did produce the fall of the Papandreou government in 2011. By 2015, after five long years of austerity, support for the two dominant parties – New Democracy and PASOK – had been so thoroughly eroded that the anti-establishment Coalition of the Radical Left, or Syriza, arose to form the first radical left-led government in EU history. Syriza's defiance of

its lenders proved to be rather short-lived, however; after barely six months in power, the Eurozone had brought the leftists to their knees, forcing Prime Minister Tsipras to execute a dramatic U-turn on austerity and sign up to a third bailout.

The main puzzle this chapter seeks to address is why Greece, despite experiencing fierce popular contestation from below, culminating in the ouster of the political establishment and the rise of an anti-austerity coalition, did not go down Argentina's path of a unilateral default. This section identifies three domestic reasons for Greece's remarkable debt compliance over the past five years. First, the existence – well before the crisis – of a powerful elite constituency that has long enjoyed unrivaled privileges and that has traditionally pursued the type of orthodox policies favored by Greece's foreign creditors, albeit with an unusually high degree of corruption, cronyism and clientelism. A second reason is the fact that Greek banks were heavily exposed to their government's debt at the start of the crisis and grew even more so as a large share of Greek bonds was repatriated when the crisis deepened after 2010. The third reason relates to Greece's growing dependence on foreign credit; a development that visibly strengthened the hand of banker-friendly Greek politicians and technocrats with orthodox views and close ties to the European political, financial and bureaucratic establishment who could more "credibly commit" to servicing the debt. Crucially, unlike Argentina, the Greek establishment was never cut loose by its creditors: while the IMF may have contemplated pulling the plug on the Greek bailout program at various points during the crisis, the Eurogroup and the ECB simply stood to lose too much taxpayer money in a Greek default and so continued to support the Greek establishment in a bid to maintain at least a semblance of (creditor-friendly) political stability.

The Establishment Triangle:

Starting with the first point, it cannot be emphasized enough that austerity and debt repayment were never purely imposed from abroad: European creditors had a powerful ally in the two establishment parties – PASOK and New Democracy – that had dominated the Greek political scene ever since the *metapolitefsi* period, or the transition to democracy in 1974. These two establishment parties were in turn structurally bound to a powerful elite constituency centered on a number of oligarchic clans with roots in shipping, construction and banking that has long enjoyed privileged access to financial policymaking and that, ever since the start of the crisis, has been a mighty force clamoring for full repayment; championing austerity, market liberalization and the privatization of public property as a means of deflecting the burden of adjustment onto the rest of society. Just as Maxfield (1990) highlighted the power of a distinct bankers' alliance inside Mexico, and just as commentators in Argentina have spoken of a *patria financiera*, a similar phenomenon has been identified in Greece: Varoufakis (2013) has referred to it as an "establishment triangle" revolving around the political class, private bankers and the technocrats at the Bank of Greece. Pagoulatos (2003), who has studied the evolution of state-finance relations in Greece, observes that the country's banks have always been "run by prominent members of the political-economic elite." He also points out that the bankers are powerful not just because of their close personal ties to the political establishment; they are powerful because they fulfill "a crucial institutional role as intermediaries and distributors of developmental finance in the economy" (Pagoulatos 2003:74). The source of their power, in other words, is structural.

Just as Mexico and Argentina opened up to foreign capital under the Washington Consensus in the 1990s, so Greece underwent a neoliberal turn of its own under the nomi-

nally Socialist Prime Minister Simitis. In these years of globalization, financialization and European integration, the privileged position of the Greek banking establishment was further entrenched. As Fouskas and Dimoulas (2013:157) write, Simitis set out to create “a new type of social alliance, the 'social alliance of modernization', gathered around the 'party of the stock exchange' and unified via a complex paralegal corruption network forming a new bipartisan consensus across the trembling [fault-lines] of post-1974 Greek politics.” As a result, even if the two establishment parties alternated in office and competed fiercely on the electoral stage, the country's political reality after 1996 was completely conditioned by the fact that both were structurally dependent on private credit to maintain their systems of patronage and their networks of clientelism. Laskos and Tsakalotos (2013:30) have noted how “finance was central to both PASOK's and New Democracy's economic strategy.” In other words, behind Simitis' alliance of modernization and the dominant two-party regime, “there was a growing symbiosis of financial and political power” (*ibid*). At the same time, as the Greek banks expanded their operations into Turkey and the Balkans and entrenched their ties with European finance after entry into the Eurozone, the banking sector became deeply integrated into the continent's monetary and financial circuits and thus structurally bound up – through foreign ownership, shared investments and other linkages like holding companies and subsidiaries – with some of the country's biggest foreign creditors, investors and trading partners. These deep ties ensured that the fate of Greece's banking oligarchy and domestic elite would from now on be closely intertwined with the fate of European finance in general, providing a powerful “internal” incentive to honor foreign obligations, maintain financial stability and ensure Greece's continued membership of the Eurozone.

Domestic Exposure and Debt Concentration:

One of the most important structural ties binding Greek creditors to foreign ones was the high *domestic* exposure to government debt and its strong concentration in a small number of systemically important institutions: the biggest banks and pension funds. While it remains difficult in the case of bond finance to confirm exactly who holds the debt at any given point in time, at the start of the crisis it was generally believed that "a significant percentage (perhaps more than 30 percent) of the bonds [were] owned by Greek institutional owners" (Buchheit and Gulati 2010:6). Others put the total share lower, at €30-40 billion, but given the size of the Greek economy and financial sector even these amounts could be considered astronomical (Roth 2013:5-6). Research undertaken by Manolopoulos (2011) for Marfin Investment Bank found that, in the spring of 2010, the holdings of the National Bank of Greece amounted to 88.6 of its investment portfolio; for Piraeus this share was 83 percent, for Eurobank 97.1 percent, for Postbank 98.5 percent, for Alpha Bank 87 percent, for the state-owned AteBank 75.6 percent, and for Emporiki Bank, then still owned by Crédit Agricole of France, 83.2 percent (Fouskas and Dimoulas 2013:153-4). Moreover, in late 2012, the top five commercial banks in Greece accounted for 70 percent of the domestic liquidity market, which meant that the collapse of any of these institutions would have had dramatic spillover effects on the provision of credit to businesses and households (*ibid.*).

On top of this, something very significant happened as the crisis deepened in 2011: while banks in the core countries divested themselves of peripheral bonds, holdings steadily migrated towards the balance sheets of banks and institutions in the periphery, increasing domestic debt concentration, heightening overall financial vulnerability in these countries, and entrenching the privileged position of domestic bankers. Brutti and Sauré (2014) show

that Greece's debt was repatriated during the crisis: as inflows from abroad declined, Greek banks reduced their foreign investment and started buying more of their own government's bonds.[54] This development appears to fit a broader pattern across the Eurozone: data show that "holdings of government debt by non-residents have diminished in proportion for all the countries in trouble (Greece, Ireland, Portugal, Spain and to a lesser extent Italy), while more or less stable for France and the Netherlands, and increasing for Germany" (Merler and Pisani-Ferry 2012:4). This reflects, on the one hand, risk aversion on the part of foreign investors, and on the other a growing dependence of the government on its own financial elite. A recent paper co-authored by some of the world's leading experts on sovereign debt explains that this process helped prevent a unilateral default and, for a while at least, even forestalled an orderly renegotiation, as "any significant restructuring of the government's debt [would have led to] a domestic banking crisis" (Buchheit, Panizza *et al* 2013:25-26). The authors note that "domestic banks are relatively immune from restructurings because they expect to be recapitalized, for financial stability reasons, if their losses from domestic sovereign bond holdings are sufficiently high. Indeed, if the holdings of the banking system as a whole are high enough, the restructuring will likely not happen at all" (*ibid*). The same could be said of a unilateral default: if the holdings of the banking system are high enough, a unilateral suspension of payments is unlikely to happen in the first place.

The result was a dynamic not unlike the one previously observed in Mexico, where the domestic bankers' alliance grew stronger as the crisis deepened at least in part because the government increasingly depended on domestic investors to refinance the *internal* debt. As in Mexico, where the foreign holding companies of Mexican banks acted as interme-

54 Brutti and Sauré (2014:6-7) explicitly position their "secondary markets" hypothesis – based on previous work by Broner, Martin and Ventura (2010) – as an answer to the traditional "enforcement problem" of sovereign debt, highlighting the importance of high domestic debt concentration in preventing default.

diaries for foreign bank syndicates, making it impossible to default on one without defaulting on the other, the Greek government was similarly constrained in its ability to default on German and French banks because the anonymous nature of secondary bond markets made it impossible to discriminate between domestic and foreign creditors. This provided the government with a strong incentive to simply accept the bailout deal it was offered by European lenders, even if this required painful adjustment and risked undermining popular and electoral support in the long run. The alternative – to default on all outstanding debts – would have led to a collapse of the country's systemic banks, the implosion of the domestic financial system and a forced exit from the euro, all with dramatic consequences for overall economic performance – at least in the short-term. As we saw earlier, this logic appears to confirm the spillover costs hypothesis and disprove the theory that the state's long-term market access was the most important factor in enforcing compliance. After all, Greece was effectively excluded from international capital markets anyway and by 2014 had established a primary surplus of 2.7 percent of GDP, removing its dependence on foreign creditors for the financing of current government expenditures. The reason Greece did not default – and even refused to do so under a nominally radical left anti-austerity government – shows that there are greater forces at play than the government's access to capital markets alone; the most important of which appears to be the vulnerability of the country's banking system and its membership of the single currency, combined with strong material and ideological opposition to default among the country's financial elite. Indeed, it is now evident that the domestic banks remained Greece's Achilles' heel throughout the crisis.

Rise of the Technocrats:

Apart from the two factors discussed so far – the long-standing privileged position of an "establishment triangle" and the dependence of the Greek state on its domestic banks – there was a third internal reason for the government not to default: the growing influence of political leaders and technocrats who maintained close ties to EU officials and the international financial establishment, who held strong orthodox views on economic policy, and who were adamant to avoid Grexit at all costs. Papandreou, himself the scion of a political dynasty, fell well within this clique, but as the protests against austerity intensified, a schism emerged between Papandreou and his Finance Minister, Evangelos Venizelos, who made no secret of his ambitions to obtain the party leadership. After two years of sustained protests, it was clear that public trust in Papandreou and the democratic legitimacy of the country's political institutions more generally were rapidly evaporating. By mid-2011 Greece began to eerily resemble the equally ungovernable Argentina of a decade before (Hawley and Allen 2011; Walker and Kakaounaki 2012; Douzinas 2013:102; Mason 2013:99; Lynn 2011:7).

The Papandreou government initially managed to face down a bout of mass protests in May and June, but it was immediately confronted with another wave of demonstrations in October. During a national holiday celebrating Greece's rejection of Mussolini's ultimatum on October 28, 1940, protesters disturbed a military parade by marching through the procession of soldiers towards the stand of dignitaries, forcing the President of the Republic to make a hasty and humiliating retreat. The media widely reported the incident as the ultimate degradation of the national honor and a sign that the legitimacy of the state had sunk to previously unimaginable lows. Kouvelakis (2011:18-19) notes that "a symbolic threshold had been crossed ... It was in response to this situation that a shaken Papandreou

suggested his high-risk referendum initiative" (see also Roth 2013:21). As a government aide confided, "George has decided to go over everyone's head and take it to the people. To do otherwise would have meant death to the political system and economy by a thousand slices. No country could go on with strikes and protests on such a scale" (cited in Smith 2011). Papandreou himself explains that "everybody was saying that the government [were] traitors. I realised the situation was getting out of control" (cited in Spiegel 2014a).

In hindsight, the Prime Minister's risky call for a plebiscite can be seen, in a way, as analogous to the bombshell announcement by President López Portillo of Mexico in late 1982 that he would be nationalizing the country's banks: both were desperate gambles for resurrection by center-left leaders who were rapidly losing control over their countries and who felt compelled by greater forces to make a dramatic last stand to save their political legacy. And just like López Portillo's bank nationalization, Papandreou's referendum call ended up backfiring disastrously. Four days later the idea had been shelved – and within a week Papandreou had ceased being the country's Prime Minister. Remarkably, however, Papandreou's resignation did not give way to chaos and default, as De la Rúa's resignation had in Argentina. An important question we should answer, then, is why the mass protests in Greece between May and October 2011 did not produce an "Argentina-style" outcome – the defeat of the bankers' alliance and the rise of a pro-default coalition – but rather had the opposite effect of Mexico's failed bank nationalization: the defeat of the center-left and the ultimate victory of the bankers' alliance.

The short answer proposed here is that, unlike in Argentina – where De la Rúa and Cavallo were completely cut off by a weakened IMF and a disinterested, inward-looking and *laissez-faire*-oriented US government – the Greek establishment triangle was still actively

supported by the Troika and its European partners, who continued to exert strong pressure on Greek officials while maintaining the prospect of future financing. Unlike Argentina's popular explosion of December 19 and 20, which occurred *after* the vast majority of US institutional investors had already shed most of their exposure and the IMF had already withheld its last credit tranche following its decision that an Argentine default would be inevitable and relatively harmless, the Greek anti-austerity revolt occurred at a time when Europe's big banks were still heavily over-exposed to Greek debt and would have very possibly required another bailout (the second after 2008-'09) in the event of a Greek default. Since this was politically unpalatable to the European creditor governments, the Eurozone's preference was to continue with the Troika bailouts, which required reliable pro-creditor partners inside the Greek government, capable of credibly committing to the country's financial obligations. Given the structural dependence of the Greek state on foreign credit and the lack of political representation of the anti-austerity coalition that had now taken control of the streets, European creditors did not encounter great difficulties in locating and imposing such partners from abroad. Put simply, the reason Greece did not go the way of Argentina in 2001 is that – even if Papandreou himself lost their backing – the Greek establishment triangle retained the support of international creditors and Greece was never cut loose from its emergency credit lines as Argentina had been.

Far from helping to build national unity around the reform and stabilization effort, Papandreou's democratic brinkmanship ended up isolating the Prime Minister within his own party. Kouvelakis (2011:25) has noted how "domestically, Papandreou's gesture – followed swiftly by direct pressure from European lenders – indirectly strengthened the hand of the 'Internal Troika' faction of PASOK [whose leaders included Anna Diamantopoulou, Andreas Loverdos and Giannis Ragousis], who immediately rejected the idea of a referen-

dum and instead called for a government of 'national unity'." The more orthodox Finance Minister Venizelos, who gained the lenders' preference over Papandreou, found his position strengthened as well. When the two PASOK leaders were summoned to the G20 meeting in Cannes, those present noted that the Prime Minister "visibly deflated as the fight [with EU leaders] continued. As [Papandreou] fatigued, Mr Venizelos took up the battle, a sign many saw as the sudden realisation by the Greek prime minister that he had become a spent political force – and Mr Venizelos, who had long coveted the premiership, was moving to exploit the change in circumstances" (Spiegel 2014a). The European Commission President Barroso approached Venizelos at the gathering and agreed with the Finance Minister that the referendum had to be "killed." As soon as this alliance between Venizelos and European lenders was forged, Papandreou lost control over his own governing party. In discussions with aides, it was later revealed, Barroso personally handpicked former ECB Vice-President Lucas Papademos to head a technocratic government of national salvation with the backing of Samaras' New Democracy and Venizelos himself as Finance Minister and PASOK's new leader (*ibid*). As Kouvelakis (2011:26) writes, "thus the way was paved for the formation of a government headed by the banker Papademos – the natural incarnation of a ruling bloc that is entirely dominated by the interests of European finance."

The rise of Papademos himself closely mirrored that of the pro-creditor technocrats in Latin America in previous decades. Like Cavallo and Silva Herzog, Papademos was seen as capable of enhancing the credibility of Greece's commitment to its financial obligations and hence seeing to the state's deep dependence on foreign credit. As Laskos and Tsakalotos (2013:92) write, "Papademos was chosen for his technocratic prowess and his affinity with financial markets" and he was "a favourite of both the Troika and important business and media interests within Greece itself." In a telling sign of his loyalties, one of the first public

statements by the new unelected prime minister was an opinion piece published in the *Financial Times* in which Papademos (2011) explicitly opposed the idea of a 50 percent hair-cut of Greece's privately held debt; a much more extreme position than that of the German government, whose proposal for a 50 percent write-down eventually prevailed in the debt restructuring of February 2012, when German banks had already reduced the bulk of their exposure. Tellingly, Papademos' article stressed the spillover costs of a potential default on Greek banks, investor confidence and the wider economy: "the adverse consequences for Greece of 'hard', involuntary debt restructuring and a sovereign default are not limited to the costs of recapitalising domestic banks and supporting pension funds. The effects on confidence, the liquidity of the Greek banking system and the real economy are likely to be substantial, though difficult to predict and quantify."

Apart from strengthening the "internal Troika" and giving rise to a technocratic government, Greece's continued dependence on foreign creditors also greatly strengthened the position of the Governor of the Bank of Greece, George Provopoulos, who was himself a former CEO of Emporiki Bank and later Piraeus Bank. A *New York Times* report noted that "few hold as much power within their own country as [George Provopoulos], who has played a crucial role in keeping Greece out of bankruptcy and in the euro zone" (Thomas 2013a). The waxing influence of the central bank within the establishment triangle was a direct outcome of its control over the flow of credit through the economy and its central role in keeping Greece's *private* banks – the state's principal creditor after 2011 – afloat. As Thomas (2013a) writes, "for decades, political influence in this country has been a direct function of a politician's ability to borrow and spend, with local banks, as the main buyers of Greek government bonds, acting as the primary facilitators. Under an austerity regime, such an approach is no longer possible. And as governments have come and gone ..., the

power of the Bank of Greece's governor has only solidified." Thus, in the first years of the crisis, the establishment triangle further strengthened its hold on financial policymaking.

Counterarguments:

These observations differ in several important respects from the conclusion reached by Pagoulatos (2014), who argues that Greek bankers had structural power and enjoyed a privileged position in policymaking during the credit-fueled consumption and construction boom of 2001-'08, but lost their power and privileges with the deepening of the crisis after 2009. Pagoulatos' (2014:452) main argument is that the "fiscal failure of the sovereign and the current account imbalances of the euro area" created a set of structural limitations under which "the banks cannot escape the confines of their sovereign," thus circumscribing the bankers' power. While this is true, the conclusions he draws from this is problematic.

First, it is based too narrowly on the capital mobility hypothesis of the globalization literature, which holds that high mobility provides bankers with an exit option – the main source of structural power – whereas low mobility erodes this power. But while capital mobility, as we already saw in Chapter II, is undoubtedly a key source of the structural power of finance, it is not the only one. For as long as nation states have depended on "the private management of public debt," creditors – whether mobile or immobile – have enjoyed a privileged position in financial policymaking (Dyson 2014). The deep source of the structural power of finance cannot be reduced to capital mobility alone; it must be traced back to the structural dependence of the state on private credit; a dependence that in the case of Greece greatly increased as the crisis deepened and the state relied more and more on its domestic banks to refinance the *internal* debt, even as these banks lost their exit threat.

The second problem concerns the fact that Pagoulatos never spells out the relative nature of the banks' reduced power. It is one thing to note that the banks became vulnerable and structurally constrained over the course of the crisis; it is quite another to argue that therefore the banks lost their privileged political position, or the state was able to exert greater control over the banking sector. The broader issue here is that power is a relational concept, so when arguing that a given actor is less powerful one should always follow up by asking relative to whom. In the Greek case, Pagoulatos appears to describe the structural constraints operating on private banks through their insertion into the Eurozone and their dependence on creditor states for bank recapitalization funds and on the ECB for liquidity. The Greek state itself was incapable of providing either as it lacked its own central bank and the required currency reserves. So, while it is certainly true that the Greek banks were weakened by their financial vulnerability, this was a weakness vis-à-vis European creditors. It does not automatically follow from this that the Greek state thereby gained power over the banks; in fact, the dependence of the Greek state and banks was mutual, their fate structurally intertwined – a phenomenon analysts refer to as the "doom loop" between sovereign and banking risk. While the banks' power was certainly circumscribed, so was the power of the Greek state, which – despite the banks' weakness – continued to depend on them.

A third problem with Pagoulatos' conclusion, flowing naturally from the previous two, is that it does not appear to be borne out by the available evidence. If the banks really lost their privileged position or their relative power vis-à-vis the state, we would expect the Greek government to assert control over them in one way or another. Pagoulatos presents one piece of evidence to this effect: the PSI debt restructuring deal of 2012, in which Greek banks took a €37.7 billion hit on their government bond holdings (Pagoulatos 2014:475). At the same time, however, the Greek state assumed up to €50 billion in new debts from its

European creditors in order to be able to recapitalize the banks, effectively passing the debt from one hand to another: while PSI reduced the state's obligations to domestic banks, the recapitalization increased its debts to the Troika just to make the banks whole again. Most crucially, despite the fact that the Greek state thus covered 90 percent of the total capital injection into the banking system, it never actively asserted ownership rights over the banks. While the bank owners themselves only put up 10 percent of the injected funds, they were left untouched and remained in full control of their banks. Perhaps Pagoulatos, who served as an advisor to Papademos – who presided over PSI – has his own perspective on PSI, but the terms of the restructuring clearly favored private bankers. A critical report in the *New York Times* noted that "the banks' top executives are poised to potentially strike it rich. The plan developed by the Greek government and its international creditors to recapitalize the country's banks involves an unusual twist as stock offerings go: the new shares in the banks will give investors free and potentially lucrative warrants that will entitle them to buy many more shares in the future at a predetermined price."[55] Given the rising stock valuation of the banks post-PSI, this warrant – which came in the form of a put-option – constituted yet another state handout to private bankers.

Legitimation Crisis:

Eventually, as the social and humanitarian crisis deepened and the pro-banker bias in the prevailing policy response became all but undeniable, the political establishment rapidly

55 "Because many of the investors who are expected to participate in the stock program are the same executives who were running the banks at the time of their near collapse, critics see it as a case of bankers being rewarded despite their management missteps. And they say the Greek government is forgoing billions of euros in potential revenue with the way the stock offering is being handled. To date, of the 206 billion euros ... that the troika has dispensed to bail out Greece, an estimated 58 billion euros — all of which comes from European taxpayers — has been spent propping up the country's banks" (Thomas 2013b).

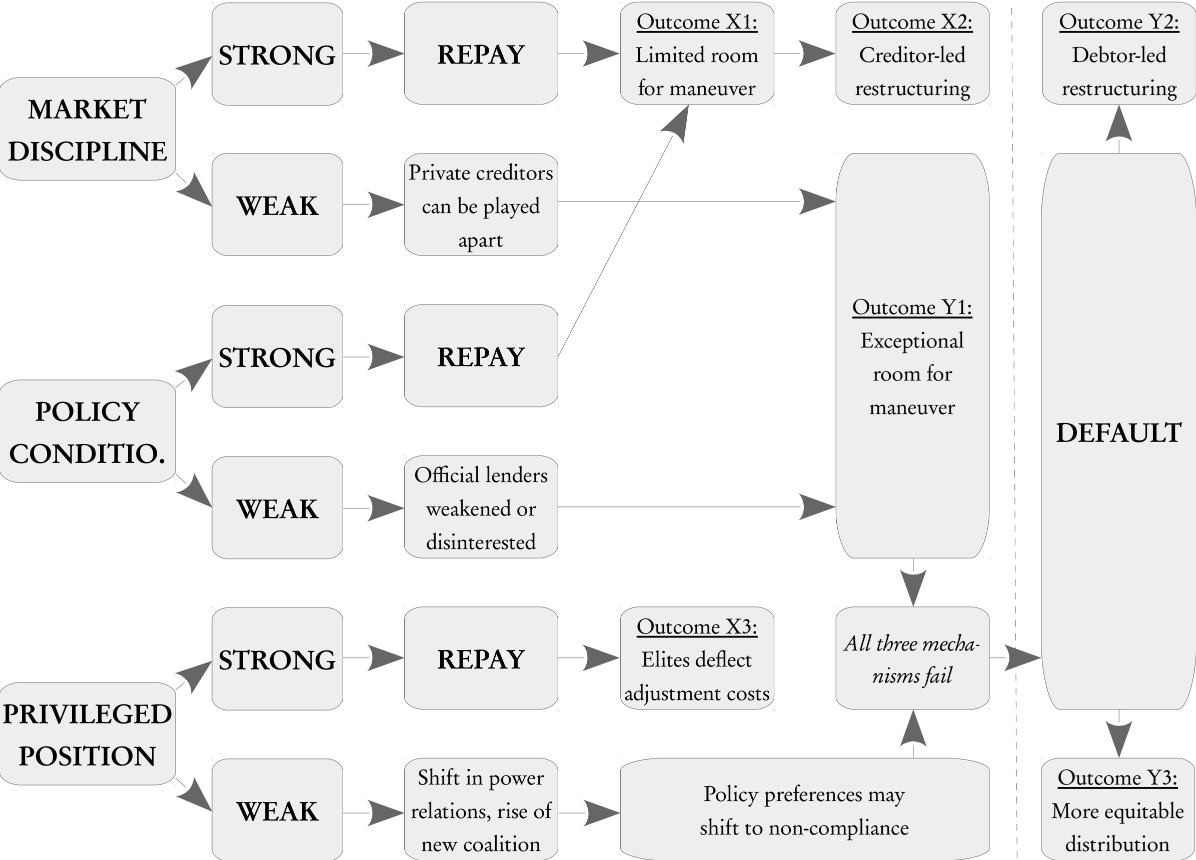
lost the trust of the Greek people. The protests that rocked the country in 2010-'12 were a case in point, and while the mobilizations subsided after February 2012, the incidence of protest remained impressive. Official data from the Ministry of Public Order show that the number of protest actions and demonstrations that took place in Greece between 2010 and 2014 was 20,210, with 6,266 of those taking place in the metropolitan region of Attica. As a report in the Greek establishment newspaper *Kathimerini* points out, "this translates into 5,100 protests per year, or approximately 14 marches and rallies on a daily basis, including Sundays" (Stangos 2014). The protests were a visible expression of the deep legitimation crisis of the Greek state and of the capacity of Greece's social movements to mobilize large segments of society against austerity and structural reform. While the demonstrations initially went unheard, over time the widespread social discontent translated into the collapse of the two establishment parties, which fell from a combined 77 percent of the vote in 2009 to 32 percent in the first election round of 2012. This crisis of representation and the burgeoning social movements in turn fed into the rise of the anti-austerity party Syriza.

After narrowly losing the 2012 elections to New Democracy, Syriza – which had up to that point persistently called for a unilateral suspension of debt payments – toned down its rhetoric and moderated its policy proposals, much as Lula had in Brazil, in an attempt to win over middle-class voters who remained fearful of the spillover costs of default and of the consequences of Grexit in particular; showing how the structural power of finance (in this case of official creditors) exerts its influence even over left-wing *opposition* parties. With its vague and inconsistent new pledge to "renegotiate" the debt, avoid unilateral action and at the same time end austerity while remaining inside the Eurozone, Syriza finally won the snap elections of January 25, 2015 and formed a coalition government with the xenophobic far-right Independent Greeks after falling just one seat short of an absolute majority. Setting

out with a series of symbolic anti-austerity moves – rolling back past privatizations and lay-offs, refusing to meet Troika negotiators on Greek territory, and demanding a negotiated debt restructuring from European creditors – the left-led government initially appeared to resemble the Kirchners of Argentina in their fierce rhetorical defiance of foreign creditors. Unlike Argentina, however, Greece explicitly rejected unilateral action. Its non-compliance with the bailout conditions was also quickly neutralized by the aggressive response of the Troika. In the next section on the outcomes of the crisis we will take a closer look at these events, which reveal just how limited the room for maneuver in the Eurozone has become, especially for the heavily indebted states of the periphery.

Outcomes of the Crisis

Figure 6.8 – outcomes according to structural power hypothesis:



The previous section has shown how the three hypothesized enforcement mechanisms were fully operative in the Greek case. When the initial mechanism of market discipline broke down in early 2010, after Greece was excluded from international capital markets, the second mechanism of the lender of last resort kicked in with force, starting with the first bailout. The third mechanism of privileged domestic elites served to entrench fiscal discipline within the Greek state apparatus. Unlike in Mexico, however, and reminiscent in some ways of Argentina, this third mechanism briefly broke down with the election of the Syriza government in January 2015. But unlike Argentina, where the Bush administration and the IMF pulled the plug on the program, this breakdown of the third mechanism in Greece did not coincide with a breakdown in the second mechanism, as official creditors – despite substantial internal disagreements – managed to maintain a united front and kept providing the prospect of further financing, as long as Greece proved itself willing to accept the Troika's strict policy conditions. In the following section, we will consider if and how the three enforcement mechanisms produced the outcomes of the crisis. Like the previous chapters, this final section will start with an assessment of Greece's room for maneuver before turning to the "resolution" of the crisis and the distribution of adjustment costs.

The first part will show how, in terms of Greece's room for maneuver, the outcome has been reminiscent of the Latin American debt crisis of the 1980s, with very limited space for unilateral action by the debtor countries as a result of a set of structural constraints on sovereignty that have compelled even left-leaning anti-austerity governments to abide by the terms of the creditor-imposed bailout programs. Second, in terms of the supposed "resolution" of the crisis through the PSI debt restructuring of 2012, a closer inspection reveals that – as was the case with previous debt restructurings in Latin America – Eurozone banks had already reduced most of their exposure, boosted their capital ratios and written down

their remaining bonds by the time they signed up for the deal. Like the 2001 mega-swap in Argentina, the 2012 PSI was in fact an opportunity for institutional bondholders to divest themselves of their remaining Greek debt. But unlike the mega-swap, in which the holdings of Argentine bonds were dispersed, following PSI holdings of Greek bonds were *socialized*. Debt concentration thus remains inexorably high, although the vast majority of Greek debt has now been transferred from the private to the public sector, leaving European taxpayers on the hook to bear the burden of a future Greek debt restructuring, even as the big banks escape unscathed and hedge funds continue to land windfall profits. Finally, when it comes to the distribution of adjustment costs within Greece, the same familiar pattern emerges – with the popular sector taking the hit even as the elite retains its wealth and privileges. The "left parenthesis" of 2015 proved to be too impotent to genuinely challenge these dynamics, highlighting once again just how deeply entrenched the structural power of creditors has become and how little national autonomy heavily indebted peripheral states truly have.

The Eurozone Straitjacket: Limited Room for Maneuver

The first and most obvious outcome of the European debt crisis has been the very constrained space for monetary and fiscal policymaking in the heavily indebted states of the periphery. While social opposition to austerity has been fierce at times, it has not led to any change in policy outcome (Glencross 2013:14-15). The prevailing approach to crisis management across the Eurozone periphery has presented a challenge to some of the established theories in Comparative Political Economy. For one, the Varieties of Capitalism literature has been ill-equipped to account for the similarity in policy responses across institutional contexts (Bruff and Horn 2012; Streeck 2014). Similarly, the Gourevitch (1986) approach of

examining diverging domestic policy responses to common economic shocks appears to be less fruitful in a situation where everyone is compelled by external forces to pursue the same measures. Armingeon and Baccaro (2012:182) observe how "governments of different political orientations, of different political strength, with different capacities for concertation with the social partners found themselves implementing essentially the same structural adjustment program centered on public sector cuts, pension reform, easing of employment protection legislation, weakening of unemployment insurance, and flexibilization of collective bargaining rules. The only type of choice left to governments was in the modalities used to mobilize popular consensus for, or at least blunt hostility against, austerity."

This broad and largely uncontested similarity in policy outcomes strongly hints at the existence of structural factors that overruled party politics and institutional contexts by disciplining national governments, circumscribing the policy options available to them, punishing divergent actions and ideas, and compelling policymakers to play by the rules of the game or face the wrath of bond markets and European institutions. As Armingeon and Baccaro (2011:31) put it, the European debt crisis is a clear "case in which domestic politics, either party- or interest group-based, does not matter: there is only one option – internal devaluation – and it is imposed from the outside." They conclude that "for peripheral countries, the policy space and the amount of discretion have shrunk dramatically." This limited room for maneuver is, in a way, reminiscent of the Latin American debt crisis of the 1980s, in which even left-leaning governments were compelled by their creditors to comply with the basic tenets of the Washington Consensus. If anything, the constraints on policy autonomy in the Eurozone appear to be even greater, as national governments lack control over monetary policy, thus forcing them to shift the full burden of adjustment onto fiscal policy; with the option of an external devaluation foreclosed, the only remaining choice is between

internal devaluation or default. The fact that the latter has been successfully banished and internal devaluation remains as the only policy option within the Eurozone is in fully in line with what the structural power hypothesis would lead us to expect – after all, it is the preferred outcome of creditors, as it deflects the burden of adjustment onto the debtors.

The brief period of defiance under the Syriza government in the first half of 2015 constitutes an ideal test for this structural power hypothesis, precisely because the radicals inside the cabinet actively tried to push out the "boundaries of the possible" during their first six months in office – only to find these boundaries rapidly closing in on them as the Troika, fearful of the leftists setting a successful precedent of debtor resistance that might embolden similar anti-austerity forces elsewhere (notably Podemos in Spain) mobilized all its might in a concerted attempt to crush Syriza's democratic experiment. The mechanism through which Eurozone creditors forced Alexis Tsipras to his knees was twofold: first, by the Eurogroup withholding the last €7 billion credit tranche of the 2012 bailout and the ECB withholding €2 billion in retained profits on Greek bonds acquired through SMP; and second through what has been called the "liquidity asphyxiation" of Greek banks, limiting the amount of emergency financing available to domestic lenders and surgically raising this limit by only just enough to keep the banks going from week to week. This constantly left the Greek financial system teetering on the brink of collapse, which in turn enabled the ECB to keep the Syriza government on a tight leash: a refusal by the ECB to increase the ELA ceiling next time around would instantly lead to a collapse of Greece's private banking system and force the country out of the euro.

It should be emphasized that the creditors' methods were applied in a context of extremely high dependence – both of the Greek government and of its banking system – on

the Eurozone creditor states and the ECB. The Greek government's payment schedule for 2015 was exceptionally onerous, with a total sum of €17 billion[56] falling due over the course of the year and a series of large payments due to the ECB in July and August – obligations that the government would never have been able to service without the disbursement of the €7 billion credit tranche from the last bailout and, at the very least, an additional bridging loan. For the Greek banks, meanwhile, liquidity was a major concern since the "bank jog" and widespread capital flight were eroding their capital base and cash reserves, leaving them acutely dependent on ECB liquidity assistance to be able to stay afloat and keep dispensing cash. In January alone, both in the lead-up to and in the wake of the elections of January 25, a total of €12 billion was withdrawn from Greek banks, pushing deposits down to €155 billion – the lowest level in 10 years, lower even than the previous nadir of the crisis during the 2012 elections. All of this rendered the Greek government vulnerable to a withdrawal of creditor support; a fact that the Syriza government appeared to be strangely oblivious to, but the Europeans were clearly well aware of. In a sign that it was willing to aggressively use the dependence of the Greek state and banks on European credit as a political weapon, the ECB first disqualified Greek government bonds as collateral for regular funding operations, forcing Greek banks – which had up to that point depended on the central bank accepting these bonds in return for access to its discount window – to turn to the higher-interest rate emergency liquidity assistance (ELA) instead. The ECB then systematically refused to raise the ELA ceiling to the levels it had allowed Greek banks to access under the technocratic Papademos government in 2012: while it had provided almost €110 billion in emergency liquidity assistance in 2012, by June 28, 2015 it was only providing up to €89 billion. As a senior international banker put it, "they [ECB] are squeezing them [Syriza] on everything,

56 This excludes treasury bills that are regularly rolled over by the domestic banks that hold them. If these bills are included the total amount due in 2015 rises to €37.5 billion.

it's part of a system to suffocate them, to make them realise the end is coming, to realise it is time to get on their knees" (cited in Barker and Hope 2015).

Despite a number of defiant moves in its first days in office, by February 20 the ECB and Eurogroup finance ministers had effectively forced the Syriza government into its first capitulation, signing up to a preliminary agreement that would extend the second bailout program to June 30 – but without disbursing the remaining loan tranche or raising the ELA ceiling. The agreement stated that "the Greek authorities commit to refrain from any roll-back of measures and unilateral changes to the policies and structural reforms that would negatively impact fiscal targets, economic recovery or financial stability, as assessed by the institutions." Dijsselbloem noted that "the biggest driver" behind the deal – which did not offer any concessions on debt relief, privatizations or fiscal surpluses, as Tsipras had hoped – were "fears that Greece might experience a full-blown bank run" (Giugliano 2015; Spiegel 2015). Michala Marcussen, head of economics at Société Générale bank, noted that "Greece is being kept on an incredibly tight leash" and stated that the Eurozone's refusal to disburse further credit or to provide additional liquidity was "clearly intended to keep Greece under pressure and keep things moving forward in the negotiations" (Chrysoloras and Bensasson 2015). This pressure was kept up over the next months, as Eurozone finance ministers systematically refused to give in to Greek demands for leniency. Faced with the inflexibility of its counterparts, the Greek government eventually opted for a cataclysmic last stand in June 2015. The crisis finally came to head when the increasingly unproductive talks approached a critical June 30 deadline, when the second bailout was set to expire and a big IMF payment was due, which Greece was unable to make without the disbursement of the final tranche. By then, Tsipras was in the thralls of a fierce power struggle inside his cabinet in which he "oscillated between rival groups of ministers and aides" (Stamouli and Walker 2015).

On one hand, the influential internal opposition around the Left Platform (made up mostly of former Communists and led by the far-left Energy Minister Panagiotis Lafazanis) and the so-called “Group of 53” (made up of prominent Syriza officials inside Tsipras' presidential faction of the party who were increasingly critical of the government's negotiating strategy) strongly opposed the idea of further concessions to the creditors. Exasperated by the intransigence of his fellow Eurozone finance ministers, Varoufakis was also pushing for a more confrontational line, as was Zoë Konstantopoulou, the Speaker of Parliament who presided over the Truth Committee on Public Debt (2015), which in a preliminary report declared parts of Greece's debt to be “illegal, illegitimate, odious and/or unsustainable” and called on the government to pursue a unilateral suspension of payments followed by an aggressive restructuring and a repudiation of all odious debts. This hotchpotch of radicals inside the party and the cabinet squared off against a highly influential group of close prime ministerial aides (including Tsipras' closest confidant, Nikos Pappas) and high-ranking cabinet members (most importantly Deputy Prime Minister Yannis Dragasakis) who had long been pushing for a more moderate and conciliatory line in a bid to unlock the remaining money of the previous bailout and to avoid a forced exit from the Eurozone.

In the weekend of June 20 and 21, Tsipras backed Dragasakis and other moderates inside the government, who had already taken control of the Brussels negotiating team after Tsipras had partly sidelined Varoufakis following an ill-fated previous summit in Riga on April 24, in drafting up a proposal that practically amounted to a declaration of surrender, including a commitment to much harsher fiscal targets than anything the government had previously agreed to and rolling back virtually all of the prime minister's election promises. But when, on Tuesday, June 23, the Greek proposal came back marked in “red ink,” with Eurozone officials striking through most of the Greek concessions as insufficient, replacing

them with their own words and leaking the document to the press, the combination of the creditors' intransigence and their insistence on his public humiliation convinced Tsipras of the merit of Varoufakis' repeated calls for a more confrontational line: if the creditors even refused to accept his capitulation, what options remained but to make a dramatic last stand?

After this rejection, the sequence of events unfolded in rapid succession. First, at an EU leaders summit on June 26, billed as the "last chance" to avoid Greece from going into arrears on the Fund and crashing out of the euro, Eurozone leaders made Greece an offer it could not refuse, in the form of a take-it-or-leave-it deal demanding much tougher measures in return for a bridging loan. Reportedly startled and infuriated by what he perceived to be the creditors' ultimatum, Tsipras stormed out of the Brussels negotiating room and flew back to Athens to inform his cabinet that he would be activating a referendum plan that he had long been contemplating in a bid to strengthen his negotiating position. In reality, the call for a referendum was more like a last-ditch attempt by the prime minister to keep his flailing party together. Cornered by his creditors and in full awareness that accepting their demands would lead to an internal rebellion and possibly a secession by the Left Platform, Tsipras took the decision to the people, urging them to vote against the creditors' demands with the promise that this would allow him to extract greater concessions from creditors in further negotiations. Even at this point, he explicitly rejected unilateral action.

As we saw before, the creditors' response to this move was very aggressive. Despite Tsipras' repeated claims to the contrary, European leaders instantly declared that the referendum would constitute a vote on Greek euro membership. Jeroen Dijsselbloem reiterated his long-standing calls for further austerity and declared that "if [the Greek] people say they don't want that, there is not only no basis for a new programme, there is also no basis for

Greece in the euro zone" (cited Sterling 2015). European leaders immediately cut off negotiations on further financing and refused to agree to a five-day bridging period requested by the Greek government to be able to carry out the referendum in peace. As a result, the ECB felt that it was no longer justified to keep increasing ELA and decided in a governing board meeting the next day that it would maintain the present level – which, in the face of the incipient bank run that had started following Tsipras' referendum announcement, amounted to a decision to cut the Greek banking system loose from further central bank support. The dramatic consequences – ATMs running out of cash, a closure of the banks, and the imposition of far-reaching capital controls and withdrawal limits – were already discussed in the section on spillover costs. Here it is just worth citing a policy advisor at the Greek finance ministry who reported that in a matter of days after the ECB's decision large parts of the economy and state were already starting to "die off" or malfunction (cited in Salmon 2015):

> *Companies [that] do not pay their employees through bank accounts cannot pay cash to employees – and there are many ... So we have a situation which is escalating into a chain reaction ... like having a heart attack ... if you view cash liquidity as the blood of the economy. On the weekend when the ECB stopped, we had the heart attack. Now [the week before the referendum] we are having its after-effects. Different organs are getting numb. Some stop working, others are trying but they don't have enough blood.*

The creditors' dramatic response – and the debilitating spillover costs it triggered – subsequently caused Tsipras to veer back towards his more moderate advisors and ministers, who in a heated cabinet meeting on June 30 called for a cancellation of the referendum and a resumption of negotiations with the creditors. Refusing to go down in history as another Papandreou, Tsipras upheld his referendum decision but decidedly shifted his tone, insisting once again that he would not take unilateral action and that Greece's position within the Eurozone was not in question. To give substance to this pledge and to please the moderates

inside the government, Tsipras authorized his negotiating team to draft a contradictory new proposal – remarkably similar to the one he was calling on voters to reject – and sent it to the Eurogroup. Unsurprisingly, it was rejected out of hand by the Europeans, who insisted that there would be no further negotiations until after the July 5 referendum. In the next days, mass rallies took place in favor of the "yes" and "no" vote, with the latter drawing hundreds of thousands into Syntagma Square on July 3. Two days later, an overwhelming 61.8 percent of Greeks, far more than the government had anticipated, voted to reject the creditors' terms, defying threats made by the European creditors and the Greek opposition, business elite and corporate media that a "no" vote would spell disaster and constitute an exit from the euro. A geographical analysis of the outcome showed that the poorer areas in Athens had overwhelmingly voted against while the wealthier areas had overwhelmingly voted in favor, highlighting a deep social divide over the issues of austerity, debt repayment and euro membership (Galatsidas and Arnett 2015).

That same night, Varoufakis presented a dramatic plan to an inner-cabinet meeting, proposing to capitalize on the spectacular energy generated by the popular mobilizations around the referendum and the resounding "no" vote through a three-pronged approach: to issue euro-denominated IOUs, declare a unilateral haircut on ECB-held Greek bonds, and take back control over the Bank of Greece (Lambert 2015). The plan was rejected outright by the majority of the six-member inner cabinet, with only Varoufakis and one other cabinet member voting in favor, having failed to convince Tsipras himself.

That very night, Varoufakis resigned. Within less than a week, Tsipras found himself back at the table in Brussels signing up to a new bailout with conditions even worse than the ones he had just convinced his own people to reject. It is difficult to think of a clearer

manifestation of the strategic exercise of structural power than the process through which Greece's creditors forced the leader of Europe's first radical left government and the figurehead of a continent-wide anti-austerity movement into this *kolotoumba*, or somersault. As a senior Syriza official put it, "It is a total capitulation. We never had a 'Plan B' for what to do if the [ECB] cuts off liquidity and the creditors simply destroyed our country, which is what they are doing" (cited in Evans-Pritchard 2015a). An EU official confided that Tsipras had been "crucified" by his Eurozone counterparts during the post-referendum negotiations, while a diplomat from German-allied country described the terms of the agreement as "akin to turning Greece into an economic protectorate" (cited in Spiegel and Wagstyl 2015). The third memorandum stipulated that "No unilateral fiscal or other policy actions will be taken by the authorities, which would undermine the liquidity, solvency or future viability of the banks. All measures, legislative or otherwise, taken during the programme period, which may have an impact on banks' operations, solvency, liquidity, asset quality, etc., should be taken in close consultation with the EC/ECB/IMF and where relevant the ESM." The *Financial Times* concluded that Greece had "pledged to accept a level of external oversight of its economy unprecedented of an EU member ... This can be seen as a hard-nosed programme in which the principal authors sit not in Mr Tsipras's cabinet but in the offices of the IMF, the EU and the creditors, led by Germany" (Wagstyl 2015).

In the parliamentary debate on the third memorandum of understanding with the resuscitated Troika of foreign lenders – which had never really gone away – Labor Minister Panos Skourletis declared that "the current balance of power makes capitulation inevitable." As Tsipras himself lamented as he passed the third bailout agreement through Parliament: "I had a choice between a deal I did not agree with, or a disorderly default." In line with the generalized trend away from the latter, he opted for the deal. As a Greek finance ministry

official explained afterwards, when asked about the reasons for Syriza's dramatic capitulation: "we underestimated their power" (cited in Salmon 2015).

Restructuring and Socialization of the Debt

Long before Syriza's rise to power, the restructuring of February 2012 was supposed to have brought an end to the crisis. European leaders announced the 53.5 percent haircut on private holdings of Greek bonds as a major sacrifice by creditors to help Greece back onto its feet and allow it to grow again. But as in the Brady plan of the 1980s and the mega-swap in Argentina, it is questionable how much debt relief Greece actually obtained and how heavily creditors were really hit by private sector involvement. In fact, three crucial points stand out. First, over the course of 2011 the European banks had already divested themselves of the majority of their bondholdings, boosted capital ratios and marked the remaining bonds to market (Allen & Overy 2012:13; Angeloni and Wolff 2012:9). Second, the restructuring was rigged so as to not harm existing bondholders and benefit hedge funds and other speculators, while doing very little to resolve Greece's underlying debt problems (Buchheit and Gulati 2012; Cline 2013). Third, the debt restructuring mostly hit the Greek banks, pension funds and small investors, which by that point held the majority of Greek government bonds. And while Greek banks were made whole through the recapitalization that came with the second bailout – a sum that would consequently be added to the public debt, forcing the costs of PSI onto Greek taxpayers – the pension funds and 15,000 small investors were never compensated for the haircut.[57] This outcome, favoring international

57 "Among the losers of PSI were public entities which suffered losses of €16.2 billion. Most of these losses accrued to pension schemes, with losses of €14.5 billion. ... Another group, which registered significant losses, were the small bond-holders. It is estimated that more than 15.000 families lost their life savings" (Truth Committee on Public Debt 2015:17/20).

finance at the expense of Greek citizens and European taxpayers, is once again in line with what the structural power hypothesis would lead us to expect: the power of the former allowed lenders to profit during the boom while deflecting the costs of the bust onto others.

On the first point, it was clear that European banks were much better prepared for an orderly debt write-down in early 2012 than they had been around the same time a year before. Over the course of 2011, most private bondholders had gotten rid of their exposure to Greek debt by selling their Greek junk bonds to the ECB or to vulture funds (Buchheit, Panizza *et al* 2013:25-26). As one analyst noted, “when Europe's leaders claim the continent is now better placed to withstand a crisis they mean only that this accumulation [of Greek bonds] has been largely transferred from the private to the public sector, mainly the European Central Bank” (Kay 2012). Through SMP, discussed at length in the previous section, the ECB bought peripheral junk bonds from banks at above-market prices, thus enabling private bondholders to dump their exposure on taxpayers for much better money than they could possibly have obtained on the market. As Ruparel and Persson (2011:13) noted early on in the ECB's bond-buying scheme, “by buying government bonds that otherwise would have been close to unsellable, the ECB is monetising otherwise illiquid debt – which is one of the reasons why the practice is (in theory) explicitly prohibited by the ECB's own rules.”

The debt that could not be dumped was written down (Roth 2013:19). Bloomberg data revealed that some of the biggest lenders had already written down their Greek bonds by over 70 percent in early 2012. PSI, which would bring about an estimated 74 percent loss on the net present value of these bonds, thus forced them to only subtract a little bit more, leaving “Europe's largest lenders and insurers ... likely to accede to the Greek debt swap because they've already written down their sovereign holdings and want to avert the risk of

a default" (Benedetti-Valentini and Kirchfeld 2012). Notably, these write-downs did not constitute real capital destruction but simply a downward adjustment of prospective profits (Roth 2013). An analyst at Kepler Capital Markets remarked that "European banks have had a long time to prepare and many already have the losses behind them. In the end, this deal was negotiated by the biggest banks and insurers, so a large participation rate is assured" (Benedetti-Valentini *et al* 2012). French banks, which had been most heavily exposed at the start of the crisis, had already written down their holdings of Greek government bonds to 25 percent of nominal value, making the haircut involved in PSI meaningless in terms of the banks' overall profits. For BNP Paribas, for instance, the amount was estimated to be in the range of €300 million – a negligible amount for a bank that raked in €6.5 billion in profits in 2012, up from €6 billion in 2010, making it Europe's most profitable financial institution. For other big lenders like Deutsche Bank and Commerzbank exposures were similarly negligible. For the banks, a debt restructuring started to look like an increasingly attractive option to reduce the risk of default and further divest of their Greek bonds.

As a result, Eurozone officials – who had been so terrified of a Greek default in 2011 – suddenly reversed course and embraced the need for a PSI debt restructuring. "Europe is prepared," Finland's Finance Minister Alexander Stubb said. "A hell of a lot better prepared than it was on May 9, 2010 – and a hell of a lot better prepared than it was last year" (cited in Chaffin 2012). And so the PSI deal went ahead, providing a misleading impression that Greece's foreign private bondholders had now shared in the burden of adjustment for the crisis. The reality was different. After the deal was concluded, one senior Eurozone official observed that "they [private bondholders] got a good deal. They get nearly 50 percent [of the debt's face value] back. Given the alternative, that's good" (cited in Baker and Sassard 2012). In fact, the deal turned out to be a boon for creditors. For one, lenders were offered

an “exceptionally large cash sweetener, in the form of highly rated EFSF notes... Regardless of what happened in Greece, participating investors would have this 'bird in hand'” (Zettelmeyer, Trebesch and Gulati 2013:26). In the process, creditors managed to divest themselves of their last-remaining toxic Greek bonds at decent prices, with significant upfront benefits and with their restructured bonds now denominated under English as opposed to Greek law, making it impossible for Greek officials to retrofit different conditions onto them or to legally denounce the debts by passing a repudiation bill through parliament.

The result of the above, unfolding over the two years between the onset of the crisis in early 2010 and the conclusion of PSI in February/March 2012, was a complete transformation of Greece's debt profile. The shift in the ownership structure was so dramatic that some of the world's leading sovereign debt scholars felt compelled to point out that “we are not aware of any other similarly drastic case of 'credit migration' from private into official hands in the history of sovereign debt” (Zettelmeyer, Trebesch and Gulati 2013:34). Where Greece's privately-held debt had once constituted nearly 80 percent of the total, by late 2012 this was only 20 percent, with the remaining 80 percent now held in official hands – marking a perfect inversion of the country's debt profile in the space of just one year. As in Argentina's mega-swap, private bondholders once again managed to get rid of their exposure. This time, however, the debt was not dispersed among hundreds of thousands of small investors, but *socialized* by official creditors.[58] The process through which this socialization occurred was twofold, going back to the second enforcement mechanism of official-sector

58 “[S]tarting in May 2010, Greece began drawing down on its official sector loans, partly to cover its budget deficits, but mostly to repay its bondholders at par. The liabilities thus inexorably began to migrate out of the hands of the folks who had lent the money and taken the commercial risk (the bondholders) and into the hands of Greece’s official (taxpayer funded) sponsors. It was a policy that lasted ... until the summer of 2011. It seems belatedly to have dawned on the official sector players that they were gradually displacing their private sector counterparts as the principal lenders to Greece” (Buchheit and Gulati 2012:4).

intervention: first, the lion's share of the two emergency loans to the Greek government – amounting to €240 billion in total – went straight to debt servicing, leading to a gradual replacement of privately-held debt with officially-held debt. It has been calculated that, for every single euro Greece received in Troika financing, it spent 89 cents on debt repayment and recapitalizing its banks (Mouzakis 2015). This, combined with the fact that the Greek government did not regain market access by the date foreseen in the program, meant that Greece literally assumed debts to the official sector in order to be able to repay its debts to the private sector – amounting to a *de facto* bailout of the latter in all but name. The second process through which the debt was socialized was the ECB's securities markets program, which allowed bondholders to dump Greek junk bonds on the central bank.

The outcome was possibly even more scandalous than Argentina's mega-swap: not only did private bondholders manage to shift the burden of adjustment onto the people of Greece and their liabilities onto European taxpayers, thereby avoiding essentially inevitable losses; they also found a way to completely obscure that fact (Roubini 2012; Buchheit and Gulati 2012:4; Eiffel Group and Glienicker Group 2015; Modi 2015). As the IMF (2013:17) concluded in its critical review of the 2010 bailout program:

> *Private creditors were able to significantly reduce their exposure ... There was a large-scale substitution from privately-held to publicly-held debt. Part of this was by design – program financing was to be used to repay maturing bonds in 2010 and 2011 – but the shift was intensified by market access not being regained in 2012, as well as by SMP. Purchases of Greek government bonds under SMP created rigidities when debt was restructured as a result of the decision to exclude SMP ... bond holdings from the PSI.*

By the time Syriza came to power in January 2015 and began to demand debt relief from Eurozone creditors, the big European banks had only negligible exposures to Greece. According to Reuters (2015) figures, German banks held €23.5 billion in Greek bonds, but

the biggest two banks – Deutsche and Commerzbank – "hold only a tiny fraction of that," with the state-owned development bank KfW responsible for the majority of holdings at €15 billion. As the head of the German banking association BdB put it, "the credit exposure of German banks in Greece is low. That's why, should it come to insolvency for Greece, the direct effects on German banks could be overcome." Consolidated exposure to Greek banks and companies was also down sharply compared to 2011. An emailed report by J.P Morgan showed that the cutting of links to Greek units and the systematic dumping of Greek bonds on the ECB left Europe's biggest banks with "limited risk to Greece." The total amount owed to the major European banks like BNP Paribas, Crédit Agricole, Société Générale, Commerzbank, Deutsche Bank and ING – which had been among Greece's main creditors before 2012 – were said to range between 0.1 and 0.9 percent of these banks' total outstanding loans: "very limited" and "immaterial" for the banks' profits (Bloomberg 2015). All of this significantly changed the nature of the game: by the time Syriza took power, the struggle over the burden of adjustment was no longer a question of how much European bankers would be made to pay for the irresponsible lending that helped cause the crisis, but how much European *taxpayers* should be made to pay to alleviate the burden of their Greek counterparts. By August 2015, the US and the IMF were insisting that the Eurozone should distribute the adjustment more equally – but Germany and its allies would have none of it, and fiercely resisted any type of debt relief or restructuring.

In the end, just like in Mexico and in Argentina, the debt reduction Greece obtained from the 2012 restructuring was negligible. As Cline (2013:4) points out, "the overall effect of the large PSI of April 2012 was ... to reduce total Greek debt by slightly less than one-fourth. It is perhaps not surprising that once the country had plunged into the insolvency mode, a debt reduction by only one-fourth would not have been sufficient to reestablish sol-

vency decisively." Others conclude that "the PSI component of the deal was little more than symbolic, and provided no meaningful debt relief" (Ardagna and Caselli 2014:17). What is worse, the next time the debts are restructured, the burden will not fall on the bankers who had taken the risks of lending to Greece in the first place, but on the taxpayers of the core countries who – mostly without being aware of it – have already bailed them out.

Unequal Distribution of Adjustment Costs

As a result of the above, the distribution of adjustment costs between Greece and its creditors ended up heavily skewed, with Greece shouldering virtually the entire burden. We have already seen how private creditors escaped unscathed and how a number of hedge funds made windfall profits. To this we can now add the highly asymmetric distribution of adjustment costs between Greece and its official European creditors. The ECB, for one, made significant profits off the Greek bonds it acquired in the SMP – profits it had pledged to return to Greece in late 2012, but has failed to after 2013.[59] The ECB itself estimates that it will make €5.6 billion in profits on Greek debt between 2014 and 2016, setting it on course for total profits of €10.4 billion by the 2020s. However, according to calculations by the Jubilee Debt Campaign (2015), the actual numbers may be significantly higher, as the interest rates the ECB receives and the discount at which it bought the bonds could push yields up to €22 billion. And the ECB – which systematically refused to partake in any debt restructuring – is not the only actor that profited: the German government has turned out handsome gains as well, not necessarily from interest paid by the Greek government but in

59 In fact, the ECB made the return of the profits it made on Greek bonds in 2014 conditional on the Greek government sticking with the letter of the second bailout agreement, using the return of these profits as another lever for enforcing discipline and exerting control over Greek policy.

particular from the lower interest rates it paid on its own bonds as a result of the "investor flight to safety." Recent research by the Halle Institute for Economic Research has found that "Germany benefited substantially from the Greek crisis," saving over €100 billion – or 3 percent of GDP – on lower interest payments between 2010 and 2015, with most of this reduction attributable "Greece flight" alone. The authors specify that "these benefits should not be overlooked, as they tend to be larger than the expenses, even in a scenario where Greece does not repay any of its debts" (Dany, Gropp, Littke and von Schweinitz 2015).

Beyond this asymmetric international distribution of adjustment costs, the burden of adjustment within Greece was also heavily skewed towards working people, pensioners, the youth, the middle class, the unemployed and the poor, as opposed to the wealthy (Roth 2013:63-64).[60] Unsurprisingly, as in past crises in the Global South, the adjustment process depended almost exclusively on cuts in pensions and welfare spending, regressive tax hikes, public sector layoffs, wage reductions and privatizations, all of which disproportionately harmed low and middle income households that depend on income from wages or welfare spending for their livelihoods. To provide just a particularly egregious example: low income households witnessed a 333.7 percent increase in their tax burden between 2009 and 2013; contrasting sharply to the 9 percent increase for the upper decile (Giannitsis and Zografakis 2015:17). Meanwhile, under the weight of austerity, unemployment rose over 25 percent (60 percent for the young) and average wages were cut by over a quarter. While the labor share of income (wage-related income relative to GDP) had increased from 34 percent to 35.7 percent between 2008 and 2010, it "fell significantly to 32.3% in 2013" while "the absolute amount of total wages decreased to €59.3 billion (2013) from €82.4 billion in 2008 (-28.0%)"

60 "The measures taken so far place the burden of adjustment almost exclusively on the crisis countries, despite that they are not solely responsible for the crisis. Even worse, within these countries, the burden is borne disproportionately by the weakest and least-responsible for the crisis" (Antzoulatos 2012:531).

(*ibid*:36). As a result, the average income of the poor fell 45.2 percent in 2008-'12 (*ibid*:63). This relative depravation has been unprecedented; it is difficult to think of any other case in which living standards in an advanced capitalist economy have collapsed so rapidly and so dramatically in peacetime conditions.

To make matters worse, as the public hospital budget was slashed in half and some 3 million uninsured Greeks lost access to the healthcare system, an unmitigated medical crisis took hold (see Stuckler and Basu 2013). HIV infections, child mortality and depression rates have all shot up dramatically, cancer patients are going untreated as hospitals – in arrears on their international pharmaceutical suppliers – can no longer obtain crucial drugs, and even tuberculosis and malaria have been staging a comeback. Charities report that in some of the poorest districts of Athens up to 90 percent of inhabitants rely on soup kitchens and food banks to avoid hunger. Apartment buildings are unheated during winter as landlords and tenants can no longer afford heating oil; brand new EU-funded highways remain eerily quiet as drivers can no longer afford the toll or the petrol. With a third of Greeks estimated to live below the poverty line and more than 680,000 children at risk of poverty or social exclusion, it is fair to say that austerity has unleashed a veritable humanitarian catastrophe; an acute and ongoing social crisis on a scale unseen in Greece since the Great Famine under the German occupation. More than 200,000 Greeks have already fled their homeland since 2010 – a mass migration that has been described as "the biggest brain drain in an advanced western economy in modern times" (Smith 2015b). In 2015, this even prompted the Obama administration to issue a number of sharp rebukes of Europe's crisis management. Caroline Atkinson, US deputy national security advisor, declared that "they have asymmetric rules. They need to make it socially fairer. It is important for creditors to take into account that Greece has had a very sharp drop in incomes, real wages, and output as well as a big rise in

unemployment. Greece has moved into primary surplus. How much more fiscal consolidation is necessary?" (cited in Evans-Pritchard 2015b).

The sacrifices of ordinary Greeks contrast sharply to the preferential treatment and financial privileges of the country's elite – most of whom have been able to evacuate their wealth from Greek banks by depositing it in Swiss bank accounts or routing their incomes via various tax havens like Cyprus, Luxembourg and the Netherlands, avoiding both taxes and a possible post-Grexit devaluation in the process. The aforementioned case of Greek bankers being offered a special "call option" after the post-PSI bank recapitalization – allowing them to buy back shares in their own banks at very low fixed prices – is possibly the most glaring indication of the special position of the country's financial establishment, whose privileges have largely been left intact despite the financial vulnerability and moral bankruptcy of their institutions (Varoufakis 2014). The perverse incentives created by this call option in turn allowed speculators like John Paulson, the US hedge fund billionaire, to pick up Greek bank shares at deflated prices with a view to collecting easy profits a few years out; a development that triggered an anomalous stock exchange bubble between mid-2012 and late 2014, while the economy was mired in depression. The outcome was clear: "The bigger winners ... were hedge funds, which pocketed higher profits than many had expected, in yet another Greek bailout financed by European taxpayers" (Thomas 2012).

In the end, perhaps the most telling conclusions about the Greek debt crisis were those reached by the IMF (2013) itself in its review of the initial 2010 bailout program. The report noted that "the actual decline in GDP was so much greater than anticipated [because] the fiscal multipliers were too low" (p. 21); "the burden of adjustment was not shared evenly across society" (p. 24); "ownership of the program was limited" (p. 24); "the prog-

ram was based on a number of ambitious assumptions" (p. 26); "the risks were explicitly flagged" (p.27); and "ex-ante debt restructuring was not attempted" (p. 27). The most remarkable admission in the IMF report is that there was an alternative at the start of the crisis – a negotiated debt restructuring – but that this was not taken because of political pressure exerted by European governments whose banks carried great exposure to Greece. IMF officials recognized that "many commentators considered debt restructuring to be inevitable," but it was not an option to the Fund's European partners (Xafa 2014:14). And so, "with debt restructuring off the table, Greece faced two alternatives: default immediately, or move ahead as if debt restructuring could be avoided. The latter strategy was adopted, but in the event, this only served to delay debt restructuring and allowed many private creditors to escape" (IMF 2013:27). The Standby Agreement, by the IMF's own admission, thus "served as a holding operation" for the banks to reduce their exposure (IMF 2013:28). "An upfront debt restructuring would have been better for Greece," the Fund notes, "although this was not acceptable to the euro partners. A delayed debt restructuring ... provided a window for private creditors to reduce exposures and shift debt into official hands. As seen earlier, this shift occurred on a significant scale and limited the bail-in of creditors when PSI eventually took place, leaving taxpayers and the official sector on the hook" (*ibid*). The worst part, then, is that much of the suffering turned out to be unnecessary: "Earlier debt restructuring could have eased the burden of adjustment on Greece and contributed to a less dramatic contraction in output" (IMF 2013:33). A counterfactual analysis by the Hans Böckler Stiftung's Macroeconomic Policy Institute found that "austerity explains almost the entire collapse of Greek GDP," and suggests that "in the absence of austerity, the Greek economy would have entered a prolonged period of stagnation, rather than a depression," as 80 percent of the contraction would have been avoided (Gechert & Rannenberg 2015:1).

Conclusion and Possible Alternative Interpretations

The findings presented in this chapter appear to confirm those uncovered in the previous two chapters. The three standard explanations of debtor compliance – reputation, sanctions and institutions – are unconvincing in the face of the available evidence. Instead, we find the same enforcement mechanisms at work as in the Mexican and Argentine cases, with high debt concentration and structurally interlocked creditor interests producing strict market discipline; with the high risk of contagion and the vulnerability of the European banking sector producing an aggressive official-sector intervention in the form of the three largest international bailout loans in world history, each provided under strict policy conditionality; and with the Greek political and financial elite strengthened in the first phases of the crisis as a result of the state's deepening dependence on private credit. As in Argentina, a deep legitimation crisis eventually led to a temporary and partial breakdown of the latter mechanism, with an anti-austerity coalition rising to power; unlike in Argentina, however, this did not produce a unilateral default since the second enforcement mechanism – the loan conditionality imposed by the Troika of foreign lenders – remained fully operative. Until the moment of writing, at least, official sector creditors have still not completely cut Greece off from further credit, although there have been tentative moves in this direction, most importantly in the wake of Tsipras' referendum announcement in the summer of 2015.

Driven in part by ideological motivations and in part by growing public opposition to further bailouts inside the creditor countries, the hardline position taken by German Finance Minister Wolfgang Schäuble and his conservative allies in small creditor countries like Finland, Austria, Latvia and the Netherlands, offers the possibility that an Argentina-style outcome – whereby official sector creditors accept the inevitability of default and cut

off their financial lifeline – may yet become a reality further down the road. With the third bailout program likely to fail in its stated attempts to restore debt sustainability, much will depend on the capacity of the second Tsipras government to stick to the letter of the memorandum, on the willingness of the official lenders to keep propping up the insolvent and imploding Greek state apparatus, and on the Troika's capacity to maintain a degree of internal coherence despite deepening tensions between the IMF and the Europeans. At the time of writing, it appears that – in contrast to the first half of 2015 – the immediate threat of a unilateral default has momentarily subsided, thanks to Tsipras' neutralization by the creditor powers and Syriza's metamorphosis into a pro-memorandum force. Still it remains unclear how much longer the Greek government and its official creditors can keep buying time to stave off the inevitable moment of reckoning at which a significant part of Greece's unsustainable debt will simply have to be written down, either voluntarily or forcefully.

Can we imagine alternative explanations for the evidence presented in this chapter? As in the previous two cases, the instrumentalist interpretation would emphasize the resort to direct forms of political pressure, interpersonal relations, lobbying, campaign finance and the like in preventing a Greek default. To varying degrees, some of these factors have indeed been observed: Eurozone officials exerted direct pressure on the Greek government when they threatened Grexit; close ties between Greek technocrats and the European financial establishment helped to cement fiscal discipline into the Greek state apparatus; lobbying by the Institute of International Finance likely played some role behind the scenes; and Greek banks poured hundreds of millions into the Greek political system over the years. Again, the point of this chapter has not been to disconfirm the existence of this instrumental type of power. However, as the chapter has tried to make clear, a truly exhaustive account of the Greek crisis should consider the unique form of power that private and official creditors

derived from the structural dependence of the Greek state on credit. Without the threat of withholding further credit and/or liquidity, the exercise of other forms of power would never have been as effective. The Eurozone could exert such enormous pressure on Greece precisely because of the credibility of its threat to withhold further credit and the extreme economic dislocation this would bring about; the Greek technocrats with close ties to the European financial establishment did not just "colonize" the state apparatus in isolation, but found their hand strengthened as the Greek crisis deepened and the state's dependence on foreign credit became more acute; the capacity of the IIF to exert direct pressure was a product of the highly concentrated ownership structure of the Greek debt and the structural interlinking of creditor interests, which eased the formation of a coherent creditors' cartel; and the Greek banks did not just exert influence by financing the election campaigns of the two establishment parties but by financing the very reproduction of the Greek state apparatus as such. In this sense, we should follow Culpepper and Reinke (2014) in emphasizing that the key feature that makes structural power structural is not the *way* in which it is exercised (through indirect and automatic rather than direct and intentional means) but the *source* of the power as such (in this case the capacity of private and official lenders to withhold credit from a heavily indebted peripheral state that acutely depended on it). Structural power, in this sense, can be exercised with deliberate and strategic intent on the part of its bearer; it need not be limited to the more impersonal, indirect and automatic channels that past work on structural power tended to emphasize.

Another possible explanation would be the constructivist one, which would emphasize the role of norms, ideas, narratives and the like. Again, the objective of this chapter has not been to disprove the importance of such factors. Quite the contrary: it can be argued that a "creditor morality" fiercely opposed to burden sharing ruled supreme throughout the

crisis, while the role of ideas has been emphasized as an important intersubjective adhesive maintaining the internal coherence of the international alliance between Greek elites and European creditors. If these factors did not receive a more extensive treatment it is simply because the aim of the chapter (and of the thesis more generally) has not been to investigate how creditors understand or formulate their interests but *how they enforce* their prevalent ideas of crisis management and their dominant norms of debt repayment. Here it is argued that the economic consequences of a “sudden stop” in credit provision create a hard barrier to default that even the most well-formulated heterodox ideas would find impossible to penetrate. Again, as in the previous two cases, ideas need to be taken seriously – but always in relation to underlying conflicts and power dynamics.

In this sense, the experience of the first Syriza-led government has once again been instructive. In the summer of 2015, Tsipras' belief that his fellow Eurozone leaders could simply be won over by force of argument suffered a bruising defeat at the hands of an unforgiving power balance that systematically favored and institutionally entrenched creditor-friendly norms and ideas. Indeed, the dominance of neoliberal ideas at the highest echelons of the Eurozone and the extreme asymmetry in the power balance between Greece and its creditors was such that the alternative norms and ideas proposed by the Syriza government could simply be laughed off, scorned and ignored – letting the refusal of credit do the hard work of forcing the Greeks back into line while resorting to the depoliticized language of “rules” and “necessity” to paper over the creditors' own lack of ideas when it came to long-term crisis resolution. In Europe as much as elsewhere, the present balance of forces simply does not appear to be in favor of reasonable – let alone radical – ideas for crisis resolution.

CONCLUSION:

The Democratic Disadvantage

Conclusions and Implications

This thesis has sought to address a simple question with far-reaching implications: why do heavily indebted peripheral states not default on their external debts more often? The short answer is that the balance of power between these countries and their creditors tends to be heavily skewed in favor of the latter. Through the threat of withholding much-needed credit in the short term, thereby unleashing debilitating spillover costs in the debtor country's economy, international lenders – private and official – can compel a dependent borrower to pursue creditor-friendly policies even if the government in question is strongly opposed to such policies. Large international bailouts ensure that the debtor is kept solvent, while the attendant policy conditionality enforces fiscal discipline in order to free up public revenue for debt servicing. As the crisis deepens and the state's dependence on credit grows, domestic elites with creditor-friendly views and close ties to the financial establishment find their hand strengthened at the expense of those who retain heterodox ideas and a degree of

loyalty towards domestic citizens and the interests of working people. If the latter do come to power, the state's dependence on credit greatly diminishes their room for maneuver and ultimately compels them to repay. As Lipson (1981:629) noted early on, “this political structure for collective action ensures that no state will default unless it is insolvent or is willing to accept a radical rupture with the capitalist world economy.”[61]

All of this tells us important things about the nature of contemporary capitalism and the quality of democracy under conditions of financialization. Compared to both the pre-war era and the immediate post-war decades, the policy autonomy of heavily indebted peripheral states has been significantly circumscribed by the resurrection of global finance. Seen in this light, the international debt crisis of the 1980s was the signal event highlighting the start of a new era in international lending; a phase that was marked by a generalized trend away from unilateral default and a propensity towards negotiated settlements favoring creditor interests. This evolution – which has only further intensified in subsequent decades – is in turn indicative of a shift not just in the international debtor-creditor relation, but in the state-finance relation more generally, with financial and political interests increasingly closely intertwined as state administrators become ever more concerned with the systemic prerogatives of finance-led growth. In this sense, the process through which the state-finance nexus and the international financial institutions have managed to banish the specter of unilateral default speaks to a much broader development in the global political economy and in the nature of the capitalist state. After drawing a set of conclusions from the findings presented in the case studies, the final section of the thesis will briefly discuss the implications of these findings for the study of political economy and of political science more generally.

61 “The debts are politically secure because they are backed by a network of multilateral banks, private lenders, and ... advanced capitalist states. They are jointly capable of consolidating debt in emergencies and severely punishing those who default lightly” (Lipson 1981:629).

Conclusions from the Findings

The findings presented in the case studies allow us to draw at least three conclusions about the structural power of finance in contemporary capitalism. First, at the heart of this structural power lies the vast increase in market concentration and the oligopolistic tendencies in international lending, which have produced a situation in which public debt instruments are increasingly held by a handful of systemically important financial institutions, as a result of which governments come to depend ever more on the willingness of these institutions to keep providing credit. This conclusion stands in contrast to arguments made by proponents of the Efficient Markets Hypothesis and other scholars who hold that market discipline resides in the "the democracy of the marketplace"; in other words, in the impersonal, decentralized and "apolitical" process of thousands of individually rational investors collectively pursuing their own self-interest and thereby inadvertently arriving at the optimal outcome for all involved. If the investigation into the first enforcement mechanism has revealed anything, it is that market discipline is far from a neutral economic phenomenon. What is generally referred to as "the markets" is in fact constituted by a small number of very powerful financial institutions whose lending decisions have far-reaching redistributive implications and whose preferences carry enormous weight in political decision-making.

These observations are corroborated by the findings of at least two groundbreaking studies that came out while this thesis was being written. First, Voth and Drelichman (2014) have found that the Genoese bankers' syndicates that lent to King Philip II of Spain in the sixteenth century benefited from a highly concentrated and interlocked lending structure to form a closely-knit "lenders' coalition" that, by acting as one, was capable of compelling even the world's most powerful sovereign to settle his debts every time he defaulted. These

findings indicate that the variable nature of market structure and debt concentration is not just a decisive factor in the contemporary global political economy, but holds significant explanatory power in the historical development of financial power more generally. Second, Hager (2016) has recently mapped the emergence of a "new aristocracy of finance" over the past three decades, demonstrating statistically how growing concentration in the ownership of the US public debt has gone hand-in-hand with an expansion of corporate power, which has "reinforced patterns of social inequality and proceeded in tandem with a shift in government policy, one that prioritizes the interests of government bondholders over the general citizenry" (Hager 2015:1). Hager's findings seem to confirm that the role of debt concentration in shaping the power of finance is not just limited to the periphery but applies even in the case of the most powerful capitalist state in the world today.

The second conclusion is that the power, profitability and privileges of finance have been crucially underwritten by creditor states, central banks and the international financial institutions. Since market discipline, as we have seen, is a necessary but insufficient barrier to default, there is an acute need – from the creditors' point of view – for an international lender of last resort capable of keeping distressed debtors solvent and enforcing strict fiscal discipline to free up resources for debt servicing. The record emergency loans provided by official-sector creditors and the policy conditionality they impose in return for such lending have been foundational to the ability of finance to reproduce itself in the face of its propensity to generate severe crises through speculative excess. Where in the past even the most powerful financial institutions risked going bankrupt in a major debt crisis, today the very survival and success of systemic ("too big to fail") institutions is guaranteed by the public sector. In sharp contrast to the 1930s, which famously lacked an international lender of last resort, today this function has been enshrined deep within the global financial architecture.

The third conclusion is that the dual processes of globalization and financialization have greatly strengthened the hand of wealthy elites – or Streeck's *Marktvolk* – in financial policymaking. The structural dependence of the debt state on credit creates an institutional bias in favor of fiscally orthodox policymakers and business-friendly technocrats with close ties to the international financial establishment. Political leaders who retain less orthodox views and a degree of loyalty towards domestic citizens, by contrast, are confronted with higher borrowing costs, creating an incentive structure that systematically favors fiscally conservative candidates. Over time, this bias tends to be internalized into the state through various means, including the pre-selection of orthodox economists in the financial bureaucracy, the introduction of constitutional checks on government spending, and the sidelining of the legislative at the expense of the executive power. This dynamic in turn contributes to a gradual breakdown of traditional processes of political representation, as fiscal policy – and hence highly contentious decisions over public spending and taxation – is increasingly insulated from popular pressures and removed from the orbit of democratic accountability. As a result, citizens find it more and more difficult to influence their governments' spending priorities through traditional democratic channels like elections and pressure politics.

Implications for Political Economy

The conclusions of this thesis have a number of important implications for both the study of sovereign debt and the study of structural power. To begin with, the former will have to become much more attentive to the tendency of mainstream economics scholarship to depoliticize its subject matter. A *political economy* approach to sovereign debt would take into account the redistributive consequences of default and repayment; the centrality of

conflicts of interest and power struggles over the distribution of the burden of adjustment; the asymmetric balance of forces and structural constraints on state autonomy that lie at the heart of the global political economy; and the different forms that default can take in practice: unilateral or negotiated. The latter, meanwhile (i.e., the study of structural power), will have to devise innovative new ways to account for variation in outcomes between cases and across issue areas. This thesis has focused specifically on the enforcement mechanisms through which the power of finance is exercised in the management of sovereign debt crises in the global periphery, identifying the precise conditions under which these mechanisms are effective and the conditions and countervailing mechanisms under which they will tend to break down. Moreover, by taking social struggles seriously, allowing for structural power to be contested from below, it has aimed to restore collective agency to its appropriate place in the study of political economy; even if this collective agency is increasingly being overshadowed by structural power in the important redistributive conflicts of our times.

While the exact mechanisms and conditions shaping the structural power of business will differ across sectors and issue areas[62], we can nevertheless distill a number of important themes from the key factors identified in this research project; themes that may hold relevance for scholarship in political economy and political science more generally. From the discussion above we can extrapolate at least three such themes, which could be summarized under the rubrics of (1) the growing concentration of wealth and power; (2) ongoing transformations in the state-finance relation; and (3) growing tensions between capitalism and democracy. These final pages of the conclusion will briefly consider each of these areas.

62 The structural power of the oil or pharmaceutical industry does not operate through the withholding of credit, for instance, while the structural power of finance will operate through different mechanisms and be affected by different conditions in the effort to fend of criminal litigation instead of a sovereign default.

On the first point, the findings presented in this thesis could be considered part of an emerging research agenda that places a strong emphasis on the concentration of wealth and power. In the wake of the global financial crisis and the Occupy Wall Street movement, talk of the "1 percent" has not just become a mainstay of contemporary political discourse, but is now also considered a subject area worthy of scholarly inquiry. After Stiglitz (2011), Graeber (2011) and the Occupy movement popularized the concept, the focus on the 1 percent has evolved from a political catchphrase into an important analytical tool in scholarship on wealth inequality (Piketty 2014; Alvaredo, Atkinson, Piketty and Saez 2013; Dorling 2014), public policy (Gilens and Page 2014) and business power (Hager 2016; Di Muzio 2015; De Donder and Roemer 2013). If the findings of these studies and this thesis are anything to go by, there thus appears to be extensive fertile ground for further research into the political, economic and social consequences of the growing concentration of capital. Taking this metric as an important co-determinant of structural power could help future political economy scholarship produce a better understanding of how this power varies in practice.

The second theme on the transformation of the state-finance relation also has important implications for political economy. While the globalization literature of the 1990s and early 2000s tended to conceive of the relationship between state and market as one in which the former was passively retreating at the expense of the latter, future research is likely to pay much more attention to the ways in which the state is actually being *actively restructured* in line with financial prerogatives. Far from standing in opposition to financial markets, the state has been foundational to their spectacular expansion over the past four decades, as well as their survival in the wake of the financial meltdown of 2008. This is in turn forcing a rethinking of the concepts of "the political" and "the economic", especially in terms of the relationship between states and markets – or state and capital – as a complex set of mutually

constituted interdependencies rather than a simple dichotomy (Mügge 2010). In the process, long-standing work on the centrality of the state in making and governing markets (Polanyi 1944; Wade 1990; Bruszt 2002) is likely to gain renewed interest from political economists, while a host of new opportunities will open up for innovative scholarship probing into the intricacies of the state-finance relationship in particular. In this light, the role of multilateral lenders like the IMF and World Bank in underwriting global financial interests has already been treated extensively in the development studies literature, but one area of inquiry that will probably prove to be of growing interest to scholars in the next years is the increasingly important role of central banks in propping up financial systems in the post-2008 period. The Greek case in this thesis, for instance, has demonstrated how the ECB played a leading role not just in enforcing debtor compliance and fiscal discipline, but also in subsidizing heavily over-leveraged banks and nurturing these private lenders back to life through its participation in numerous international bailouts, negative real interest rates, quantitative easing and a *de facto* socialization of their liabilities. Much more work is needed in this domain to help scholars better understand the ways in which financial markets are affected by central bank intervention and the ways in which central banks are affected by market pressures.

The third thematic concerns the deepening tensions between capitalism and democracy and the disintegration of traditional processes of political representation as a result of the state's need to consolidate its enormous debt load. Greece may be an extreme example of this development, but the tendency is more generalized and appears to affect countries in the core and periphery alike. Here Streeck's analysis of the rise of the *Marktvolk* as a second constituency alongside the *Staatsvolk* remains pertinent; even more important, however, is his observation that in the wake of the global financial crisis, the *Marktvolk* has increasingly become the only constituency that really counts, as the state – eager to consolidate its debt

burden through the internalization of fiscal discipline – has begun to actively shield policy-making from popular pressures to please its creditors. For Streeck (2014), this dynamic is now giving rise to a "consolidation state," marked by "the immunization of policy against pressure from below, so as to win back the confidence of 'the markets' in the system." In the course of this transition, "capitalism is emptied of democracy" (Streeck 2014:94; see also Streeck 2015). The findings presented in this thesis seem to corroborate this observation.

As the administration of the emerging consolidation state takes on an increasingly depoliticized form, with technocratic governments and grand coalitions replacing electoral party politics as the paradigmatic mode of governance in capitalist society, citizens lose the capacity to affect policy outcomes and social realities through elections or petitions, causing them to increasingly "tune out" from institutional politics altogether (Crouch 2004; Mair 2013). This development is gradually giving rise to a situation in which representatives who do remain responsive to popular concerns are systematically punished by "the markets" for their democratic inclinations and derided by technocratic experts and financial institutions for unnecessarily politicizing economic decisions that are supposed to be left firmly outside of the realm of politics. In this light, we could even hypothesize the existence of a distinct *democratic disadvantage* at the heart of financial capitalism, confronting those who retain a degree of responsiveness towards their voters with higher borrowing costs than those who answer solely to their creditors (*cf.* Schultz and Weingast 2003). As Streeck (2014:87) notes, "the mere possibility that a less market-friendly opposition might come to power may cost the state dearly in confidence and therefore in money." Over time, the repeated punishment meted out to less "responsible" politicians will tend to disincentivize popular responsiveness and institutionalize fiscal discipline at the level of the state, with negative consequences for the quality of democracy and the distribution of wealth and income.

Of course the notion of a distinct democratic disadvantage, or an inherent tension between capitalism and democracy that is intensified under conditions of financialization, will have to be further tested and refined through careful empirical investigation. But if the findings of this thesis and the emerging literature on the political consequences of the global financial crisis are anything to go by, it is a concept that future scholarship will likely have to reckon with over the next years. Certainly the case for polyarchy will become a lot more difficult to sustain as the oligarchic and anti-democratic tendencies in capitalism continue to come to the fore. The substantively important question, then, is not just how scholars will study and interpret these developments, but how we choose to respond to them.

BIBLIOGRAPHY:

Aggarwal, V. K. (1987) *International Debt Threat: Bargaining Among Debtors and Creditors in the 1980s.* Policy Paper in International Affairs No. 29. Berkeley, CA: Berkeley Institute for International Studies, University of California.

Aggarwal, V. K. (1990) 'Foreign Debt: The Mexican Experience' *Relazioni Internazionali*, September, pp. 26-33. Available at: http://basc.berkeley.edu/pdf/articles/Foreign %20Debt%20The%20Mexican%20Experience.pdf (Last accessed January 31, 2015).

Aggarwal, V. K. (1996) *Debt Games: Strategic Interaction in International Debt Rescheduling*. Cambridge: Cambridge University Press.

Aglietta, M. (2012) 'The European Vortex' *New Left Review* 75, May-June.

Ahmed, F. Z. Alfaro, L. and Maurer, N. (2010) 'Lawsuits and Empire: On the Enforcement of Sovereign Debt in Latin America' *Law and Contemporary Problems,* 73(39): 39-46.

Alfaro, L. and Kanczuk, F. (2005) 'Sovereign debt as a contingent claim: a quantitative approach' *Journal of International Economics*, 65(2): 297-314.

Allen & Overy (2012) *How the Greek Debt Reorganisation of 2012 Changed the Rules of Sovereign Insolvency*. Law Intelligence Unit. London: Allen & Overy. Available at: http://www.allenovery.com/SiteCollectionDocuments/AO%20-%20Greek%20debt %20reorganisation%20of%202012.pdf (last accessed January 31, 2015).

Althusser, L. (1965) *Pour Marx.* Paris: François Maspero.

Althusser, L. and Balibar, E. (1970) *Reading Capital.* London: New Left Books.

Altman, R. (2011) 'We need not fret over omnipotent markets' *Financial Times*, Dec. 1.

Alvaredo, F., Atkinson, A. B., Piketty T., and Saez, E. (2013) 'The Top 1 Percent in International and Historical Perspective' *Journal of Economic Perspectives*, 27(3): 3-20.

Alvarez, S. (2014) *The Untold Story of the Mexican Debt Crisis: Domestic Banks and External Debt, 1977-1989.* EABH Working Paper No. 14-03.

Andrews, D. M. (1994) 'Capital Mobility and State Autonomy: Toward a Structural Theory of International Monetary Relations' *International Studies Quarterly,* 38: 193-218.

Angeloni, C. and Wolff, G. B. (2012) *Are Banks Affected by their Holdings of Government Debt?* Working Paper 2012/07. Brussels: Bruegel.

Antzoulatos, A. A. (2012) 'Policy Responses to the European Debt Crisis Treating the 'Symptoms' or the 'Disease'?' *Panoeconomicus*, 5: pp. 529-552.

Archer, C. Biglaiser, G. and DeRouen, K. (2007) 'Sovereign Bond Ratings and Democracy: The Effects of Regime Type in the Developing World' *International Organization*, 61(1): 341-365.

Ardagna, S. and Caselli, F. (2014) 'The Political Economy of the Greek Debt Crisis: A Tale of Two Bailouts' *American Economic Journal: Macroeconomics*, 6(4): 291-323.

Ariso, G. and Jacobo, G. (2002) *El Golpe S.A.* Buenos Aires: Grupo Editorial Norma.

Armendariz, B. and Armendariz, P. (1995) 'Debt Relief, Growth and Price Stability in Mexico' *Journal of Development Economics*, Vol. 48: 135-149.

Armingeon, K. W. and Baccaro, L. (2011) 'The Sorrows of Young Euro: Policy Responses to the Sovereign Debt Crisis'. *Paper presented at CES conference*, Barcelona, June 2011.

Armingeon, K. W. and Baccaro, L. (2012) 'The Sorrows of Young Euro: The Sovereign Debt Crisis of Ireland and Southern Europe. In: Bermeo, N. and Pontusson, J. (eds.) *Coping with Crisis: Government Reactions to the Great Recession*. New York: Russell Sage Foundation.

Arrighi, G. (1994) *The Long Twentieth Century: Money, Power, and Origins of Our Times*. London and New York: Verso.

Arteta, C. and Hale, G. (2005) 'Are Private Borrowers Hurt by Sovereign Debt Rescheduling?' Available at: www.aeaweb.org/annual_mtg_papers/2006/0108_1300_1303.pdf (last accessed 3 March 2013).

Babb, S. (2001) 'The Rise of the New Money Doctors in Mexico' *Paper Presented at Financialization of the Global Economy Conference.* Political Economy Research Institute (PERI). Amherst, MA: University of Massachussetts, December 7-8.

Bachrach, P. and Baratz, M. S. (1962) 'Two Faces of Power' *The American Political Science Review,* 56(4): 947-952.

Badkar, M. (2011) 'How Exposure to Greece Has Changed in the Last Year' *Business Insider*, September 19. Available at: http://www.businessinsider.com/greece-exposure-2010-2011-default-2011-09 (last accessed August 24, 2015).

Baer, W. Margot, D. and Montes-Rojas. G. (2010) *Argentina's Default and the Lack of Dire Consequences*. Department of Economics Discussion Paper No. 10/09. London: City University.

Bailey, B. A. and Cohen, R. (1987) *The Mexican Time Bomb.* New York: Priority Press.

Baker, L. and Sassard, S. (2012) 'How the Greek debt puzzle was solved' *Reuters*, Feb 29.

Balcerowicz, L. (2010) 'Sovereign Bankruptcy in the EU in the Comparative Perspective' *Presented at the XII Travemünde Symposium zur ökonumischen Analyse des Rechts.* Trevemünde, March 24-26, 2010.

Bank for International Settlements (2011) *The Impact of Sovereign Credit Risk on Bank Funding Conditions*. s 43. Basel: Bank for International Settlements.

Bank of Canada (2014) *Introducing a New Database of Sovereign Defaults*. Technical Report No. 101. Available at: http://www.bankofcanada.ca/2014/02/technical-report-101/ (Last accessed January 31, 2015).

Barclays Capital (2011) 'Greece: The (Long) Countdown to Restructuring' Economics Research Briefing, May 11. Available at: http://www.gramercy.com/portals/0/pdfs/Greece%20-%20The%20%28long%29%20countdown%20to%20restructuring%205-11-11%20BarCap.pdf (Last accessed January 31, 2015).

Barker, A. and Hope, K. (2015) 'Greek banks pin hopes on political accord' *Financial Times*, February 18.

Barnett, M. and Duvall, R. (2005) 'Power in International Politics' *International Organization,* 59: 39-75.

Barrow, C. W. (1993) *Critical Theories of the State: Marxist, Neo-Marxist, Post-Marxist*. Madison: University of Wisconsin Press.

Bastain, C., 2012. *Saving Europe: How National Politics Nearly Destroyed the Euro*. Washington DC: Brookings Institution Press.

Beaulieu, E. Cox, G. W. and Saiegh, S. M. (2011) 'Sovereign debt and regime type: Re-considering the democratic advantage' *Presented at the MPSA Annual National Conference.* Chicago, IL, 30 March - 3 April 2011.

Beers, D. and Chambers, J. (2006) 'Sovereign Defaults at 26-Year Low, To Show Little Change in 2007' Standard & Poor's Commentary, 18 September.

Beetsma, R. (1994) *Servicing the Public Debt: Comment.* Working Paper No. 9477. Tilburg University, Center For Economic Research.

Benedetti-Valentini, F. and Kirchfeld, A. (2012) 'Greek Debt Swap Seen Winning Support From Europe's Banks' *Bloomberg*, February 21.

Bennett, A. (2004) 'Process Tracing and Causal Inference' In: Brady, H. E. Collier, D. (eds.) *Rethinking Social Inquiry: Diverse Tools, Shared Standards.* Lanham, MD.: Rowman & Littlefield.

Bensasson, M. and Chrysoloras, N. (2015) 'Draghi Pressures Tsipras as Greece Hung Outside QE Plan' *Bloomberg*, January 22.

Berg, V. (1984) 'Argentina's Rebuff to the IMF Panics Bankers' *EIR Economics*, 11(25): 4-7.

Berg, V. (1985) 'Pragmatic Concessions to IMF May Kill Debtor Nations' *EIR Economics*, 12(1): 20-22.

Bernal, R. (1982) 'Transnational Banks, the International Monetary Fund and External Debt of Developing Countries' *Social and Economic Studies*, 31(4): 71-101.

Bertola, L. and Ocampo, J. A. (2012) 'Latin America's Debt Crisis and Lost Decade' *Mimeo,* Institute for the Study of the Americas, University of London.

Bhagwati, J. N. (1998) 'The capital myth: The difference between trade in widgets and dollars' *Foreign Affairs,* 77(3): 7-12.

Birnbaum, M. (2011) 'Greece Agrees on Unity Government' *Washington Post*, Nov. 6.

Blanchard, O. and Leigh, D. (2013) *Growth Forecast Errors and Fiscal Multiplier.* IMF Working Paper 13/1. Washington, D.C., International Monetary Fund.

Block, F. (1987) *Revising State Theory: Essays In Politics and Postindustrialism.* Philadelphia: Temple University Press.

Bloomberg (2015) 'European Banks Have Limited Greek Exposure, JPMorgan Says' *Bloomberg Business*, January 5.

Blustein, P. (2005) *And the Money Kept Rolling In (and Out): Wall Street, the IMF, and the Bankrupting of Argentina.* New York: PublicAffairs.

Blustein, P. (2015) Laid Low: The IMF, the Euro Zone and the First Rescue of Greece. CIGI Paper No. 61, April. Waterloo, ON: Center for International Governance Innovation.

Boone, P. and Johnson, S. (2012) 'It's Not About Greece Anymore' *New York Times Economix*, May 6. Available at: http://economix.blogs.nytimes.com/2010/05 /06/its-not-about-greece- anymore/. (Last accessed January 31, 2015).

Borchard, E. M. (1951) *State Insolvency and Foreign Bondholders, Volume I: General Principles*. London: Oxford University Press.

Bordo, M. D. and Oosterlinck, K. (2005) 'Do Political Changes Trigger Debt Default? And Do Defaults Lead to Political Changes?' *Mimeo,* Rutgers University.

Borensztein, E. and Panizza. U. (2008) *The Costs of Sovereign Default.* IMF Working Paper 08/238. Washington, D.C., International Monetary Fund.

Borensztein, E. Cowan, K. and Valenzuela, P. (2007) *Sovereign Ceilings 'Lite'? The Impact of Sovereign Ratings on Corporate Ratings in Emerging Market Economies.* IMF Working Paper 07/75. Washington, D.C., International Monetary Fund.

Borensztein. E. and Panizza. U. (2010) 'Do Sovereign Defaults Hurt Exporters?' *Open Economies Review,* 21(3): 393-412.

Boughton, J. M. (2001) *Silent Revolution: The International Monetary Fund, 1979-1989*. Washington, D.C.: International Monetary Fund.

Branford, S. and Kucinski, B. (1988) *Debt Squads: The US, the Banks and Latin America*. London: Zed Books.

Bratsis, P. (1999) 'Nicos Poulantzas and the Ontological Status of the State in Marxist Theory' *Journal of the Hellenic Diaspora* 25(1-2): 155-177.

Braumoeller, B. F. and Goertz, G. (2000) 'The Methodology of Necessary Conditions' *American Journal of Political Science,* 44(4): 844-858.

Brewer, T. L. and Rivoli, P. (1990) 'Politics and Perceived Country Creditworthiness in International Banking' *Journal of Money, Credit, and Banking*, 22(3): 357-369.

Bruff, I. (2011) 'What about the Elephant in the Room? Varieties of Capitalism, Varieties in Capitalism' *New Political Economy*, 16(4): 481–500.

Bruff, I. and Horn, L. (2012) 'Varieties of Capitalism in Crisis?' *Competition and Change*, 16(3): 161-168.

Bruszt, L. (2002) 'Market Making as State Making: Constitutions and Economic Development in Post-Communist Eastern Europe' *Constitutional Political Economy*, 13(1): 53-72.

Brutti, F. (2011) 'Sovereign Defaults and Liquidity Crises' *Journal of International Economics*, 84(1): 65-72.

Brutti, F. and Sauré, P. (2014) *Repatriation of Debt in the Euro Crisis: Evidence for Secondary Market Theory*. SNB Working Paper No. 3/14. Zurich: Swiss National Bank.

Buchheit, L. and Gulati, G. M. (2012) *The Eurozone Debt Crisis: The Options Now*. Available at: http://ssrn.com/abstract=2158850 (Last accessed January 31, 2015).

Buchheit, L. C. (2011) 'The Eurozone Debt Crisis in Historical Perspective' *Mimeo*, Available here: http://www.hoover.org/sites/default/files/buchheit.pdf (Last accessed January 31, 2015).

Buchheit, L. C. and Gulati G. M. (2002) *Sovereign Bonds and the Collective Will.* The Georgetown-Sloan Project on Business Institutions Working Paper No. 34. Washington, D.C., Georgetown University Law Center.

Buchheit, L. C. and Gulati, G. M. (2010) *How to Restructure Greek Debt*. Duke Law Working Paper No. 47. Durham: Duke University.

Buchheit, L. C. Panizza, A. Gulati G. M. Panizza U. Weder B. and Zettelmeyer J. (2013) *Revisiting Sovereign Bankruptcy*. Washington DC: Brookings Institution. Available at: http://ssrn.com/abstract=2353173 (Last accessed January 31, 2015).

Buchheit, L.C. and Gulati G. M. (2009) 'The Coroner's Inquest: Ecuador's Default and Sovereign Bond Documentation' *International Financial Law Review,* 29(9): 22-25.

Buckley, R. P. (2009) 'The Bankruptcy of Nations: An Idea Whose Time Has Come' *The International Lawyer*, 43(3): 1189-1216.

Buffie, E. (1990) 'Debt Management and Negotiations' In: Sachs, J. D., (ed.) *Developing Country Debt and Economic Performance, Volume 2: The Country Studies – Argentina, Bolivia, Brazil, Mexico*. Chicago, IL: Chicago University Press.

Bugaric, B. (2013) *Europe Against the Left? On Legal Limits to Progressive Politics*. LEQS Working Paper No. 61/2013. London: London School of Economics.

Bulow, J. and Rogoff, K. (1989) 'Sovereign Debt: Is to Forgive To Forget?' *The American Economic Review,* 79(1): 43-50.

Calvo, G. A. (1988) 'Servicing the Public Debt: The Role of Expectations' *The American Economic Review*, 78(4): 647-661.

Canak, W. L. (1989) *Lost Promises: Debt, Austerity, and Development in Latin America*. Boulder, CO: Westview Press.

Carnoy, M. (1984) *The State and Political Theory.* Princeton: Princeton University Press.

Cassou, J., Erce-Domínguez, A. and Vázquez-Zamora, J. J. (2008) *Recent Episodes of Sovereign Debt Restructurings: A Case-Study Approach*. Documentos Ocasionales No. 0804. Madrid: Banco de España.

Catão, L. and Sutton, B. (2002) *Sovereign Defaults: The Role of Volatility*. IMF Working Paper 02/149. Washington, D.C, International Monetary Fund.

Cavallo, D. F. (2002) 'An Institutional Coup' *Declaration to judge responsible for investigating events of 2001.* Available at: www.cavallo.com.ar/wp-content/uploads/an_institutional.pdf (last accessed May 30, 2014).

Cavallo, D. F. (2004) 'Argentina and the IMF During the Two Bush Administrations' *International Finance*, 7:1: 137-150.

Cerny, P. G. (1993) 'The Political Economy of International Finance' In: Cerny, P. G. (ed.) F*inance and World Politics: Markets, Regimes and States in a Post-hegemonic Era*. Aldershot: Edward Elgar.

Chaffin, J. (2012) 'Athens rehearses the nightmare of default' *Financial Times*, February 17.

Chahoud, T. (1991) 'The Changing Roles of the IMF and the World Bank' In: Altvater, E., Hübher, K. *et al* (eds.) *The Poverty of Nations: A Guide to the Debt Crisis from Argentina to Zaire.* London: Zed Books.

Checkel, J. T. (2005) *It's the Process Stupid! Process Tracing in the Study of European and International Politics.* Working Paper No. 26. University of Oslo.

Choi, S. J. Gulati, M. and Posner, E. A. (2011) *Pricing Terms in Sovereign Debt Contracts: A Greek Case Study with Implications for the European Crisis Resolution Mechanism*. Working Paper No. 541. University of Chicago, John M. Olin Law & Economics.

Choi, S. J. Gulati, M. and Posner, E. A. (2012) 'The Evolution of Contractual Terms in Sovereign Bonds' *Journal of Legal Analysis,* 4(1): 131-79.

Chrysoloras, N. and Bensasson, M. (2015) 'Greek Deposit Outflows Said to Slow to 3 Billion Euros' *Bloomberg*, April 1.

Chrysoloras, N. Ziotis, C. and Bensasson, M. (2015) 'Greek Bank Deposit Flight Said to Accelerate to Record' *Bloomberg*, January 28.

Cibils, A. and LoVuolo, R. (2012) 'At Debt's Door: What Can We Learn from Argentina's Recent Debt Crisis and Restructuring?' *Seattle Journal for Social Justice*, 5(2).

Cibils, A. B., Weisbrot, M. and Kar, D. (2002) *Argentina Since Default: The IMF and the Depression*. CEPR Briefing Paper. Washington, DC: Center for Economic and Policy Research.

Claessens, S., Diwan, I. and Fernandez-Arias, E. (1992) *Recent Experience with Commercial Bank Debt Reduction*. Working Paper no. 995, World Bank.

Claessens, S., Oks, D., and Van Wijnbergen, S. (1993) *Interest Rates, Growth and External Debt: The Macroeconomic Impact of Mexico's Brady Deal*. Working Paper No. 1147. Washington, DC: World Bank.

Cline, W. R. (1983) 'International Debt and the Stability of the World Economy' *Policy Analyses in International Economics*, Policy Brief No. 4-31. Washington, D.C.: Institute for International Economics.

Cline, W. R. (1995) *International Debt Reexamined.* Washington, D.C.: Institute of International Economics.

Cline, W. R. (2013) *Debt Restructuring and Economic Prospects in Greece*. Policy Brief No. Pb13-3. Washington: Peterson Institute for International Economics.

Cohen, B. J. (1998) *The Geography of Money*. Ithaca, NY: Cornell University Press.

Cohen, B. J. (2000) 'Money and Power in World Politics' In: Lawton, T. C. and Verdun, A. C. (eds.) *Strange Power: Shaping the Parameters of International Relations and International Political Economy.* Farnham: Ashgate.

Cohen, B. J. (2012) *The Future of Global Currency: The Euro Versus the Dollar.* London: Routledge.

Cohen, D. (1991) *Private Lending to Sovereign States*. Cambridge, MA.: MIT Press.

Cole, H. L. and Kehoe, T. J. (2000) 'Self-fulfilling Debt Crises' *Review of Economic Studies,* 67: 91-116.

Colectivo Situaciones (2002) *19 & 20: Notes for a New Social Protagonism*. New York: Minor Compositions.

Collier, D. (1993) 'The Comparative Method' In: Finifter, A. W. (ed.) *Political Science: The State of the Discipline II.* Washington D.C.: American Political Science Association.

Collier, D. (2011) 'Understanding Process Tracing' *Political Science and Politics*, 44(4): 823-830.

Collier, D. and Mahoney, J. (1996) 'Insights and Pitfalls: Selection Bias in Qualitative Research' *World Politics*, 49(1): 56-91.

Collier, R. B. and Collier, D. (1991) *Shaping the Political Arena: Critical Junctures, The Labor Movement, and Regime Dynamics in Latin America.* Princeton: Princeton University Press.

Cooper, A. F. and Momani. B. (2005) 'Negotiating Out of Argentina's Financial Crisis: Segmenting the International Creditors' *New Political Economy*, 10(3): 305-320.

Cooper, R. N. and Sachs, J. D. (1985) 'Borrowing Abroad: The Debtor's Perspective' In: Smith, G. and Cuddington, J. T. (eds.) *International Debt and the Developing Countries.* Washington: World Bank.

Corrales, J. (2002) 'The Politics of Argentina's Meltdown' *World Policy*, 19(3): 29-42.

Crouch, C. (2004) *Post-Democracy*. Cambridge, UK: Polity.

Crowley, T. (1993) 'The Role of the Commercial Banks in the Latin American Debt Crisis' *Trocaire Development Review*, 9-29.

Cruces, J. J. (2007) 'The Value of Pleasing International Creditors' Universidad Torcuato di Tella Department of Economics, Buenos Aires.

Culpepper, P. D. (2008) 'Business Power, Policy Salience, and the Study of Politics' *European Studies Forum,* 38(2): 5-11.

Culpepper, P. D. (2011) *Quiet Politics and Business Power: Corporate Control in Europe and Japan*. Cambridge: Cambridge University Press.

Culpepper, P. D. (2015) 'Structural Power and Political Science in the Post-Crisis Era' *Business and Politics*, 17(3): 391-409.

Culpepper, P. D. and Reinke, R. (2014) 'Structural Power and Bank Bailouts in the United Kingdom and the United States' *Politics & Society*, September 24.

Cypher, J. C. (1990) *State and Capital in Mexico: Development Policy since 1940*. Boulder, CO: Westview Press.

Dahl, R. A. (1961) *Who Governs? Democracy and Power in an American City*. New Haven: Yale University Press.

Dalakoglou, D. (2014) 'The real reasons bailout talks took place in Paris – and what it all means for Greece' *The Conversation*, September 5. Available at: http://theconversation.com/the-real-reasons-bailout-talks-took-place-in-paris-and-what-it-all-means-for-greece-31314 (Last accessed January 31, 2015).

Damill, M., Frenkel, R. and Rapetti, M. (2005) *The Argentinean Debt: History, Default and Restructuring*. Paper prepared for 'Sovereign Debt' project of the Initiative for Policy Dialogue (IPD). New York, NY: Columbia University.

Dany, G., Gropp, R. E., Littke, H. and von Schweinitz, G. (2015) *Germany's Benefit from the Greek Crisis*. IWH Working Paper 7/2015, Halle: Leibniz Institut für Wirtschaftsforschung.

Das, U. S. Papaioannou, M. G. and Trebesch, C. (2011) 'Spillovers of Sovereign Default Risk: How Much Is the Private Sector Affected?' In: Kolb, R. W. (ed.) *Sovereign Debt: From Safety to Default.* New York: Wiley.

Das, U. S. Pappaioannou, M. G. and Trebesch, C. (2012) *Sovereign Debt Restructurings 1950–2010: Literature Survey, Data, and Stylized Facts*. IMF Working Paper 12/203. Washington, D.C., International Monetary Fund.

Datz, G. (2009) 'Held Out? Reputation, International Litigation, Financial Incentives and Domestic Debt in Sovereign Restructurings' *Presented at the Annual Convention of the International Studies Association*, San Francisco: April 3-6.

Datz, G. (2013) ‚What Life after Default? Time Horizons and the Outcome of the Argentine Debt Restructuring Deal ' *Review of International Political Economy*, 16(3): 456-484.

De Donder, P., Roemer, J. E. (2013) *An Allegory of the Political Influence of the Top 1%*. CESIFO Working Paper No. 4478, November.

De Grauwe, P. and Ji, Y. (2013) *Mispricing of Sovereign Risk and Multiple Equilibria in the Eurozone*. CEPS Working Paper No. 361. Brussels: Centre for European Studies.

Delamaide, D. (1984) *Debt Shock: The Full Story of the World Debt Crisis*. New York, NY: Doubleday.

Devlin, R., and Ffrench-Davies, R. (1995) 'The Great Latin American Debt Crisis: A Decade of Asymmetric Adjustment' *Revista de Economia Política*, 15(3): 117-142.

Di Muzio, T. (2015) *The 1% and the Rest of Us: A Political Economy of Dominant Ownership* London: Zed Books.

Diaz-Alejandro, C. F. (1983) 'Stories of the 1930s for the 1980s' In: Aspe, P. A., Dornbusch R., and Obstfelt M. (eds.) *Financial Policies and the World Capital Market: The Problem of Latin American Countries.* Chicago: University of Chicago Press.

Diaz-Alejandro, C. F. (1984) 'Latin American Debt: I Don't Think We're in Kansas Anymore' *Brookings Papers on Economic Activity,* 15(2): 335-403.

Dimsky, G. (2011) 'The International Debt Crisis' In: Michie, J. (ed.) *The Handbook of Globalisation (Second Edition).* Cheltenham: Edward Elgar.

Dominguez, K. M. E. and Tesar, L. L. (2004) 'International Borrowing and Macroeconomic Performance in Argentina ' *Prepared for the NBER conference on International Capital Flows*, December 17-18. Cambridge, MA: National Bureau of Economic Research.

Donadio, R. and Erlanger, S. (2012) 'As Greeks Head to Polls Again, a Fear That No One Will Win' *New York Times,* June 16.

Dooley, M. P. (1995) *A Retrospective on the Debt Crisis.* NBER Working Paper No. 4963. Cambridge, MA: National Bureau of Economic Research.

Dooley, M. P. (2000) 'International Financial Architecture and Strategic Default: Can Financial Crises be Less Painful?' Carnegie-Rochester Conference Series on Public Policy, 53: 361–377.

Dooley, M. P., Fernandez-Arias, E. and Kletzer, K. M. (1994) *Recent Private Capital Inflows to Developing Countries: Is the Debt Crisis History?* NBER Working Paper No. 4792. Cambridge, MA: National Bureau of Economic Research.

Dorling, D. (2014) *Inequality and the 1%.* New York: Verso.

Douzinas, C. (2013) *Philosophy and Resistance in the Crisis*. Cambridge, UK: Polity.

Draghi, M. (2015) 'Introductory statement to the press conference (with Q&A)' Frankfurt: European Central Bank, March 5. Available at: <https://www.ecb.europa.eu/press/pressconf/2015/html/is150305.en.html> accessed September 16, 2015.

Drazen, A. (1998) 'Towards a Political Economic Theory of Domestic Debt' In: Calvo, G. and King, M. (eds.) *The Debt Burden and its Consequences for Monetary Policy*. London: Macmillan.

Drelichman, M. and Voth, H. (2014) *Lending to the Borrower from Hell: Debt, Taxes and Default in the Age of Philip II.* Princeton: Princeton University Press.

Duménil, G. and Levy, D. (2011) *The Crisis of Neoliberalism*. Cambridge, MA: Harvard University Press.

Dyson, K. (2014) *States, Debt, Power: 'Saints' & 'Sinners' in European History & Integration*. Oxford: Oxford University Press.

Eaton, J. and Fernandez. R. (1995) *Sovereign Debt.* Working Paper No. 5131. Cambridge, MA., National Bureau of Economic Research.

Eaton, J. and Gersovitz, M. (1981) 'Debt with Potential Repudiation: Theoretical and Empirical Analysis' *The Review of Economic Studies*, 48(2): 289-309.

Eaton, J. Gersovitz. M. and Stiglitz, J. E. (1986) *The Pure Theory of Country Risk.* Working Paper No. 1894. Cambridge, MA., National Bureau of Economic Research.

ECB (2010a) *Keynote speech at the 9th Munich Economic Summit*. Frankfurt: European Central Bank. Available at: https://www.ecb.europa.eu/press/key/date/2010/html/sp100429.en.html (last accessed June 12, 2015).

ECB (2010b) 'The ECB's response to the recent tensions in financial markets' *Speech by Jean-Claude Trichet at the 38th Economic Conference of the Oesterrichische Nationalbank*. Vienna, 31 May 2010. Available at: https://goo.gl/cq6hts (last accessed June 12, 2015).

ECLR editorial (2012) 'The Fiscal Compact and the European Constitutions: "Europe Speaking German"'. *European Constitutional Law Review*, 8(1): 1-7.

Economist (1981) 'The New Hero' *The Economist,* March 10: 68-69.

Economist (1984) 'Mexico's Happy Creditors' *The Economist*, April 8: 60.

Economist (2003) 'Hard or Soft?' *The Economist*, September 25.

Economist (2005) 'Victory by Default? Argentina's Debt Restructuring' *Economist*, May 3.

Eichengreen, B. (1992) *Golden Fetters: The Gold Standard and the Great Depression, 1919-1939*. New York: Oxford University Press.

Eichengreen, B. (2002) *Financial Crises and What To Do About Them*. New York: Oxford University Press.

Eichengreen, B. (2005) *Capital Liberalization and the Fund*. Prepared for the High Level Seminar on Capital Account Liberalization and the IMF. Bern: Swiss Ministry of Finance, December 12.

Eichengreen, B. and Bordo, M. D. (2003) 'Crises Now and Then: What Lessons from the Last Era of Financial Globalization' In: Mizen, Paul (ed.) *Monetary History, Exchange Rates and Financial Markets: Essays in Honor of Charles Goodhart, Vol 2.* London: Edward Elgar.

Eichengreen, B. and Portes, R. (1988a) *Settling Defaults in the Era of Bond Finance.* CEPR Discussion Paper No. 272. London, Center for Economic Policy Research.

Eichengreen, B. and Portes, R. (1988b) *Foreign Lending in the Interwar Years: The Bondholders' Perspective*. CEPR Discussion Paper No. 273. London, Center for Economic Policy Research.

Eichengreen, B. and Portes, R. (1989) *Dealing with Debt: The 1930s* and *the 1980s.* Working Paper No. 2867. Cambridge, MA., National Bureau of Economic Research.

Eichengreen, B. and Portes, R. (2000) 'Debt Restructuring With and Without the IMF' Unpublished, UC Berkeley.

Eichengreen, B., Hausmann, R. and Panizza, U. (2005) 'Currency Mismatches, Debt Intolerance, and Original Sin: Why They Are Not the Same and Why It Matters' In: Edwards S. (ed.) *Capital Controls and Capital Flows in Emerging Economies: Policies, Practices and Consequences*. Chicago, IL.: University of Chicago Press.

Eiffel Group & Glienicker Group (2015) 'Giving Greece a Chance' Brussels: Bruegel. http://bruegel.org/2015/05/giving-greece-a-chance/ (last accessed June 12, 2015).

Enderlein, H. Trebesch, C. and von Daniels, L. (2011) 'Sovereign Debt Disputes: A Database on Government Coerciveness During Debt Crises' *Journal of International Money and Finance,* 31(2): 250-266

Epstein, E. and Pion-Berlin, D. (2006) 'The Crisis of 2001 and Argentine Democracy' In: Epstein, E. and Pion-Berlin, D. (eds.) *Broken Promises? The Argentine Crisis and Argentine Democracy*.

Epstein, G. A. (2001) 'Introduction: Financialization and the World Economy' In: Epstein (ed.) *Financialization and the World Economy*. Cheltenham: Edward Elgar.

European Commission (2015a) *European Economic Forecast: Winter 2015*. Brussels: European Commission. Available at: http://ec.europa.eu/economy_finance/publications/european_economy/2015/pdf/ee1_en.pdf (accessed August 24, 2015).

European Parliament (2014). 'Report on the enquiry on the role and operations of the Troika (ECB, Commission and IMF) with regard to the euro area programme countries' Report A7-0149/2014. Available at: http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//TEXT+REPORT+A7-2014-0149+0+DOC+XML+V0//EN (last accessed September 7, 2015).

Evans-Pritchard, A. (2015a) 'Crippled Greece yields to overwhelming power as deal looms' *The Telegraph*, July 11.

Evans-Pritchard, A. (2015b) 'White House warns Europe on Greek showdown' *The Telegraph*, February 13.

Exadactylos, T. and Zahariadis, N. (2013) 'The lack of public trust in political institutions is a massive obstacle to public policy change in Greece' *EUROPP: European Politics and Policy.* LSE blog: http://blogs.lse.ac.uk/europpblog/2013/01/17/greece-trust-institutions/ (last accessed August 24, 2015).

Falletti, T. G. (2006) 'Theory-Guided Process Tracing in Comparative Politics: Something Old, Something New' *APSA Comparative Politics Newsletter,* 17(1): 9-14.

Fearon, J. (1994) 'Domestic Political Audiences and the Escalation of International Disputes' *American Political Science Review*, 88(3): 577-592.

Féliz, M. (2012) 'Neo-Developmentalism: Beyond Neoliberalism? Capitalist Crisis and Argentina's Development since the 1990s' *Historical Materialism*, 20(2): 1-19.

Ferreira Rubio, D. and Goretti, M. (1995) 'Governar la emergencia. Uso y abuso de los decretos de necesidad y urgencia (1989-1993)' *Agora* 1(3).

Finnemore, M. (2003) *The Purpose of Intervention: Changing Beliefs about the Use of Force*. Ithaca, NY: Cornell University Press.

Fiorentini, F. (2012) 'Argentina: Que Se Vayan Todos – They All Must Go!' *Red Pepper*, May 2012.

Fischer, S. (1989) 'Resolving the International Debt Crisis' In: Sachs, J. D. (ed.) *Developing Country Debt and Economic Performance*. Chicago: University of Chicago Press.

Flandreau, M. and Flores, J. H. (2009) 'Bonds and Brands: Foundations of Sovereign Debt Markets, 1820–1830' *The Journal of Economic History*, 69(3): 646-684.

Flandreau, M. and Flores, J. H. (2011) *Bondholders vs. Bond-Sellers? Investment Banks and Conditionality Lending in the London Market for Foreign Government Debt, 1815-1913*. Working Paper No. 0002, European Historical Economics Society (EHES).

Fleming, J. M. (1962) 'Domestic Financial Policies under Fixed and under Floating Exchange Rates' *IMF Staff Papers,* 9(3): 369-79.

Foley, S. (2011) 'S&P's powerful chief steps out of the shadows' *The Independent*, August 8.

Foster, J. B. (2007) 'The Financialization of Capitalism' *Monthly Review*, 58(11).

Fouskas, V. K. and Dimoulas, C. (2013) *Greece, Financialization and the EU*. London: Palgrave.

Frieden, J. A. (1991) *Debt, Development, and Democracy: Modern Political Economy and Latin America, 1965-1985*. Princeton: Princeton University Press.

Friedman, T. (1995) 'Don't mess with Moody's' *New York Times*, February 22.

Fuentes, M. and Saravia, D. (2010) 'Sovereign Defaulters: Do International Capital Markets Punish Them?' *Journal of Development Economics,* 91: 336-347.

Fuhrmans, V. and Moffett, S. (2010) 'Exposure to Greece Weighs on French, German Banks. *Wall Street Journal*, February 17.

Galatsidas, A. and Arnet, G. (2015) 'Greek referendum: how Athens voted – interactive map' *The Guardian datablog*, July 9. Available at: http://www.theguardian.com/news/datablog/ng-interactive/2015/jul/09/greek-referendum-how-athens-voted-interactive-map (last accessed: September 7, 2015).

Garuda, G. (2000) 'The Distributional Effects of IMF Programs: A Cross-Country Analysis' *World Development*, 28(6): 1031-51.

Gechert, S. and Rannenberg, A. (2015) *The costs of Greece's fiscal consolidation*. Policy Brief, March 2015, Institut für Makroökonomie und Konjunkturforschung. Düsseldorf: Hans Böckler Stiftung. Available at: http://www.boeckler.de/pdf/p_imk_pb_1_2015.pdf (last accessed September 7, 2015).

Gelos, R. G. Sahay, R. and Sandleris, G. (2004) *Sovereign Borrowing by Developing Countries: What Determines Market Access?* IMF Working Paper 04/221. Washington, D.C., International Monetary Fund.

Gelpern, A. (2005) *After Argentina*. Policy Brief No. PB05-2, Washington, D.C.: Institute for International Economics.

Gennaioli, N., Martin, A. and Rossi, S. (2013) 'Sovereign Default, Domestic Banks and Financial Institutions'. Citation based on working paper, later published as Gennaioli, N., Martin, A. and Rossi, S. (2014) *Journal of Finance*, 69(2): 819-866.

George, A. L. and Bennett, A. (2005) *Case Studies and Theory Development in the Social Sciences.* Cambridge, MA.: MIT Press.

George, A. L. and McKeown, T. J. (1985) 'Case Studies and Theories of Organizational Decision Making' *Advances in Information Processing in Organizations,* 2: 21-58.

Gerring, J. (2007) *Case Study Research: Principles and Practices.* Cambridge: Cambridge University Press.

Giannitsis, T. and Zografakis, S. (2015) *Greece: Solidarity and Adjustment in Times of Crisis*. Study No. 38, Institut für Makroökonomie und Konjunkturforschung. Düsseldorf: Hans Böckler Stiftung. Available at: http://www.boeckler.de/pdf/p_imk_study_38_2015.pdf (last accessed September 7, 2015).

Gibson, H. D. Hall, S. G. and Tavlas, G. S. (2011) *The Greek Financial Crisis: Growing Imbalances and Sovereign Spreads.* Working Paper No. 124, Athens, Bank of Greece.

Gilens, M. and Page, B. I. (2014) 'Testing Theories of American Politics: Elites, Interest Groups and Average Citizens' *Perspectives on Politics* (forthcoming, fall 2014).

Gill, S. (1992) 'Economic Globalization and the Internationalization of Authority: Limits and Contradictions' *Geoforum,* 23(3): 269-283.

Gill, S. (1995) 'Globalization, Market Civilisation, and Disciplinary Neoliberalism' *Millennium,* 24: 399-423.

Giugliano, F. (2015) 'Athens faces uphill struggle despite eurozone deal' *Financial Times*, March 4.

Glencross, A. (2013) 'The Eurozone Crisis as a Challenge to Democracy and Integration in Europe' *Orbis*, 58(1): 55:68.

Goldscheid, R. (1919) *Sozialisierung der Wirtschaft oder Staatsbankrott: Ein Sanierungsprogramm*. Vienna: Anzengruber Verlag: Brüder Suschitzky.

Goodman, J. B. and Pauly, L.W. (1993) 'The Obsolescence of Capital Controls? Economic Management in the Age of Global Markets' *World Politics,* 46(1): 50-82.

Gouge, T. (2003) *Exodus from Capitalism: The End of Inflation and Debt.* Bloomington, IN: iUniverse.

Gourevitch, P. (1986) *Politics in Hard Times: Comparative Responses to International Economic Crises*. Ithaca, NY: Cornell University Press.

Graeber, D. (2011) *Debt: The First 5,000 Years.* London: Melville House.

Griffith-Jones, S. (ed.) (1988) *Managing World Debt.* New York: St. Martin's.

Grossman, H. I. and Van Huyk, J. B. (1985) *Sovereign Debt as a Contingent Claim: Excusable Default, Repudiation, and Reputation.* Working Paper No. 1673. Cambridge, MA., National Bureau of Economic Research.

Grugel, J. and Riggirozzi, M. P. (2007) *The Return of the State in Argentina*. Working Paper No. WEF0018, World Economy and Finance Research Programme, University of Sheffield.

Guembel, A. and Sussman, O. (2008) 'Sovereign Debt Without Default Penalties' *Review of Economic Studies,* 76(4): 1296-1320.

Gurría, A. (1988) 'Debt Restructuring: Mexico as Case Study' In: Griffith-Jones, S. (ed.) *Managing World Debt.* New York: St. Martin's.

Gurría, A. (1995a) 'The Mexican Debt Strategy' *Challenge*, 38(2): 34-38.

Gurría, A. (1995b) 'Capital Flows: The Mexican Case' In: Ffrench-Davis, R. and Griffith-Jones, S. (eds.) *Coping with Capital Surges: The Return of Finance to Latin America.* Boulder, CO: Lynne Riener.

Gurría, A. (2013) Interview with the author. OECD Headquarters, Paris: January 2013.

Hacker, J. S. and Pierson, P. (2002) 'Business Power and Social Policy: Employers and the Formation of the American Welfare State' *Politics and Society,* 30(2): 277-325.

Hager, S. B. (2015) *Public Debt as Corporate Power: Mapping the New Aristocracy of Finance*. Working Papers on Capital as Power, No. 2015/01, available at: http://www.capitalaspower.com/wp-content/uploads/2015/01/hager_2015_CasPWP1.pdf (last accessed August 24, 2015).

Hager, S. B. (2016) *Public Debt, Inequality, and Power: The Making of a Modern Debt State.* Oakland, CA.: University of California Press.

Hall, P. A. (2006) 'Systematic Process Analysis: When and How to Use It' *European Management Review,* 3: 24-31.

Hannon, P. (2015) 'Eurozone PMI Survey Shows Collapse in Greek Manufacturing Output' *Wall Street Journal*, August 3.

Hardt, M. and Negri, A. (2000) *Empire*. Cambridge, MA: Harvard University Press.

Harvey, D. (2005) *A Brief History of Neoliberalism*. Oxford: Oxford University Press.

Harvey, D. (2010) *The Enigma of Capital and the Crises of Capitalism*. London: Profile.

Hausman, R. and Velasco, A. (2002) 'Hard Money's Soft Underbelly: Understanding the Argentine Crisis' *Brookings Trade Forum 2002.* Washington, DC: Brookings Institute. In the text it says it's 2003, you sure it's not 2002?

Hawley, C. and Allen, K. (2011) 'Greek Exit from Eurozone Just a Matter of Time' *Der Spiegel*, November 2.

Helleiner, E. (1994) *States and the Reemergence of Global Finance: From Bretton Woods to the 1990s*. Ithaca, NY: Cornell University Press.

Helleiner, E. (2005a) *Structural Power in International Monetary Relations*. EUI Working Paper RSCAS No. 2005/10. Florence, European University Institute.

Helleiner, E. (2005b) 'The Strange Story of Bush and the Argentine Debt Crisis' *Third World Quarterly*, 26(6): 951-969.

Helleiner, E. (2006) 'Below The State: Micro-Level Monetary Power' In: Andrews, D. M. (ed.) *International Monetary Power.* Ithaca, NY: Cornell University Press.

Héritier, A. (2008) 'Causal Explanation' In: Della Porta, D. and Keating, M. (eds.) *Approaches and Methodologies in the Social Sciences: A Pluralist Perspective.* Cambridge: Cambridge University Press.

Hindmoor, A. (2012), 'Taming the City? Structural Power and the Evolution of British Banking Policy amidst the Great Financial Meltdown' *Mimeo,* University of Sheffield.

Hirschman, A. O. (1970) *Exit, Voice and Loyalty: Responses to Decline in Firms, Organizations, and States.* Cambridge, MA.: Harvard University Press.

Holloway, J. and Picciotto, S. (1978) 'Introduction: Towards a Materialist Theory of the State' In: Holloway, J. and Picciotto, S. (eds.) *State and Capital: A Marxist Debate*. London: Edward Arnold.

Hope, K. and Wagsty, S. (2015) 'Two Greek banks seek emergency funds from ECB' *Financial Times*, January 16.

International Monetary Fund (2002) 'Fund Policy on Lending into Arrears to Private Creditors: Further Consideration of the Good Faith Criterion' *Prepared by the International Capital Markets, Policy Development and Review and Legal Departments.* Washington D.C., International Monetary Fund.

International Monetary Fund (2013) *Greece: Ex Post Evaluation of Exceptional Access Under the 2010 Stand-by Agreement*. IMF Country Report No. 13/156. Washington, DC: International Monetary Fund.

Islam, F. (2013) *The Default Line: The Inside Story of People, Banks and Entire Nations on the Edge*. London: Head of Zeus.

J.P. Morgan (2013) *The Euro area adjustment: about halfway there*. Europe Economic Research Note, May 28. Available at: https://culturaliberta.files.wordpress.com /2013/06/jpm-the-euro-area-adjustment-about-halfway-there.pdf (Last accessed January 31, 2015).

Jensen, N. (2002) 'Democratic Governance and Multinational Corporations: The Political Economy of Foreign Direct Investment' *Mimeo*. New Haven: Yale University.

Jessop, B. (1977) 'Recent Theories of the Capitalist State' *Cambridge Journal of Economics*, 1(4): 353-373.

Jessop, B. (1982) *The Capitalist State: Marxist Theories and Methods*. New York: NYU Press.

Johnson, S. and Kwak, J. (2010) *13 Bankers: The Wall Street Takeover and the Next Financial Meltdown.* New York: Knopf Doubleday Publishing Group.

Jolly, D. and Bradhser, K. (2015) 'Greece's Debt Crisis Sends Stocks Falling Around the Globe' *New York Times*, June 29.

Jones, G. (2011) 'ECB debates ending Italy bond buys if reforms don't come' *Reuters*, November 5.

Jorgensen, E. and Sachs, J. D. (1989) 'Default and Renegotiation of Latin American Foreign Bonds In The Interwar Period' In: Eichengreen B. and Lindert, P. H. (eds.) *The International Debt Crisis in Historical Perspective*. Cambridge, MA: MIT Press.

Jubilee Debt Campaign (2015) 'ECB to make between €10 and €22 billion profit out of loans to Greece' *Jubilee Debt Campaign*, July 10. Available at: jubileedebt.org.uk/blog/ecb-to-make-between-e10-billion-and-e22-billion-out-of-loans-to-greece (last accessed September 7, 2015).

Kaletsky, A. (1985) *The Costs of Default.* New York: Priority Press.

Kaminsky, G. and Schmukler, S. L. (2002) 'Emerging Market Instability: Do Sovereign Ratings Affect Country Risk and Stock Returns? ' *The World Bank Economic Review,* 16(2): 171-195.

Kaminsky, G. L. and Vega-Garcia, P. (2014) *Systemic and Idiosyncratic Sovereign Debt Crises*. NBER Working Paper No. 20042, Cambridge, MA, National Bureau of Economic Research.

Kaplan, S. B. (2013) *Globalization and Austerity Politics in Latin America*. Cambridge, UK: Cambridge University Press.

Kaufman, R. R. (1985) 'Democratic and Authoritarian Responses to the Debt Issue: Argentina, Brazil, Mexico' *International Organization*, 39(3): 473-503.

Kay, J. (2012) 'Some euros are more equal than others' *Financial Times*, May 22.

Keohane, R. (2000) 'Foreword' In: Lawton, T. C. and Verdun, A. C. (eds.) *Strange Power: Shaping the Parameters of International Relations and International Political Economy.* Farnham: Ashgate.

Kindleberger, C. P. (1973) *The World in Depression.* Berkeley: University of California Press.

King, G. Keohane, R. O. and Verba, S. (1994) *Designing Social Inquiry: Scientific Inference in Qualitative Research*. Princeton: Princeton University Press.

Kirshner, J. (2005) *Currency and Coercion in the Twenty-First Century.* EUI Working Paper RSCAS No. 2005/13. Florence, European University Institute.

Kirshner, J. (2009) 'After the (Relative) Fall: Dollar Diminution and the Consequences for American Power' In: Helleiner, E. and Kirshner, J. (eds.) *The Future of the Dollar*, Ithaca, NJ: Cornell University Press.

Klein, M. (2004) 'Stumbling on the Verge of the Abyss (Without Falling into It): Argentina and its Crisis of the Millennium' In: Fiorucci and Klein, M. (eds.) *The Argentine Crisis at the Turn of the Millennium*. Amsterdam: Aksant, pp. 1-14.

Klein, N. (1999) *No Logo*. New York: Picador.

Kocharov, A. (ed.) (2012) *Another Legal Monster? An EUI Debate on the Fiscal Compact Reality*. EUI Working Paper Law No. 2012/9. Florence: European University Institute.

Kolb, R. W. (ed.) (2011) *Sovereign Debt: From Safety to Default.* New York: John Wiley.

Körner, P., Maass, G., Siebold, T., and Tetzlaff, R. (1986) *The IMF and the Debt Crisis: A Guide to the Third World's Dilemma*. London: Zed Books.

Korten, D. (1995) *When Corporations Rule the World.* Sterling, VA: Kumarian Press.

Kouvelakis, S. (2011) 'The Greek Cauldron' *New Left Review* 72, November-December.

Kraft, J. (1984) *The Mexican Rescue*. New York: Group of 30.

Krätke, M. (2009) 'Kritik der Öffentlichen Finanzen: Die Finanzkrise des Staates Erneut Betrachtet' *Prokla: Zeitschrift für Kritische Socialwissenschaft*, 154: 119-140. Citation from English translation by the author, available at: http://www.theseis.com/synedrio/05_a_Kraetke.pdf (last accessed May 30, 2014).

Krippner, G. R. (2005) 'The Financialization of the American Economy' *Socio-Economic Review*, 3(2): 173:208.

Krippner, G. R. (2011) *Capitalizing on Crisis: The Political Origins of the Rise of Finance.* Cambridge, MA: Harvard University Press.

Kruger, M. and Messmacher, M. (2004) *Sovereign Debt Defaults and Financing Needs.* IMF Working Paper 04/53. Washington, D.C., International Monetary Fund.

Lambert, H. (2015) 'Yanis Varoufakis full transcript: our battle to save Greece' *New Statesman*, July. Available at: http://www.newstatesman.com/world-affairs/2015/07/yanis-varoufakis-full-transcript-our-battle-save-greece (last accessed Sept 17, 2015).

Lanau, S. (2008) 'Essays on Sovereign Debt Markets' Available at: http://tesisenred.net/bitstream/handle/10803/7380/tsl.pdf (accessed March 3, 2013).

Lapavitsas, C. (2008) 'Financialised Capitalism: Direct Exploitation and Periodic Bubbles. Mimeo, University of London, School of Oriental and African Studies. Available at: http://leftlibrary.com/lapavitsas1.pdf (last accessed August 25, 2015).

Lapavitsas, C. (2013) *Profiting without Producing: How Finance Exploits Us All.* London and New York: Verso.

Lapavitsas, C. (2014) 'The Era of Financialization: An Interview with Costas Lapavitsas' *Dollars and Sense*, May/June 2014. Available at: http://www.dollarsandsense.org/archives/2014/0414lapavitsas.html (last accessed August 25, 2015).

Lapavitsas, C. et al. (2012) *Crisis in the Eurozone.* London and New York: Verso.

Laskos, E. and Tsakalotos, C. (2013) *Crucible of Resistance: Greece, the Eurozone and the World Economy*. London: Pluto.

Lasslett, K. (2014) 'The State at the Heart of Capitalism: Marxist Theory and Foucault's Lectures on Governmentality' *Critical Sociology*, 40(3): 1-18.

Lawton, T. C. Rosenau, J. N. and Verdun, A. C. (2000) 'Introduction' In: Lawton, T. C. and Verdun, A. C. (eds.) *Strange Power: Shaping the Parameters of International Relations and International Political Economy.* Farnham: Ashgate.

Lawton, T. C. Rosenau, J. N. and Verdun, A. C. (2000) 'Introduction' In: Lawton, T. C. and Verdun, A. C. (eds.) *Strange Power: Shaping the Parameters of International Relations and International Political Economy.* Farnham: Ashgate.

Lazzarato, M. (2012) *The Making of the Indebted Man: An Essay on the Neoliberal Condition.* Cambridge, MA.: MIT Press.

Leander, A. (2000) 'Strange Looks on Developing Countries: A Neglected Kaleidoscope of Questions' In: Lawton, T. C. and Verdun, A. C. (eds.) *Strange Power: Shaping the parameters of international relations and international political economy.* Farnham: Ashgate.

Leslie, P. (1983) 'Techniques of Rescheduling: The Latest Lessons' *The Banker*, 133(686): 24.

Levitsky, S. and Murillo, M. V. (2003) 'Argentina Weathers the Storm' *Journal of Democracy*, 14(4): 152-166.

Levy-Yeyati, E. and Panizza, U. (2011) 'The Elusive Costs of Sovereign Defaults' *Journal of Development Economics*, 94(1): 95-105.

Lewis, P. H. (2009) *The Agony of Argentine Capitalism: From Menem to the Kirchners*. Santa Barbara, CA: ABC-CLIO.

Lienau, O. (2014) *Rethinking Sovereign Debt: The Politics of Reputation in the Twentieth Century.* Cambridge, MA.: Harvard University Press.

Lindblom, C. E. (1977) *Politics and Markets: The World's Political-Economic Systems*. New York: Basic Books.

Lindblom, C. E. (1982) 'The Market as Prison' *The Journal of Politics,* 44(2): 324-336.

Lindert, P. H. and Morton, P. J. (1989) 'How Sovereign Debt Has Worked' In: Sachs, J. D. (ed.) *Developing Country Debt and Economic Performance, Volume 1: The International Financial System*. Chicago: University of Chicago Press.

Lipson, C. (1981) 'The International Organization of Third World Debt' *International Organization*, 35(4): 603-631.

Lipson, C. (1985) 'Bankers' Dilemmas: Private Cooperation in Rescheduling Sovereign Debts' *World Politics*, 38(1): 200-225.

Lissakers, K. (1983) 'Dateline Wall Street: Faustian Finance' *Foreign Policy*, March 16.

Llach, L. (2004) 'A Depression in Perspective: The Economics and the Political Economy of Argentina's Crisis of the Millennium' In: Fiorucci, F. and Klein, M. (eds.) *The Argentine Crisis at the Turn of the Millennium: Causes, Consequences and Explanations*. Amsterdam: Aksant.

Lomnitz-Adler, C. (2004) 'The Depreciation of Life During Mexico City's Transition into the Crisis' In: Schneier, J. and Susser, I. (eds) *Wounded Cities.* New York: Berg, pp. 47-70.

Lynn, M. (2011) *Bust: Greece, the Euro and the Sovereign Debt Crisis.* Hoboken, NK: Wiley.

Mahoney, J. (1999) 'Nominal, Ordinal, and Narrative Appraisal in Macrocausal Analysis' *American Journal of Sociology*, 104(4): 1154-1196.

Mahoney, J. (2007) 'Qualitative Methods and Comparative Politics' *Comparative Political Studies*, 40(2): 122-144.

Mahoney, J. (2010) 'After KKV: The New Methodology of Qualitative Research' *World Politics*, 62(1): 120-147.

Mahoney, J. and Rueschemeyer, D. (eds.) (2003) *Comparative-Historical Analysis in the Social Sciences*. New York: Cambridge University Press.

Mair, P. (2013) *Ruling the Void: The Hollowing of Western Democracy*. London and New York: Verso.

Malamud, A. (2006) 'Social Revolution or Political Takeover? The Argentine Collapse of 2001 Reassessed' *Presented at the XXVI Latin American Studies Association Congress (LASA)*, San Juan, Puerto Rico: March 15-18.

Mallaby, S. (2012) 'This will not be enough, Mr Draghi' *Financial Times*, August 7.

Mandel, E. (1971) *The Marxist Theory of the State*. New York: Pathfinder Press.

Manolopoulos, J. (2011) *Greece's 'Odious' Debt: The Looting of the Hellenic Republic by the Euro, the Political Elite and the Investment Community.* London: Anthem Press.

Marichal, C. (1989) *A Century of Debt Crises in Latin America*. Princeton: Princeton University Press.

Marks, S. (1978) 'The Myths of Reparations' *Central European History*, 11(3): 231-255.

Marois, T. (2007) 'The Lost Logic of State-Owned Banks: Mexico, Turkey, and Neoliberalism' *Paper presented at Canadian Political Science Association 79th annual conference.* University of Saskatchewan, May 31, 2007.

Marois, T. (2011) *The Socialization of Financial Risk in Mexico*. Research on Money and Finance Discussion Paper No. 25. University of London, School of Oriental and African Studies.

Martínez, J. V. and Sandleris, G. (2011) 'Is It Punishment? Sovereign Defaults and the Decline in Trade' *Journal of International Money and Finance,* 30: 909-930

Mason, P. (2013) *Why It's (Still) Kicking Off Everywhere*. London: Verso.

Mauro, P. Sussman, N. and Yafeh, Y. (2006) *Bloodshed or Reforms? The Determinants of Sovereign Bond Spreads in 1870-1913 and Today.* CEPR Discussion Paper No. 5528. London, Center for Economic Policy Research.

Maxfield, S. (1990) *Governing Capital: International Finance and Mexican Politics*. Ithaca, NY: Cornell University Press.

Maxfield, S. (1992) 'The International Political Economy of Bank Nationalization: Mexico in Comparative Perspective' *Latin American Research Review*, 27(1): 75-104

McGillivray, F. and Smith, A. (2000) 'Trust and Cooperation Through Agent-Specific Punishments' *International Organization*, 54(4): 809-24.

McKeown, T. J. (2004) 'Case Studies and the Limits of the Statistical Worldview' In: Brady, H. E. and Collier, D. (eds.) *Rethinking Social Inquiry: Diverse Tools, Shared Standards*. Lanham, MD: Rowman and Littlefield.

Mendoza, E. G. and Yue, V. Z. (2011) *A General Equilibrium Model of Sovereign Default and Business Cycles*. IMF Working Paper 11/166. Washington, D.C., International Monetary Fund.

Mengus, E. (2014) *Honoring Sovereign Debt or Bailing Out Domestic Residents: A Theory of Internal Costs of Default*. Banque de France Working Paper No. 480. Available at: http://ssrn.com/abstract=2417330 (last accessed August 25, 2015).

Merler, S. and Pisani-Ferry, J. (2012) *Sudden Stops in the Euro Area*. Policy Brief No. 2012/06. Brussels: Bruegel.

Middlebrook, K. J. (1989) 'The Sounds of Silence: Organised Labour's Response to Economic Crisis in Mexico' *Journal of Latin American Studies*, 21(2): 195:220.

Miliband, R. (1969) *The State in Capitalist Society.* New York: Basic Books.

Miller, D. A. Tomz, M. and Wright, M. L. J. (2006) 'Sovereign Debt, Defaults and Bailouts' *Mimeo*. Available at: http://www.atl-res.com/macro/papers/Wright%20paper.pdf (last accessed March 3, 2013).

Miller, M. Thampanishvong, K. and Zhang, L. (2004) *Learning to Trust Lula: Contagion and Political Risk in Brazil*. Working Paper, University of Warwick.

Mills, C. W. (1956) *The Power Elite.* New York: Oxford University Press.

Mitchener, K. J. and Weidenmier, M. D. (2005) *Supersanctions and Sovereign Debt Repayment.* Working Paper No. 11472. Cambridge, MA., National Bureau of Economic Research.

Mitchener, K. J. and Weidenmier, M. D. (2011) 'Supersanctions and Sovereign Debt Repayment' In: Kolb, R. W. (ed.) *Sovereign Debt: From Safety to Default.* NY: Wiley.

Modi, A. (2015) 'The IMF's big Greek mistake' *Bruegel blog,* April 27. Available at: http://bruegel.org/2015/04/the-imfs-big-greek-mistake/ (last accessed Sept 7, 2015).

Moffett, M. (2004) 'After Huge Default, Argentina Squeezes Small Bondholders' *Wall Street Journal*, January 14.

Moody's (2000) How to Sue a Sovereign: The Case of Peru. New York, Moody's Investors Service, Special Comment.

Moore, B. (1966) *Social Origins of Dictatorship and Democracy: Lord and Peasant in the Making of the Modern World*. Boston, MA: Beacon Press.

Moore, E. and Hope, K. (2014) 'Size of Greece's debt limits scope for solutions' *Financial Times*, January 13.

Mortimore, M. and Stanley, L. (2006) 'Has Investors Protection Been Rendered Obsolete by the Argentine Crisis?' *CEPAL Review*, 88: 15-31. Mexico City: United Nations Center for the Study of Latin America and the Caribbean.

Mouzakis, Y. (2015) 'Where did all the money go?' *Macropolis*, January 5. Available at: http://www.macropolis.gr/?i=portal.en.the-agora.2080 (last accessed: Sept 7, 2015).

Mügge, D. (2010) *Widen the Market, Narrow the Competition: Banker Interests and the Making of a European Capital Market.* Colchester: ECPR Press.

Mundell, R. A. (1963) 'Capital Mobility and Stabilization Policy under Fixed and Flexible Exchange Rates' *Canadian Journal of Economics and Political Science*, 29(4): 475-485.

Mussa, M. (2002) 'Argentina and the Fund: From Triumph to Tragedy' *Policy Analyses in International Economics*, 67. Washington, DC: Peterson Institute.

North, D. C. and Weingast, B. R. (1989) 'Constitutions and Commitment: The Evolution of Institutions Governing Public Choice in Seventeenth-Century England' *Journal of Economic History,* 49(4): 803-832.

O'Connor, J. (1973) *The Fiscal Crisis of the State. New York: St. Martin's Press.*

Obstfeld, M. and Taylor, A. M. (2003) 'Globalization and Capital Markets' In: *Bordo, M. D. Taylor, A. M. and Williamson, J. G. (eds.) Globalization in Historical Perspective.* Chicago: University of Chicago Press.

Ocampo, J. A. (2013) 'La Crisis de la Deuda a la Luz de la Historia Latinoamericana' *Presented at CEPAL Conference: La Crisis de la Deuda: 30 Años Despues.* Mexico City, 18-19 February 2013.

OECD (2011) *Greece: Review of the Central Administration.* Paris: Organisation for Economic Cooperation and Development. Available at: http://www.oecd-ilibrary.org/governance/greece-review-of-the-central- administration_ 9789264102880-en (accessed August 25, 2015).

Ohmae, K. (1995) 'Putting Global Logic First' *Harvard Business Review,* 73(1): 119-125.

Oliveri, E. J. (1992) *Latin American Debt and the Politics of International Finance*. Westport, CT: Praeger.

OMFIF (2015) 'OMFIF telephone briefing: Greece and Europe after the Brussels debt agreement, with Yanis Varoufakis' London: Official Monetary and Financial Institutions Forum. Full recording available at: http://www.omfif.org/media/ 1067578/omfif-telephone-briefing-greece-and-europe-after-the-brussels-debt-agreement-yanis-varoufakis-16-july.mp4 (last accessed September 7, 2015).

Ozler, S. (1992) *Have Commercial Banks Ignored History?* Working Paper No. 3959. Cambridge MA., National Bureau of Economic Research.

Pagoulatos, G. (2003) *Greece's New Political Economy: State, Finance and Growth from Postwar to EMU*. London: Palgrave McMillan.

Pagoulatos, G. (2014) 'Structural Limitations of Financial Power in Greece' *Government and Opposition*, 49(3): 452-482.

Palaiologos, Y. (2014) 'How Trichet threatened to cut Greece off' *Ekathimerini*, March 11.

Palley, T. I. (2007) *Financialization: What It Is and Why It Matters*. Working Paper No. 525, the Levy Economics Institute of Bard College. Available at: http://levyinstitute.org/ pubs/wp_525.pdf (last accessed August 25, 2015).

Panico, C. and Purificato, F. (2013) *The Debt Crisis and the European Central Bank's Role of Lender of Last Resort*. PERI Working Paper No. 306, Political Economy Research Institute, University of Massachusetts Amherst.

Panitch, L. and Gindin, S. (2013) *The Making of Global Capitalism: The Political Economy of American Empire.* New York and London: Verso.

Panizza, U. Sturzenegger, F. and Zettelmeyer, J. (2009) 'The Economics and Law of Sovereign Debt and Default' *The Journal of Economic Literature,* 47(3): 1-47.

Papademos, L. (2011) 'Forcing Greek restructuring is not the answer' *Financial Times*, October 21.

Pastor Jr., M. (1987) 'The Effects of IMF Programs in the Third World: Debate and Evidence from Latin America' *World Development*, 15(2): 249-262.

Pastor Jr., M. (1989) 'Latin America, the Debt Crisis, and the International Monetary Fund' *Latin American Perspectives*, 16(1): 79-110.

Pastor Jr., M. and Wise, C. (1991) *Peruvian Economic Policy in the 1980s: From Orthodoxy to Heterodoxy and Back*. WorkingPaper No. 161. Notre Dame: Kellogg Institute. https://www3.nd.edu/ ~ kellogg/publications/workingpapers/WPS/161.pdf (last accessed January 31, 2015).

Pauly, L. W. (1997) *Who Elected the Bankers? Surveillance and Control in the World Economy.* Ithaca, NY: Cornell University Press.

Pescatori, A. and Sy, A. N. R. (2007) 'Are Debt Crises Adequately Defined?' *IMF Staff Papers,* 54(2): 306-337.

Peters, B. G. (1998) *Comparative Politics: Theory and Methods*. New York, NY: NYU Press.

Pezzolo, L. (2007) *Government Debts and Credit Markets in Renaissance Italy*. Working Paper No 05/2007, Department of Economics, Ca' Foscari University of Venice.

Piketty, T. (2014) *Capital in the Twenty-First Century.*

Polanyi, K. (1944 [2001]) *The Great Transformation: The Political and Economic Origins of Our Time*. Boston, MA: Beacon Press.

Pontusson, J. (1995) 'From Comparative Public Policy to Political Economy: Putting Political Institutions in their Place and Taking Interests Seriously' *Comparative Political Studies*, 28(1): 117-147.

Poulantzas, N. (1969) 'The Problem of the Capitalist State' *New Left Review,* 58: 67-78.

Poulantzas, N. (1973) *Political Power and Social Classes*. London: New Left Books.

Poulantzas, N. (1978) *State, Power, Socialism*. London: New Left Books/Verso.

Przeworski, A. (1980) 'Social Democracy as a Historical Phenomenon' *New Left Review,* 122: 27-58.

Przeworski, A. and Wallerstein, M. (1988) 'Structural Dependence of the State on Capital' *The American Political Science Review,* 82(1): 11-29.

Quirk, W. J. (1983) 'Will an Underdeveled Countries Debtors' Cartel Squeeze the Big Banks?' *Business and Society Review*, 47(1): 10.

Rabobank (2011) *To Default or Not to Default? What are the economic and political costs of sovereign default?* Utrecht, Rabobank Economic Research Department.

Ragin, C. C. (2008) *Redesigning Social Inquiry: Fuzzy Sets and Beyond*. Chicago, IL: University of Chicago Press.

Rambarran, J. (2004) 'Argentina's Sovereign Default and the IMF: Global Governance in a Tailspin' *Mimeo*, UWI St. Augustine.

Reguly, E. (2013) 'George Provopoulos: facing a run on Greek banks, he never blinked' *Globe & Mail*, April 19.

Reinhart, C. M. and Rogoff, K. S. (2008) *This Time is Different: A Panoramic View of Eight Centuries of Financial Crises.* NBER Working Paper No. 13882. Cambridge, MA., National Bureau of Economic Research.

Reinhart, C. M. and Rogoff, K. S. (2009) *This Time Is Different: Eight Centuries of Financial Folly*. Princeton: Princeton University Press.

Reinhart, C. M. Rogoff, K. S. and Savastano, M. A. (2003) *Debt Intolerance*. NBER Working Paper No. 9908. Cambridge, MA: National Bureau of Economic Research.

Reinhart, C. M., Reinhart, V. and Trebesch, C. (2016) 'Global Cycles: Capital Flows, Commodities, and Sovereign Defaults, 1815-2015' *American Economic Review: Papers and Proceedings* (forthcoming, May).

Reuters (2015) 'German bank exposure to Greece around 24 billion euros: banks' *Reuters*, January 5.

Robinson, D. Wagstyl, S. and Milne, R. (2015) 'Brussels backs IMF over Greek debt relief' *Financial Times*, August 13.

Robinson, J. A. (1998) 'Debt Repudiation and Risk Premia: The North-Weingast Thesis Revisited' Available at: http://www.wcfia.harvard.edu/sites/default/files/897__jr_North1.pdf (last accessed 3 March 2013).

Robinson, W. I. (2004) 'Global Crisis and Latin America' *Bulletin of Latin American Research*, 23(2): 135-153.

Rock, D. (2002) 'Racking Argentina' *New Left Review*, 17: 55-86.

Roddick, J. (1988) *The Dance of the Millions: Latin America and the Debt Crisis*. London: Latin America Bureau.

Rodrik, D. (2011) *The Globalization Paradox: Why Global Markets, States, and Democracy Can't Coexist.* New York: Oxford University Press.

Rodrik, D. and Subramanian, A. (2009) *Why Did Financial Globalization Disappoint?* IMF Staff Paper No. 56: 112–138.

Rogoff, K. (1999) 'International Institutions for Reducing Global Financial Instability' *Journal of Economic Perspectives,* 13(4): 21-42.

Roodman, D. (2006) 'Creditor Initiatives in the 1980s and 1990s' In: Jochnick, C. and Preston, F. A. (eds.) *Sovereign Debt at the Crossroads: Challenges and Proposals for Solving the Third World Debt Crisis.*

Rose-Ackerman, S. Desierto, D. and Volosin, N. (2010) 'Hyper-Presidentialism: Separation of Powers Without Checks and Balances in Argentina and the Philippines. Yale Law & Economics Research Paper No. 418.

Rose, A. K. (2005) 'One Reason Countries Pay Their Debts: Renegotiation and International Trade' *Journal of Development Economics, 77: 189–206.*

Roth, K. H. (2013) *Greece: What Is to Be Done?* Alresford, UK: Zer0 Books.

Roubini, N. (2005) 'The Successful End of the Argentine Debt Restructuring Saga' *Economonitor*. Article available at: http://www.economonitor.com/nouriel/2005/03/02/the-successful-end-of-the-argentine-debt-restructuring-saga (accessed May 30, 2014).

Roubini, N. (2012) 'Greece's private creditors are the lucky ones' *Financial Times*, Mar 7.

Ruparel, R. and Persson, M. (2011) *A House Built on Sand? The ECB and the Hidden Cost of Saving the Euro*. London: Open Europe.

Sachs, J. D. (1986) 'Managing the LDC Debt Crisis' *Brookings Papers on Economic Activity*, 1968(2): 397-440.

Sachs, J. D. and Huizinga, H. (1987) 'US Commercial Banks and the Developing Country Debt Crisis' *Brookings Papers on Economic Activity*, 1987(2): 555-606.

Saiegh, S. M. (2005a) 'Can Democracy Prevent Default?' In: Centeno, M. A. James, H. and Londregan, J. (eds.) *The Political Economy of Recurrent Debt.* Princeton, N.J.: PIIRS.

Saiegh, S. M. (2005b) 'Do Countries Have a 'Democratic Advantage'? Political Institutions, Multilateral Agencies, and Sovereign Borrowing' *Comparative Political Studies,* 38(4): 366-87.

Salmon, C. (2015) ''We underestimated their power': Greek government insider lifts the lid on five months of 'humiliation' and 'blackmail'' *Mediapart*, July 8. Available at: http://www.mediapart.fr/journal/international/080715/we-underestimated-their-power-greek-government-insider-lifts-lid-five-months-humiliation-and-blackm (last accessed September 7, 2015).

Sandleris, G. (2008) 'Sovereign Defaults: Information, Investment and Credit' *Journal of International Economics*, 76: 267-275.

Sandleris, G. (2010) 'Sovereign Defaults, Credit to the Private Sector and Domestic Credit Market Institutions' Available at: http://www.udesa.edu.ar/files/UAEconomia/Seminarios/2010/Sandleris.pdf (last accessed 3 March 2013).

Santiso, J. (2003) *The Political Economy of Emerging Markets: Actors, Institutions, and Financial Crises in Latin America*. New York: Palgrave.

Sartori, G. (1970) 'Concept Misformation in Comparative Politics' *The American Political Science Review,* 64(4): 1033-1053.

Schadler, S. (2013) *Unsustainable Debt and the Political Economy of Lending: Constraining the IMF's Role in Sovereign Debt Crises.* CIGI Paper No. 19, October. Waterloo, ON: Center for International Governance Innovation.

Schamis, H. E. (2002a) 'Argentina: Crisis and Democratic Consolidation' *Journal of Democracy*, 13(2): 81-94.

Schamis, H. E. (2002b) *Re-forming the State: The Politics of Privatization in Latin America and Europe.* Ann Arbor: University of Michigan Press.

Schattschneider, E. E. (1960) *The Semisovereign People: A Realist's View of Democracy in America.* New York: Holt, Rinehart and Winston.

Schultz, K. A. and Weingast, B. R. (1998) 'Limited Governments, Powerful States' In: Siverson, R. M (ed.) *Strategic Politicians, Institutions, and Foreign Policy*. Ann Arbor: University of Michigan Press.

Schumacher, J. Trebesch, C. and Enderlein, H. (2014) *Sovereign Defaults in Court*. Available at SSRN: http://ssrn.com/abstract=2189997 (last accessed Aug 25, 2015).

Schumpeter, J. A. (1918 [1953]) 'The Crisis of the Tax State' In: Peacock, Alan T. (ed.) *International Economic Papers*, No. 4. London: MacMillan, pp. 5-38.

Schuster, F. L. (2008) 'Argentina – The Left, Parties and Movements: Strategies and Prospects' In: Barrett, P., Chavez, D. and Rodriguez-Garavito, C. (eds.) *The New Latin American Left: Utopia Reborn*. London: Pluto Press and Amsterdam: Transnational Institute.

Scott, H. S. (2006) *Sovereign Debt Default: Cry for the United States, Not Argentina.* Critical Legal Issues Working Paper No. 140. Washington, D.C.: Washington Legal Foundation.

Seawright, J. and Gerring, J. (2008) 'Case Selection Techniques in Case Study Research: A Menu of Qualitative and Quantitative Options' *Political Research Quarterly*, 61(2): 294-308.

Setser, B. and Gelpern, A. (2006) 'Pathways through Financial Crisis: Argentina' *Global Governance*, 12: 465-487.

Silva Herzog, J. (1991) 'Problems of Policy-Making at the Outset of the Debt Crisis' In: Dornbusch, R. and Marcus, S. (eds.) *International Money and Debt: Challenges for the World Economy*. San Francisco, CA: ICS Press.

Sitrin, M. (2012) *Everyday Revolutions: Horizontalism and Autonomy in Argentina*. London: Zed Books.

Skiles, M. E. (1988) 'Latin American International Loan Defaults in the 1930s: Lessons for the 1980s?' *Working Paper.* New York: Federal Reserve Bank of New York.

Skocpol, T. (1979) *States and Social Revolutions: A Comparative Analysis of France, Russia and China.* Cambridge: Cambridge University Press.

Skocpol, T. and Somers, M. (1980) 'The Uses of Comparative History in Macrosocial Inquiry' *Comparative Studies in Society and History*, 22(2): 174-197.

Smith, H. (2014) 'How Greece pulled back from the brink of plunging Europe into chaos' *The Guardian*, May 22, 2014.

Smith, H. (2015a) 'Greek minister moves to allay fears of bank run' *The Guardian*, Jan 9.

Smith, H. (2015b), 'Young, gifted and Greek: Generation G – the world's biggest brain drain' *The Guardian*, January 19, 2015.

Soederberg, S. (2005) 'The Transnational Debt Architecture and Emerging Markets: The Politics of Paradoxes and Punishment' *Third World Quarterly,* 26(6): 927-949.

Solanas, F. E. (2004) *El Saqueo de la Argentina/Argentina's Economic Collapse*. Documentary film about the Argentine crisis. Available at: https://www.youtube.com/watch?v=0CzS6eHqtnQ (last accessed May 30, 2014).

Spiegel, P. (2014) 'How the euro was saved' *Financial Times*, May 11.

Spiegel, P. (2015) 'How Jeroen Dijsselbloem did the deal to extend the Greece bailout' *Financial Times,* March 1.

Spiegel, P. and Wagstyl, S. (2015) 'Greece's Alexis Tsipras faces Syriza rebellion over 'humiliation'' *Financial Times*, July 14.

Stallings, B. (2013) 'La dinámica de las negociaciones' *Presented at CEPAL Conference: La Crisis de la Deuda: 30 Años Despues.* Mexico City, 18-19 February 2013.

Stamouli, N. and Walker, M. (2015) 'How Alexis Tsipras's Greek Referendum Call Came After Creditors Covered His Proposals in Red Ink' *The Wall Street Journal*, June 28.

Stangos, A. (2014) 'The costs of protests' *Kathimerini*, May 9.

Stasavage, D. (2002) 'Credible Commitment in Early Modern Europe: North and Weingast Revisited' *The Journal of Law, Economics and Organization,* 18(1): 155-186.

Stasavage, D. (2007a) 'Partisan Politics and Public Debt: The Importance of the 'Whig Supremacy' for Britain's Financial Revolution' *European Review of Economic History,* 2: 123-153.

Stasavage, D. (2007b) 'Cities, Constitutions, and Sovereign Borrowing in Europe, 1274-1785' *International Organization*, 61: 489-525.

Stasavage, D. (2011) *States of Credit: Size, Power, and the Development of European Polities.* Princeton, NJ: Princeton University Press.

Sterling, T. (2015) 'Greek 'no' risks place in eurozone – Dijsselbloem' *Reuters*, July 2.

Stiglitz, J. E. (2002) *Globalization and its Discontents*. New York, NY: W. W. Norton.

Stiglitz, J. E. (2011) 'Of the 1%, by the 1%, for the 1%' *Vanity Fair*, April 30.

Stinga, L. (2009) 'Still Elected Dictators? A Study of Executive Accountability in Multi-Party Democracies' *Presented at ECPR Joint Session Workshops*, Rennes, April 11.

Story, J. (2000) 'Setting the Parameters: A Strange World System' In: Lawton, T. C. and Verdun, A. C. (eds.) *Strange Power: Shaping the parameters of international relations and international political economy.* Farnham: Ashgate.

Strange, S. (1988) *States and Markets*. Oxford: Blackwell Publishers.

Strange, S. (1991) 'Big Business and the State' *Millennium: Journal of International Studies*, 20(2): 245-250.

Strange, S. (1994) 'Wake up Krasner! The World Has Changed' *Review of International Political Economy,* 1: 209-219.

Strange, S. (1996) *The Retreat of the State: The Diffusion of Power in the World Economy*. Cambridge: Cambridge University Press.

Strange, S. (1998) *Mad Money: When Markets Outgrow Governments*. Manchester: University of Michigan Press.

Streeck, W. (2011) 'The Crises of Democratic Capitalism' *New Left Review*, 71: 5-29.

Streeck, W. (2013) *The Politics of Public Debt: Neoliberalism, Capitalist Development, and the Restructuring of the State.* MPIfG Discussion Paper 13/7, Cologne: Max Planck Institute for the Study of Societies.

Streeck, W. (2014) *Buying Time: The Delayed Crisis of Democratic Capitalism*. London and New York: Verso.

Streeck, W. (2015) *The Rise of the European Consolidation State*. MPIfG Discussion Paper 15/1, Cologne: Max Planck Institute for the Study of Societies.

Strupczewski, J. (2015) 'Counting the cost for Greece and Europe' *Reuters,* July 17.

Stucker, D. and Basu, S. (2014) *The Body Economic: Why Austerity Kills*. New York, NY: Basic Books.

Sturzenegger, F. and Zettelmeyer, J. (2006) *Debt Defaults and Lessons from a Decade of Crises.* Cambridge, MA.: MIT Press.

Sussman, N. and Yafeh, Y. (2000) 'Institutions, Reforms, and Country Risk: Lessons from Japanese Government Debt in the Meiji Era' *Journal of Economic History*, 60(2): 442-67.

Suter, C. and Stamm, H (1992) 'Coping with Global Debt Crises Debt Settlements, 1820 to 1986' *Comparative Studies in Society and History*, 34(4): 645-678.

Sweezy, P. (1942) *The Theory of Capitalist Development.* New York: Monthly Review Press.

Tabak, M. (1999) 'A Poulantzasian Approach to the State and Globalization' *Journal of the Hellenic Diaspora* 25(1-2): 135-155.

Teichman, J. A. (2001) *The Politics of Freeing Markets in Latin America: Chile, Argentina and Mexico.* Chapel Hill, NC: University of North Carolina Press.

Tello, C. (1984) *La Nacionalización de la Banca en Mexico*. Mexico, DF: Siglo XXI.

Thomas, L. (2012) 'Buying Back Greek Debt Rewarded Hedge Funds' *New York Times,* December 23.

Thomas, L. (2013a) 'In Greece, the Banking Chief Draws Scrutiny' *New York Times*, October 16.

Thomas, L. (2013b) 'Greek plan may reward some bank executives' *New York Times*, June 25.

Thomas, P. (2002) 'Bringing Poulantzas Back In' In: Aronowitz, S. and Bratsis, P. (eds.) *Paradigm Lost: State Theory Reconsidered.* Minneapolis: University of Minnesota Press.

Thompson (2015) 'Greek bank shares hit as deposits flee' *Financial Times*, January 27.

Tomz, M. (2002) 'Democratic Default: Domestic Audiences and Compliance with International Agreements' *Presented at the 2002 Annual Meeting of the American Political Science Association.* Boston, August 29-September 1.

Tomz, M. (2007) *Reputation and International Cooperation: Sovereign Debt across Three Centuries.* Princeton: Princeton University Press.

Tomz, M. and Wright, M. L. J. (2007) 'Do Countries Default in "Bad Times"?' *Journal of the European Economic Association,* 5(2-3): 352-360.

Tomz, M. and Wright, M. L. J. (2008) 'Sovereign Theft: Theory and Evidence about Sovereign Default and Expropriation' *Presented at the Conference on Populism and Natural Resources.* Kennedy School of Government, Harvard University, 1– 2 November 2007.

Treanor, J. (2010) 'France and Switzerland most exposed to Greece's debt crisis, say analysts' *The Guardian*, February 11.

Truth Committee on Public Debt (2015) *Preliminary Report*. Athens: Hellenic Parliament. Available at: http://cadtm.org/IMG/pdf/Report.pdf (last accessed September 7, 2015).

Turner, F. C. and Carballo, M. (2005) 'Argentina: Economic Disaster and the Rejection of the Political Class ' *Comparative Sociology*, 4(1-2): 175-206.

Tussie, D. (1988) 'The Coordination of the Latin American Debts: Is There a Logic Behind the Story?' In: Griffith-Jones, S. (ed.) *Managing World Debt.* New York: St. Martin's.

Tussie, D. (2013) 'El Fracaso del Consenso de Cartagena' *Presented at CEPAL Conference: La Crisis de la Deuda: 30 Años Despues.* Mexico City, 18-19 February 2013.

Ugarteche, O. (2013) 'La Crisis de la Deuda desde la Perspectiva Histórica Global y Latinoamericana' *Presented at CEPAL Conference: La Crisis de la Deuda: 30 Años Despues.* Mexico City, 18-19 February 2013.

Underhill, G. R. D. and Zhang. X. (2008) 'Setting the Rules: Private Power, Political Underpinnings, and Legitimacy in Global Monetary and Financial Governance' *International Affairs,* 84(3): 535-554.

UNICEF (1989) *Children in Jeopardy: The Challenge of Freeing Poor Nations from the Shackles of Debt.* New York: UNICEF.

Van Wijnbergen, S. (1991) 'Mexico and the Brady Plan' *Economic Policy*, 6(12): 13-56.

Van Wijnbergen, S. (2013) Interview with the author. Amsterdam School of Economics, University of Amsterdam: January.

Varoufakis, Y. (2013) 'Johnny (Paulson) Got His Gun (and is aiming at some grim, Greek pickings)' *Yanis Varoufakis' blog*, October 7. Available at: http://yanisvaroufakis.eu/2013/10/07/johnny-paulson-got-his-gun-and-is-aiming-at-some-grim-greek-pickings/ (last accessed January 31, 2015).

Varoufakis, Y. (2014) 'Burst Greek Bubbles, Spooked Fund Managers: A Cause for Restrained Celebration' *Yanis Varoufakis' blog*, December 7. Available at: http://yanisvaroufakis.eu/2014/12/07/burst-greek-bubbles-spooked-fund-managers-a-cause-for-restrained-celebration/ (last accessed January 31, 2015).

Vennesson, P. (2008) 'Case Studies and Process Tracing: Theories and Practices' In: Della Porta, D. and Keating, M. eds. *Approaches and Methodologies in the Social Sciences: A Pluralist Perspective*. Cambridge: Cambridge University Press.

Verdun, A. C. (2000) 'Money Power: Shaping the Global Financial System' In: Lawton, T. C. and Verdun, A. C. (eds.) *Strange Power: Shaping the parameters of international relations and international political economy.* Farnham: Ashgate.

Vogel, D. (1987) 'Political Science and the Study of Corporate Power: A Dissent from the New Conventional Wisdom' *British Journal of Political Science*, 17(4): 385-408.

Vreeland, J. R. (2001) 'The Effect of IMF Programs on Labor' *World Development*, 30(1): 121-139.

Wade, R. H. (1990) *Governing the Market: Economic Theory and the Role of Government in East Asian Industrialization*. Princeton: Princeton University Press.

Wade, R. H. (2014) '“Market versus State” or “Market with State”: How to Impart Directional Thrust' *Development and Change*, 45(4): 777-798.

Wade, R. H. and Veneroso, F. (1998) 'The Asian Crisis: The High Debt model Versus the Wall Street-Treasury-IMF Complex' *New Left Review*, I/228, March-April.

Wagstyl, S. (2015) 'Germany criticizes Greek bailout agreement' *Financial Times*, August 12.

Waldenström, D. (2011) 'How Important Are the Political Costs of Domestic Default?: Evidence from World War II Bond Markets' In: Kolb, R. W. (ed.) *Sovereign Debt: From Safety to Default.* New York: Wiley.

Walker, M. and Kakaounaki, M. (2012) 'Greeks brace for more pain on wages' *Wall Street Journal*, July 19.

Wall Street Journal (2013) 'IMF Document Excerpts: Disagreements Revealed' *Wall Street Journal*, October 7. Available at: http://blogs.wsj.com/economics/2013/10/07/imf-document-excerpts-disagreements-revealed/ (last accessed August 24, 2015).

Wallerstein, I. (1974) 'The Rise and Future Demise of the World Capitalist System: Concepts for Comparative Analysis' *Comparative Studies in Society and History*, Vol. 16, No. 4: pp. 387-415.

Walter, A. (2001) 'Unravelling the Faustian Bargain: Non-State Actors and the Multilateral Agreement on Investment' In: Josselin, D. and Wallace, W. (eds.) *Non-State Actors in World Politics.* Basingstoke, UK: Palgrave Macmillan.

Walton, J. and Ragin, C. (1989) 'Global and National Sources of Political Protest: Third World Responses to the Debt Crisis.' *American Sociological Review*, 55(6): 876-890.

Waltzenbach, G. P. E. (2000) 'The Doubtful Handshake: From International to Comparative Political Economy?' In: Lawton, T. C. and Verdun, A. C. (eds.) *Strange Power: Shaping the parameters of international relations and international political economy.* Farnham: Ashgate.

Watkins, S. (2014) 'The Political State of the Union' *New Left Review* 90, Nov-Dec.

Weeks, N. and Ziotis, C. (2012) 'Greek bank deposits fell 2% in November after October plunge' *Bloomberg*, January 10.

Weisbrot, M. and Cibils, A. B. (2002) *Argentina's Crisis: The Costs and Consequences of Default for the International Financial Institutions*. CEPR Policy Brief. Washington, DC: Center for Economic and Policy Research.

Williamson, J. (2002) *Is Brazil Next?* International Economics Policy Brief No. PB 02-7. Washington, DC: Institute for International Economics.

Winkler, M. (1933) *Foreign Bonds: An Autopsy – A Study of Defaults and Repudiations of Government Obligations*. Philadelphia: Roland Swain Company.

Winters, J. A. (1994) 'Governing Capital: International Finance and Mexican Politics – Maxfield, S.' *World Politics*, 46(3), pp. 419-452.

Wolf, M. (2012) 'A fragile Europe must change fast' *Financial Times*, May 22.

Wood, R. E. (1984) 'The Debt Crisis and North-South Relations' *Third World Quarterly*, 6(3): 703-716.

World Bank (1983) *Focus on Poverty*. Washington, D.C.: World Bank.

World Bank (2015), *International Debt Statistics*. Washington, D.C.: World Bank. Available at: http://data.worldbank.org/news/International-Debt-Statistics-2015-now-available (last accessed August 25, 2015).

Wright, M. L. J. (2010) Restructuring Sovereign Debts with Private Sector Creditors: Theory and Practice. *Prepared for the World Bank' Economic Policy and Debt Department in Cooperation with the African Development Bank conference.* Tunisia, 29-30 March 2010.

Wucker, M. (2003) 'Searching for Argentina's Silver Lining' *World Policy Journal*, 19(3): 49-58.

Wynne, W. (1951) *State Insolvency and Foreign Bondholders: Selected Case Histories of Governmental Foreign Bond Defaults and Debt Readjustments, Volume II*. London: Oxford University Press.

Zettelmeyer, J. Trebesch, C. and Gulati, G. M. (2013) *The Greek Debt Restructuring: An Autopsy*. Working Paper No 2013-13-8. Washington, DC: Peterson Institute for International Economics.

Zibechi, R. (2003) *Genealogía de la Revuelta: Argentina, la Sociedad en Movimiento*. Buenos Aires: Herramienta.