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HUMAN RIGHTS, SOVEREIGN DEBT AND WHY STATES SHOULD NOT KEEP THEIR PROMISES

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ABSTRACT

When should binding debt contracts not be repaid? This article argues that whenever the repayment of sovereign debt threatens the human rights of the citizenry, this provides a weighty normative reason to prioritize the fulfilment of the latter over the former. Since there are specific, non-coincidental reasons to fear that a high indebtedness of states may result in the undermining of the socio-economic and the collective human rights of a state's citizenry, the more specific thesis defended in this article is the following: whenever debt repayment undermines the socio-economic and collective human rights of the state´s citizenry, states have a normatively weighty reason to prioritize the fulfilment of the citizen's human rights over meeting their contractual debt payment obligations vis-à-vis their creditors.

Keywords: Sovereign Debt, Debt Repayment, Human Rights, Global Justice, Critiques of Capitalism.

RESUMEN

¿Hay situaciones en la cuales el estado no debería pagar una deuda soberana adquirida de forma legítima? Este artículo sostiene que cuando el pago de deuda no odiosa viola los derechos humanos de la ciudadanía, esto constituye una razón normativa importante para priorizar los derechos humanos por sobre el pago de la deuda soberana. Dado que existen razones específicas, no casuales, para temer que un alto endeudamiento de los estados pueda resultar en el socavamiento de los derechos humanos socioeconómicos y colectivos de la ciudadanía, este artículo defiende lo siguiente: cuando el pago de la deuda socava los derechos humanos, los estados tienen una razón normativa importante para priorizar el cumplimiento de estos últimos sobre el cumplimiento de sus obligaciones contractuales de pago de deuda frente a sus acreedores.

Palabras clave: Deuda Soberana, Repago de la Deuda, Derechos Humanos, Justicia Global, Críticas al Capitalismo.

I. Introduction

Contracts matter. They matter for all sorts of reasons. We might think that it is integral to the autonomy and moral personhood of individuals to take responsibility for their own actions and that keeping one's promises shows respects for other persons. Or we may think that failing to uphold our contractual obligations violates a duty of fair play.[1] These deontological considerations seem to give a prima facie obligation to fulfil past promises. Consequentialist reasons further strengthen this prima facie obligation. Keeping one's promises allows agents to enter mutually beneficial agreements and provides agents incentives to make prudent decisions, since they know that they will be held responsible for them.[2] In short: contracts matter. And since they do, we better ought to abide by them.

Or should we not? This is the question I set out to answer in this paper. I do so with respect to one specific type of contract,

1. For a more elaborate account of these arguments, see Barry and Tomitova (2006) and Reddy (2007).

2. For a more extensive justification of this point, see Reddy (2007).

namely sovereign debt contracts. Sovereign states break the terms of the agreement made when accruing debt more often than one might think. Indeed, evidence suggests that they do so quite often.[3] This is not what I am concerned with here, however. What interests me is not if and how often they do so, but when they ought to do so. More specifically, I am interested in defending one particular instance in which sovereign states should override a perfectly legitimate debt contract, or, more specifically still; identify the conditions under which they at least have weighty normative reasons to do so.[4] The answer I provide is the following: whenever servicing a perfectly legitimate sovereign debt contract comes at the expense of violating its citizen's human rights, this provides a weighty normative reason to default on their debt.

To make this argument I draw inspiration from two central ideas exposed in *World Poverty and Human Rights*, namely Pogge´s critique of what he calls 'explanatory nationalism' and his 'international borrowing privilege'.[5] Moreover, my analysis is embedded in a specific historical time period, namely the period from 1971 to the present. To that extent, "I don't claim to have achieved any great distance from the social world in which I live".[6] Rather than leaving the cave, climbing the mountain and constructing an objective, universal standpoint, "I mean to stand in the cave, in the city, on the ground".[7] Therefore, an important first step of this paper is to lay out how what I call the 'Sovereign Debt Regime' has evolved from

3. Reinhart and Rogoff, 2009.

4. Saying that there are reasons to override a binding debt contract does not entail that the debt contract is non-binding to begin with. It means, instead, that weighty normative reasons exist not to keep a binding debt contract. Put differently, it entails that there are normative reasons that *outweigh* the normative reasons to keep the contract.

5. Pogge, 2008.

6. Walzer, 1983, p. xiv.

7. Walzer, 1983, p. xiv.

1971 to the present. Portraying the relevant facts accurately is already a meaningful contribution to make, and a necessary condition to evaluate these practices normatively. From the vantage point of this historical time period, I argue, second, that the specific nature of sovereign debt contracts is such that we have reason to worry about the undermining of two particular types of human rights in particular, namely the socio-economic and collective rights of citizens of highly indebted states.

The argument provided is the first normative defence – to the best of my knowledge – of human rights as weighty normative reasons to override binding debt contracts. To be sure, odious debt scholars have long pointed at the relevance of human rights when arguing that a sovereign state that violates the human rights of its citizens cannot legitimately accrue debt. Any debt contract made by a regime that violates its citizen's human rights is illegitimate and non-binding by definition.[8] To this day, however, no scholar has argued that the prospect of not being able to fulfil the human rights of

8. First developed after the Spanish American War of 1898 and later formalized by Alexander Sack in 1927, the classical legal doctrine of odious debt has proven hugely successful in challenging the repayment of debt accrued by autocratic regimes The doctrine consists of two provisos, the first of which focuses on the nature of the regime that contracted the debt (the regular government proviso), and the second which concentrates on the purpose and use given to the debt accrued (the public interest proviso). According to Sack, both provisos are sufficient conditions. That implies that "if a debt was in fact incurred to benefit the people, then it should not be considered odious even if it lacked popular consent." In contrast, Gosseries shows that while the second proviso alone may be sufficient, the first proviso alone is not. According to Gosseries, it is the second proviso that does the normative heavy lifting (Gosseries, 2007). Despite this disagreement on whether or not the first proviso is a sufficient condition, scholars working with the odious debt doctrine agree that from a normative standpoint, the second proviso is the most significant one (Toussaint, 2016). Two authors who develop the two provisos by making reference to human rights and human rights violation are Raffer (2007) and Dimitriu (2011, 2017).

its citizenry can also provide a normative ground to override perfectly legitimate and binding debt contracts.

My argument differs from the arguments made by odious debt scholars in that I am not interested in evaluating the conditions under which a debt contract is non-binding. This is the question that odious debt scholars are concerned with. I am interested in the question of when a binding debt contract ought to be overridden. The difference is substantial: claiming that a binding debt contract ought to be overridden does recognize the legitimacy of the initial debt contract, whereas simply stating that the contract is non-binding does not.

I proceed as follows: After introducing the relevant aspects of Pogge´s theory in Section I, I provide what I call a 'global explanation of a country's sovereign debt history' in Section II. On this basis, in Section III I defend the main thesis briefly outlined here; the idea, that is, that the fulfilment of its citizen's human rights may trump a state's obligation of keeping its debt servicing promises.

II. Explanatory Nationalism, the Global Order and Human Rights

Pogge makes two central arguments which are of relevance for the question that concerns us here. First, the overarching argument or 'general normative outlook'[9] that Pogge defends is the following: The global order harms the global poor by treating them unjustly. They are treating them unjustly because 'we citizens of the rich countries' enforce rules that violate the human rights of 'the global poor' and that could be changed in ways that would relieve most of the world´s

9. Cohen in Jaggar, 2010, p. 20.

extreme poverty.[10] Poverty undermines both socio-economic and collective human rights. Socio-economic rights encompass rights such as the right "to a standard of living adequate for the health and well-being of oneself and one´s family, including food, clothing, housing, and medical care".[11] Collective rights, in turn, include the right to development and to political self-determination. If an individual suffers from poverty, her socio-economic rights are undermined by definition, while her collective rights are progressively eroded as a consequence therefrom. Pogge claims:

> *"Socioeconomic rights, are currently, and by far, the most frequently unfulfilled human rights. Their widespread underfulfillment also plays a major role in explaining global deficits in civil and political human rights demanding democracy, due process, and the rule of law. Extremely poor people – often physically and mentally stunted owing to malnutrition in infancy, illiterate owing to lack of schooling, and much preoccupied with their family's survival – can cause littler harm or benefit to the politicians and bureaucrats who rule them" (2008, p. 97-98).*

The second relevant contribution that Pogge makes is what he terms'explanatory nationalist'[12] explanations for poverty. An explanatory nationalist reading of poverty sustains that domestic policies determine the fate of a particular country and its citizenry: whereas good domestic policies can result in development, growth and poverty reduction, bad domestic policies and / or corruption reproduce poverty. In its most extreme version, explanatory nationalism negates all responsibility of 'the affluent few'. For if the global order really were to harm the global poor, impressive developments

10. Cohen in Jaggar, 2010, p. 20.
11. UDHR, Article 25.
12. Pogge, 2008.

such as the one witnessed by the Asian tigers would not be possible.

To show that explanatory nationalism "is quite true on the whole, but also totally one-sided,"[13] Pogge invites us to think of a class with great variation in student performance. Although variation in performance will undoubtedly be influenced by student-specific factors, it does not follow that these factors alone explain the performance of the class. Other 'global' factors, such as the quality of the teacher's teaching, also impact the overall student performance. Similarly, while bad policies might indeed be an explanatory variable in poverty, this does not prove global factors to be inert. The reason why explanatory nationalism explanations for poverty are 'totally one sided', then, is because they "hold fixed, and thereby entirely ignore, the economic and geopolitical context in which the national economies and governments of the poorer countries are placed" in[14]

Pogge's theory is anything but uncontentious and many have pointed at important problems with the 'general normative outlook' that the global order harms the poor by violating their human rights.[15] The argument I wish to make here does not depend on it. Pogge's theory does, however, provide a promising starting point to think through the question that concerns us in this paper – the question, that is, of the circumstances under which an otherwise binding debt contract ought to be overridden. For what Pogge suggests is that the type of explanation provided (whether it is a global or an explanatory-nationalist explanation) conditions the normative conclusions we draw therefrom. The explanations provided condition our thinking and draw or deviate attention from different phenomena that are normatively

13. Pogge, 2008, p. 145.
14. Pogge, 2008, p. 149.
15. Risse 2005, Jaggar 2010.

salient. Different explanations bring into focus different kinds of evidence. According to Pogge, global explanations are ultimately, both more compelling and more revealing of the type of injustices that characterize the global order. It is this global explanation that brings his overarching argument into the fore; the insight that in the current global order, human rights are systematically being violated in a manner that could be avoided by those who benefit from it.

In the next two sections I take this as a starting point, first, to complement the explanatory nationalist story usually told about a country's sovereign debt history and, second, to show why in moments of crisis debt repayment may threaten the fulfilment of the collective and socio-economic rights of the debtor state's citizenry. I argue that if continued debt servicing results in the violation of the socio-economic and collective rights of a state's citizenry, this provides us with strong normative reasons to override otherwise binding debt contracts.

III. Explanatory Nationalism and Sovereign Debt Histories

Sovereign states have rich debt histories – histories of acquisition and servicing of debt, of default and restructuring; histories of moderate debt levels that become unsustainable and of exorbitantly high levels of debt which never do; histories of crises, and – by no means less central - histories of responses to these crises. So far, these histories have been explained with reference to one particular narrative: an explanatory nationalist story about a sovereign state which, in a position of freedom and equality, decides to accrue debt. If a crisis erupts and the state is no longer able to service its debt, then this default is the debtor country's responsibility. Emphasis is laid on the bad management of the debtor country, on expansionary macroeconomic policies, and on fiscal deficits leading to the accumulation of unsustainable levels of debt.[16] It only seems right, so this explanatory nationalist story continues, to insist that such a state service its debt, for contracts carry normative force and ought to be obeyed. Failing to live up to this contractual obligation, moreover, becomes a sign of irresponsibility on the part of the sovereign and provides good reasons to police, via various degrees of persuasion and intervention, the future policy choices of such a political pariah.

The explanatory nationalist story is embodied in the sovereign debt regime. The sovereign debt regime can be defined as all those formal and informal institutions that govern the extension and repayment of debt.

First, on the level of principle, the repayment norm governs the sovereign debt regime: the idea, that is, that "sovereign borrowers must repay, regardless of the circumstances of the initial debt contract, the actual use given to the proceeds, or the exigencies of any potential default".[17] The legal expression of this 'repayment norm' is Pacta Sunt Servanda – agreements must be kept.[18] As put by Barry and Tomitova: "Pacta Sunt Servanda, or 'pacts must be respected,' is the basic norm that underlies the present treatment of sovereign debt contracts."[19] The repayment norm and its legal expression of Pacta Sunt Servanda is the embodiment of the explanatory nationalist story on the level of principle, because by emphasising the normative weight of contracts to the detriment of everything else, it assumes that states accrue debt in a position of freedom and equality. Failing

16. Palley, 2003, Soederberg, 2005.

17. Lienau, 2014, p. 1.

18. Howse defines Pacta Sunt Servanda (2007). Howse's is among the first and most important contributions of contemporary international law that examines and questions Pacta Sunt Servanda, through the exploration of actual cases in which the odious debt doctrine has been invoked by successor regimes as a ground for limiting its obligations to repay debt incurred by previous regimes.

19. Barry and Tomitova, 2006, p. 53.

to live up to this contractual obligation thus becomes a sign of irresponsibility on the part of the sovereign.

Second, on the level of institutional design, "the international financial system lacks clear and systematic procedures for restructuring sovereign debt and handling sovereign default."[20] The absence of a facility to restructure sovereign debt has been referred to as 'the gaping hole' of the international financial system.[21] It exemplifies the explanatory nationalist story on an institutional level, because it places all the burdens arising from restructuring on the sovereign debtor.

In this section, I argue that a first step to answer the question of when a binding debt contract ought to be overridden in the world as we know it is to complement this explanatory nationalist story with an alternative explanation that considers the global order in which a country is embedded in. For simplicity's sake, I call this alternative explanation 'global explanation'. This first step is important precisely because of the reason identified by Pogge, namely that explanations bring into focus different kinds of evidence that is normatively significant and informs our answer to the question of when a bdinign-debt contract ought to be overridden.

Concretely, in this section I argue that a country's debt history needs to be explained with reference to the sovereign debt regime. The sovereign debt regime, in turn, is embedded in a highly-financialised economy which shapes the regime. To

20. Wollner, 2017, p. 1 The absence of a facility to restructure sovereign debt has been referred to as 'the gaping hole' of the international financial system, and the Group of 77 and China are currently fighting to see such a facility established. The first step towards such an establishment was taken in September 2015, when the United Nations General Assembly adopted basic principles on sovereign debt restructuring. To date, however, nothing has followed from this declaration. The absence of a sovereign debt restructuring facility exemplifies the explanatory nationalist story on an institutional level, because it places all the burdens arising from restructuring on the sovereign debtor.

21. Krueger, 2001, 2002.

offer an alternative to the standard explanatory nationalist story that is normally told about a country's sovereign debt history thus requires paying attention to both the sovereign debt regime and the way the latter is shaped by financialization.

I do so by looking at the developments in the global economy since the abolition of the Bretton Woods regime, at how this impacted the sovereign debt regime and at how this, in turn, impacted individual country trajectories. Where one situates the starting point for such a historical analysis is somewhat arbitrary, since every event has its pre-history. Yet the idea that the abolition of Bretton Woods represents some form of a critical juncture that marked the end of one era and the beginning of another has become common place and thus, I chose to lay my historical starting point here.

In 1944, toward the end of World War II, representatives of the allied nations came together in Bretton Woods, New Hampshire, with the aim of contributing to a more peaceful future by sketching out a new international financial and monetary order that was to be implemented after the war's conclusion. In a diplomatic tour de force, an agreement was reached to institute a fixed, but adjustable exchange rate system.[22] In addition to effectively fixing the dollar as the world's reserve currency, the Bretton Woods regime offered widespread provision of deposit insurance to stop bank runs by strict regulations of the financial system, such as the separation between commercial from investment banking, and by strict capital controls. These restrictions kept the financial system under tight regulatory control, making the Bretton Woods era a period of remarkable financial stability.[23]

With the outbreak of the Vietnam War and the rise of the United States' fiscal and current account deficits, it became ever more difficult to sustain a fixed yet adjustable exchange

22. Conway, 2017.
23. Ruggie, 1982.

rate regime that relied on confidence in the dollar. As U.S. creditors started fearing that there was not enough gold to back the dollars in circulation, Nixon took the unilateral decision in August of 1971 to unpeg the dollar from gold, thereby single-handedly abolishing the international monetary and financial system that had been in place since the end of WWII.[24] This marked the beginning of the period of 'financialisation' in which the tight fiscal control and stability of the Bretton Woods era was replaced by an international financial and monetary environment in which the financial sector could blossom, both at the domestic and international levels.[25]

To understand the impact that Nixon's freeing of the exchange rate had, it is useful to look at Mundell and Fleming's Impossible Trilemma and the solution that had been agreed upon during the Bretton Woods era. According to Mundell and Fleming, governments typically find three things desirable, namely: a stable exchange rate, free capital mobility, and the ability to set monetary policy to achieve domestic objectives. A stable exchange rate is thought to be valuable because it contributes to an increase in national and world income growth. On the national level, this is because a stable exchange rate contributes to greater price stability, and on the international level, it allows for a greater expansion of trade and investment, both of which are said to contribute to income growth.[26] Free capital mobility is seen by many

24. "It was not just that Nixon deliberately abolished the Bretton Woods fixed exchange rate system – though often referred to euphemistically as the 'collapse' of the system, it was actually more like a deliberate act of sabotage" (Strange, 1998, p. 40-41).

25. Although the meaning of the concept of 'financialisation' is disputed, I chose to adopt a fairly minimal definition, defining it "as a tendency for profit making to occur increasingly through financial rather than through trade and commodity production" (Krippner, 2011). See also Lapavitsas (2013), Orhangazi (2008) and Epstein (2005).

26. Reddy, 2007, p. 87.

economists as beneficial, since it facilitates efficient capital allocation across the globe, as resources flow from countries that have savings in excess of investment needs to those with investment needs unmatched by domestic savings.[27] Finally, setting monetary policy independently is valuable as domestic objectives, such as full employment, can be pursued.

The hypothesis of Mundell and Fleming, which gives the model its name, is that governments cannot have all three of these allegedly desirable things simultaneously for an extended period of time. The Bretton Woods solution to the impossible trilemma was therefore to have fixed but adjustable exchange rates and autonomous monetary policy, with the 'price' of putting in place capital controls.[28] In contrast, the solution to the impossible trilemma that emerged in the Post-Bretton Woods era is one in which independent monetary policy is sacrificed. Advanced economies adopted floating exchange rates and free capital mobility, with the price of targeting their monetary policy in a way that protects the stability of their economy's external links (especially the exchange rate) rather than meeting domestic objectives. Late developer countries started progressively moving in that direction, as well. While they initially adopted capital controls to have a fixed exchange rate (pegging their currency to the U.S. dollar) and benefiting from an independent monetary policy, they progressively dismantled capital controls, at the expense of autonomous monetary policy, as a response to IMF pressure.

The dismantling of capital controls at the international level and the adoption of floating exchange rates made domestic credit controls appear unnecessary. In the United States – considered the pioneer in banking innovation – the

27. Turner, 2016, p. 124.
28. Conway, 2017.

Glass-Steagall Act of 1933 was abolished.[29] With its abolition, banks became free to combine commercial banking (which took deposits and made loans) with investment banking (which underwrote, bought, and sold securities).[30] Although the United States took the lead in deregulating the banking system, and despite meaningful national and institutional differences among OECD countries, the trend towards progressive deregulation of the banking sector became a common feature among advanced economies.[31]

The push for financial deregulation resulted in an increase in intra-financial activities, as well as in a surge of financial innovations. Whereas in the 1960s, the typical bank's balance sheet was made up of loans to households or businesses, with the exception of government bonds and cash, today more than half of the balance sheets of the biggest banks worldwide are made up of loans or deposits between them and other financial institutions. While the growth of intra-financial activities since the 1970s was spread out across many different types of assets, one of the most important ones was the increase in credit securities. Credit securities allow banks to pool loans and sell them to other financial institutions, thereby eliminating them from the bank balance sheet.[32]

29. Strange, 1998, p. 40-41.

30. The Act suffered a death by a thousand cuts from the late 1980s onwards, and – after intense lobbying by commercial and investment banks – its remnants were abolished by Congress in 1999 via the Financial Services Modernization Act (Suarez and Kolodny, 2011).

31. While some authors argue that the deregulation of the banking and financial sector was "made in America" (Strange, 1998, p. 41), others emphasise that the deregulation of the financial system was a 'shared sickness' (Roubini and Mihm, 2011, p. 125-127) among advanced economies. For an analysis on the national institutional differences among advanced economies, see the literature on varieties of capitalism. A good introduction can be found in "An Introduction to Varieties of Capitalism" in Peter A. Hall et al. (eds), Varieties of Capitalism. The Institutional Foundations of Comparative Advantage' (2001).

32. Turner, 2016, p. 24-25.

Not only did the emergence of credit securities allow the spread of risk, but it also contributed to the growth of many non-bank financial institutions. These non-bank financial institutions constitute what we today refer to as a 'shadow banking system,' since they replicate the maturity transformations of banks, but they do so outside the regulatory system that governs traditional banks. These shadow banks took over many of the traditional roles of banks, and where banks remained involved, they did so only as one more link in a multi-step lending chain.[33] Non-financial firms also became increasingly dependent on financial revenues for a supplement, or substitute, of the profit made in their traditional productive activities.[34] The automobile producer Ford Motor Company, for instance, has in recent years made the vast majority of its revenues from selling loans to purchase cars rather than through the sale of the cars themselves.[35]

To sum, the changes in the international monetary and financial system that took place since 1971, as well as the changes in the domestic economies that the abolition of the Bretton Woods System propelled, resulted in a process of 'financialisation', both on the domestic and on the international levels, in which the financial sector expanded vis-à-vis the real economy.

Crucially, for our purposes, this process of financialisation of the economy impacted and altered the sovereign debt regime. Once freed from the constraints of the Bretton Woods fixed-exchange rate regime, and in the context of the slowdown of post-war economic growth, advanced economies started making use of the printing press to stimulate their economy.[36]

33. Turner, 2016, p. 9. The United States was, once more, "the epicentre of these developments. (…) But the impact of these changes was global" (Turner, 2016, p. 96).

34. Krippner, 2011, p. 3.

35. Froud et al. in Krippner, 2011, p. 4.

36. Streeck, 2013, p. 13.

Even before the 1973 oil crises, this use of monetary policy resulted in inflation in OECD countries. Stagflation – the combination of high inflation and recession – followed, with the two oil shocks in 1973 and 1979. Stagflation, diminished the demand for credit in OECD countries.

Stacked with petro-dollars they found difficult to invest in OECD countries, Western banks with excessive liquidity started lending to late-developing countries.[37] Developing states welcomed this increased willingness by Western banks to extend loans since, in contrast to multilateral public loans, these private debt contracts were unconditional and were not linked to political or technical conditions.[38] The need for fresh private loans, moreover, grew steadily throughout the decade: while the maturities were long in the early 1970s, they shortened throughout the decade. This lay bare a temporal gap between the repayment dates of the loans and the financial return generated by the investment of these loans in late developing countries. Consequently, debtor states had to return to the market to be able to service their debt obligations, essentially paying old debts with new ones. This created a 'treadmill effect' in which accruing debt today generated greater demand for credit tomorrow.[39]

37. Cardoso and Helwege, 1992.

38. Devlin, 1989, p. 47.

39. Devlin, 1989, p. 51. Although more and more late developing countries gained access to private bank loans as the decade advanced, it is in the 1970s where we also witness a divergence between two sets of late developing countries, namely emerging economies on one hand and Least Developed Countries (LDCs) on the other. While the former gained access to private bank loans, the latter remained unattractive for foreign creditors and remained dependent on concessionary loans from public creditors (Fogarty, 2013). This marked the beginning of what can be called a two-tier developing country debt regime, in which emerging economies are associated with private sovereign debt and LDCs with public sovereign debt. Until fairly recently, this traditional distinction was upheld and the policy responses to sovereign debt crises erupting in each of the two sets of countries diverged.

As the decade progressed, the stagflation in advanced economies continued to worsen. It was not until Paul Volcker became the chairman of the Federal Reserve in August of 1979 that the easy monetary policy that had characterised the decade was reversed. To control inflation, Volcker sharply raised interest rates "to stratospheric levels."[40] As central bankers around the world emulated him, advanced economies faced a 'shock treatment': a deep recession with high levels of unemployment, which, although short-lived, was socially and politically costly. While governments, such as those of Reagan and Thatcher, "were willing to trade mass unemployment for the restoration of 'sound money' and to crush the expected social resistance at whatever cost",[41] the radical turnaround in monetary policy was accompanied by an increase in sovereign debt levels, as governments tried to cushion the impact of the monetary shock treatment on the population. By the mid 1980s, inflation was controlled and advanced economies entered into an era of low inflation, high growth, and mild recessions, an era referred to as 'the Great Moderation'.

What constituted a cure for inflation in advanced economies came at the price of a relatively short-lived recession. But for those developing countries that had extensively borrowed from Western banks in the preceding decade, this same prescription became a recipe for disaster. When Volcker increased the

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While contractual solutions were sought for public sovereign debt crises in LDCs – namely the Heavily Indebted Poor Countries Initiative (I & II) and the Multilateral Debt Relied Initiative (MDRI) – the resolution of private sovereign debt crises still lacks such a contractual approach (Fogarty, 2013; Helleiner, 2009). Since 2006, however, twelve Sub Saharan African countries made their debut in international financial markets. Eight of these twelve countries emerged from debt write-offs only a few years before under HIPC and MDRI (Mecagni et al, 2014). This challenges the traditional association of emerging markets with private sovereign debt, and of LDC (almost exclusively) with public sovereign debt (Fogarty, 2013).

40. Roubini and Mihm, 2011, p. 25.

41. Streeck, 2013, p. 34.

Federal Reserves' interest rates in the early 1980s, a debt crisis erupted, starting first with Mexico´s default in 1982, and spread like wildfire throughout Latin America in the years that followed.[42] The rise in interest rates led to a dramatic increase in Latin America´s debt, much of which carried floating interest rates. Moreover, the short-lived recession in OECD countries resulted in a reduction in exports from the debtor countries.[43] The decline in exports, in turn, created (in Argentina and Venezuela) and further aggravated (in Brazil and Mexico) trade deficits, making Latin American countries even more dependent on loans to finance the excess of imports, loans which now became much more expensive to acquire.[44] Finally, higher interest rates made it all the more attractive to save money abroad, pulling foreign investment away from Latin America and further exacerbating capital flight.[45]

Ultimately, the crisis was resolved with the introduction of the Brady Plan. The plan consisted of offering emerging economies in crisis the opportunity to exchange their outstanding bank loans into new sovereign bonds, which were partly collateralised by U.S. Treasury bonds.[46] The Brady Plan can be seen as the starting point for the modern-day era of sovereign bond trading for emerging economies or what has been referred to as the *securitisation* of the global economy.[47] The ability to issue tradable instruments created a liquid secondary market for sovereign bonds.[48] This made lending to emerging economies less risky and hence lowered the interest rates, since private creditors could sell the sovereign

42. Cardoso and Helwege, 1992; Weeks, 1989.

43. Cardoso and Helwege, 1992, p. 116-118.

44. Cardoso and Helwege, 1992, p. 116-118.

45. Griffith-Jones and Sunkel, 1985, p. 107.

46. Das, Papaioannou and Trebesch, 2012, p. 11.

47. Helleiner, 2009.

48. Das, Papaioannou and Trebesch, 2012, p. 13. Such a market last existed during the interwar period.

debt obligations on the secondary market. Consequently, this period witnessed a vast diversification in private creditors. Long-term institutional creditors were joined by shorter-term domestic creditors, including retail investors, mutual funds, and banks that sought high returns with high-yield funds and liquid instruments as reserves. Hedge funds and governments of advanced economies also started purchasing emerging economies' bonds at the end of the decade, creating a situation in which "there are now numerous holders of sovereign debt covering a very wide geographic distribution and varying in size and sophistication from retail to institutional investors."[49]

Against this backdrop, the early 1990s were a period of low interest rates and large capital inflows into emerging economies. It was not until the outbreak of the South-East Asian crisis in 1997 and the Russian crisis in 1998 that these large capital flows dried up. The contraction in capital flows and lending to emerging economies that resulted from the South-East Asian and Russian crises led to further crises in emerging economies. Brazil devalued its currency in 1999 and was followed by outright default in Ecuador, Turkey, Ukraine and Pakistan in the year 2000.[50] In 2001, Argentina defaulted on its private sovereign debt. In 2002-2003, Uruguay managed to avoid succumbing to Argentina's fate by undertaking a voluntary restructuring of its debt.[51]

49. Marx, Echague and Sandleris, 2006, p. 57.

50. Marx, Echague and Sandleris, 2006, p. 64.

51. Panizza, 2014. If one compares these crises at the turn of the millennium with the Latin American debt crisis in the 1980s, one can recognise important differences in the dynamics of crisis eruption and contagion that are important for the analysis at hand. First, whereas in the 1980s, the crisis was triggered by adverse external shocks that affected emerging economies instantaneously (most prominently, the sharp increase of interest rates in the U.S.), the crises of the late 1990s and early 2000s were a consequence of changes in creditors' perceptions about the ability and/or willingness of the debtor countries to service their debts (Marx, Echague and Sandleris, 2006, p. 65). Second, whereas the crisis in the 1980s can be

Despite the severity and sheer number of crises erupting in developing economies at the turn of the millennium, these events did not disrupt the discourse surrounding the era of 'Great Moderation' in advanced economies.[52] Notwithstanding, in the 1990s, governments in advanced economies began to worry about the rising sovereign debt levels, while creditors – not least due to their experiences in developing economies - began to have doubts about the ability of states to repay their growing debt.[53]

The governments' response was a second wave of capital market liberalisation and a continued deregulation of the financial sector. Under the Clinton administration, attempts were made to balance the budget mainly through social spending cuts. Most advanced economies emulated this strategy and the rising sovereign debt levels that characterised the previous decade were replaced by a growing private debt burden. Regulations were adopted that enabled households to supplement their income with private sector credit rather than with state benefits.[54]

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understood as a sovereign debt crisis narrowly defined, the crises in the late 1990s and early 2000s only turned into sovereign debt crises in the wake of an ongoing capital account crisis. Narrowly defined, sovereign debt crises can be understood – in line with Reinhart and Rogoff – as crises that erupt when a country is not able or willing to service its foreign or domestic debt, under the terms agreed. Now, whereas in the 1980s the Latin American crisis originated as a sovereign debt crisis – in which the very crisis was constituted by the fact that Latin American governments were unable to service their debt obligations – the crises at the turn of the millennium originated as capital account crisis. These crises, then, are sovereign debt crises broadly defined, for they did not erupt due to a government's inability to service its debts, but only resulted in sovereign debt crises as the economic conditions deteriorated. Here, I adopt this broad definition of sovereign debt crises.

52. Roubini and Mihm, 2011, p. 30.

53. Streeck, 2013, p. 36.

54. Streeck, 2013, p. 39.

While this form of 'privatised Keynesianism'[55] allowed advanced economies to adhere to the discourse of the Great Moderation and to avoid the fate of their counterparts in developing countries, the 2007-2008 subprime mortgage crisis that erupted in the United States and reverberated through the world economy put an abrupt and unquestionable end to this. The crisis also raised serious doubts about the process of deregulation and financialisation that had been going on since the early 1970s and that had been, if not actively praised and defended, least accepted as the epoch's unquestioned background tune.

What this brief historical analysis reveals is that an individual country's debt history cannot be understood in isolation from the sovereign debt regime and the process of financialisation that shaped it. In a heavily financialised economy, credit and debt flows move rapidly from different regions in the world to others. When advanced economies were battling inflation and recession in the 1970s, debt flows moved to developing countries. Once the Latin American debt crisis erupted, debt flows moved back to the advanced economies and sovereign debt levels rose there. With the introduction of the Brady Plan and the progressive shift from sovereign debt levels to private debt levels in advanced economies, debt flows returned to developing countries. Finally, since 2008, and parallel to the eruption of the debt crises at the heart of the European Union, there has been a sharp rise in the debt levels of emerging economies, especially China, "which could host the next leg of the global leverage crisis."[56]

The geographical interdependency and the contagion effects between different countries and regions in the world challenge explanations of a country's debt history that exclusively focus on explanatory nationalist aspects such as

55. Crouch, 2009.
56. Buttiglione et al, 2014, p. 3.

'fiscal responsibility' and 'good governance.' They suggest that a country's debt history cannot be solely explained with reference to these factors. To use the classroom analogy, doing so would be parallel to trying to explain a student's performance without reference to the quality of the teacher, or to try to explain poverty solely based on the policies adopted by a developing country's government. It would, in short, be an exclusively 'explanatory nationalist' analysis.[57] Such an explanation is, at best, insufficient.

IV. Human Rights and Debt Repayment

Providing a global contextualization of a country´s debt history brings into focus different kinds of evidence and considers a broader set of empirical phenomena. This is not only relevant to complement the explanatory nationalist analysis, but also to answer the question that concerns us here. For the global explanation brings evidence into the fore that allows us to identify the conditions under which a binding debt contract ought to be overridden. More specifically, based on the global explanation, we recognize that in moments of crisis, continued debt-repayment may threaten both the collective and the socio-economic rights of the debtor's state citizenry. In this section I thus do two things: first, I show how continued debt-repayment in moments of crisis may result in the undermining of the human rights of a debtor state's citizenry. Second, I argue that this undermining of collective and socio-economic human rights is a normatively weighty reason to override a binding debt contract.

As the global explanation provided in the previous section reveals, the financialization of the economy made larger amounts of credit available to a broader sets of states. With

57. Pogge, 2008.

the growth of the supply of credit, states turned to borrowing to finance its expenses. Interestingly, the turn to finance was a choice made across partisan divisions by political leaders across the political spectrum.[58] This turn to borrowing has been referred to as the transition from the 'tax state' to the 'debt state.'[59] Rather than financing its expenses through the rising of taxes, a debt state "covers a large, possibly rising, part of its expenditure through borrowing, (…) thereby accumulating a debt mountain that it has to finance with an ever greater share of its revenue."[60]

With the changes witnessed at the international level since the end of the Bretton Woods era, domestic upper classes with capital to invest had the chance of going global, investing not only in their own state, but also in others. The abolition of capital controls and the domestic regulatory changes that followed allowed the upper class to seamlessly move their capital across territorial borders. What the gradual financialisation and liberalisation of the global economy permitted, then, was a progressive detachment of the new international creditor class from their domestic economies-cum-societies. It allowed a 'going global' of the domestic upper class, which seizes the opportunities for profit that the financialisation of the global economy offers, to secure the maximum return on their capital.[61]

With the securitisation of the economy, ever more members of this financial class became the state's creditors. Recall that during the bankerisation of the global economy, the main private lenders to states were banks, which operated as intermediaries between debtors and creditors. After the securitisation of the economy, banks stopped operating as

58. Hopkin and Lynch (2016) show, for instance, how financialisation in Britain was not only the outcome of policies adopted under the Thatcher government, but continued under New Labour.

59. Streeck, 2013.

60. Streeck, 2013, p. 72.

61. Duménil and Lévy, 2011, p. 8.

intermediaries, and became creditors in their own right. Moreover, the transition from loans to bonds also lead to a great diversification of creditors, ranging from individual pensioners to hedge funds.[62]

Once the financial class becomes the state's creditors, the debt state has two constituencies whose interests it must consider: the state's citizenry, whose claims on public policy are predicated on their membership in the state as a political community and the state's creditors – the 'second constituency'[63]– whose claims are predicated on commercial contract and whose interests can come into conflict with the first constituency qua citizens. The rise of this second constituency challenges the first constituency. The dilemma that the debt state faces, then, is trying to satisfy these two different constituencies, both of which operate on the basis of incompatible logics.

In moments of crisis, this conflict between the two constituencies is often resolved in the interest of the former. First, the debtor state itself tends to prioritise repayment to its second constituency, the domestic and international creditors. This is so in cases of both sovereign debt crises and in cases in which the crisis erupts in the private sector, in which financial institutions are saved with public funds. The attempts to solve Europe's debt crisis and the resolution of the 2008 crisis that originated in the subprime mortgage sector are emblematic examples in which the interests of the creditors were prioritised over those of the country's citizens. Streeck refers to this prioritisation of the second constituency as the transition from the 'debt state' to the 'consolidation state,' the main objective of which is to reassure creditors that they will be repaid.[64]

62. Helleiner, 2009, p. 95.
63. Streeck, 2013
64. Streeck, 2013, p. 154.

The impact of devoting a big portion of domestic resources to debt repayment over other concerns dispropor-tionally affects those citizens who are already worse off. Austerity, loosely defined as the cutting of public expenses, is a class-specific policy, in the sense that its effects are felt differently across the income distribution: those at the bottom of the distribution lose more than those at the top.[65] There are several reasons for this. First, austerity policies result in an increase in unemployment rates. While labour income is the major source of income for the middle and lowest income percentiles the higher income population has alternative or additional sources to finance their living standards.[66] Thus, an increase of unemployment rates disproportionately affects those who are already relatively worse off. This effect is exacerbated because austerity also entails a cut in public services, services on which the lower income brackets rely more than the higher income brackets. These policies also affect a deteriorating middle class. [67] Furthermore, austerity does not only affect those who currently find themselves towards the bottom of the income distribution, but also future generations. It is future generations that will no longer have the possibilities that the welfare state provided to enhance intra-generational social mobility.[68]

65. Blyth, 2015, p. 8.
66. D'Errico et al., 2015.
67. Balourdos, 2014.
68. Blyth, 2015. The fight against inflation, another policy often adopted by what Streeck calls the consolidation state, also affects the worst off more than it affects the better off: "When 'too much money' chases 'too few goods' – an inflation – it benefits debtors over creditors since the greater the inflation, the less real income is needed to pay back the debt accrued. (…) The politics of cutting inflation therefore takes on the form of restoring the 'real' value of money by pushing inflation rate down through 'independent' (from the rest of us) independent central banks. Creditors win, debtors lose. One can argue about the balance of benefits, but it's still a class-specific tax (Blyth, 2015, p. 9).

Not only the 'consolidation state', but also the sovereign debt regime functions in a way that, in moments of crisis, prioritises the repayment of private creditors and the interests of the financial class. As we saw in the proceeding section, the sovereign debt regime lacks any form of sovereign debt restructuring facility, which results in the bailing out of private creditors in moments of crisis.

This burdening of the state's citizenry – and those already worse off therein –, both in the debtor state (through austerity measures) and in those countries, that subsidise the bailout of private creditors, has become ever more apparent in the last 40 years. During the 1980s debt crisis, there was at least a legitimate concern that the default to private creditors (in this case, mostly banks) signified a systemic risk to the financial system as a whole. Conversely, by 1994, the Mexican government was defaulting on thousands of individual bond-holders in northern Mexico. Here, "bailouts now appeared simply to reward investors for their poor investment choices at the taxpayers' expense."[69] When the 1997-1998 crisis struck the East Asian region, large international bailouts were once again offered to repay private creditors and stem the crisis, which provoked some opposition from many European countries, and especially the United States. Paul O'Neill, the treasury secretary under the Bush administration, was particularly critical that international investors gained from bailouts at taxpayers' expense, stating that "as we in the finance ministries of the world talk glibly about billions of dollars of support for policies gone wrong, we need to remember that the money we are entrusted with came from plumbers and carpenters who sent 25 percent of their $50,000 annual income to us for wise use."[70]

As O'Neill's complaint makes apparent, the critique of

69. Helleiner, 2009, p. 96.
70. Helleiner, 2009, p. 99.

international bailouts stretches beyond partisan divisions. On one side of the political spectrum, free-market advocates oppose them due to the market distortions they cause. Similarly, they are concerned with moral hazard: the fear that if global investors know that they will be bailed out, they will have the incentive to make increasingly risky loans.[71] On the other side of the political spectrum, the critique is presented as one of fairness, for bailouts seldom help the nation regain its economic footing, and essentially send taxpayer money outside of the economy to repay creditors.[72]

The crucial insight that this analysis reveals, then, is that in order to defend the repayment norm – in order to insist, that is, that sovereign debts must always be serviced by the citizenry of the debtor state – it is not enough to simply point at the sanctity of contracts. Rather, the contractual claim that the creditors hold must be seen in relation to, and weighted against the claim that citizens have, in virtue of being part of the state as a political community. The conflict of interests between the first and the second constituency of the state highlights the importance of not seeing the contractual claim of creditors in a vacuum, but in considering the weight of such claims in today's real political landscape, namely one in which the interests of the citizenry may be opposed to those of an international financial elite.

This is partly a matter of distribution. It concerns the question of how much of the state's budget is devoted to honour contractual obligations with its creditors, and how much is devoted to meet the legitimate claims of its citizenry. The more indebted the state is, the larger will the portion of the budget be that will have to be devoted to repaying its creditors, and the more difficult it may become for the state to meet the legitimate claims of its citizenry. At its most extreme,

71. Gallagher, 2011, p. 8.
72. Gallagher, 2011.

the servicing of debt might come at the expense of meeting the socio-economic human rights of the state´s citizenry. But the concern with high indebtedness also goes beyond matters of distribution, and speaks to the states responsiveness to the interests of its citizenry. The problem here seems to be that the highly-indebted state may lose its ability to act in the name of the citizenry it allegedly represents; the dependence on its 'second constituency' thus threatening the state's very raison d'être and undermining the citizens collective right to political self-determination.

What I wish to suggest here is the following: Whenever the repayment of debt threatens the human rights of the citizenry, this provides a weighty normative reason to prioritize the fulfilment of the latter over the former. This applies to all human rights, for as the Human Rights Charter emphasizes, human rights are universal, inalienable, indivisible, interdependent and interrelated. As we saw, however, there are specific reasons to fear that a high indebtedness of states may result in the undermining of the socio-economic and the collective human rights of a state's citizenry in particular. More specifically formulated, then, what I am proposing here is that whenever debt repayment undermines the socio-economic and collective human rights of the state´s citizenry, states have a normatively weighty reason to prioritize the fulfilment of the citizen's human rights over meeting their contractual debt payment obligations vis-à-vis their second constituency.

Let me clarify what is and what is not entailed by this argument. First, I do not mean to imply that the violation of human rights by the state in general provides a reason to question the bindingness of debt. This is a thesis that odious debt scholars may defend. The argument would be that if a state systematically violates the human rights of its citizens, it is not the type of agent who can accrue debt in their name legitimately. Hence, the systematic violation of human rights by the state would entail that the debt accrued by it is non-binding. Of course, all states violate some human rights at some point in time. Scholars defending this type of argument would thus face the tricky question of how to define the exact threshold: When exactly has the state violated so many human rights as to lose its authority to accrue binding debt in its citizen's name? This is not the argument I am making, however. My suggestions is different. I am interested in a particular instance in which human rights are violated, namely cases in which the continued servicing of binding debt contracts results in the undermining of the socio-economic and the collective human rights of a state's citizenry. In these cases – cases which can be foreseen by the state who is about to decide how to invest its finite state resources – the undermining of the socio-economic and collective human rights of the state´s citizenry is a normatively weighty reason to prioritize the fulfilment of the citizen's human rights over meeting their contractual debt payment obligations vis-à-vis their second constituency.

Second, as I have already clarified above, stating that states have weighty normative reasons to prioritize the fulfilment of human rights over debt servicing does not entail that the debt contract is no longer binding, or that all debt should be forgiven. There are both normative and practical differences between these two statements: Normatively, the difference resides in the fact that claiming that a binding debt contract ought to be overridden does recognize the legitimacy of the initial debt contract, whereas simply stating that the contract is non-binding does not. Practically, the difference is as stark as one between declaring a debt jubilee and restructuring the debt. Whereas nothing in my argument suggests that the former could be normatively justified, the latter might be. My argument does entail that in cases in which debt repayment undermines the human rights of the state's citizenry, the state has weighty normative reasons to enforce a non-voluntary debt restructuring, which entails that creditors are forced to exchange old debt obligations for new ones.

Third, the formulation I chose indicates that this is not an all-things-considered argument. When stating that the state has ‘weighty normative reasons’ to prioritize the fulfilment of its citizen’s human rights over meeting its contractual obligations I am thus not suggesting that this will always be justified. The dilemma between the interests of the first over the second constituency may dissolve, for instance, if we adopt a time window that is long enough. In such a case, prioritizing meeting the fulfilment of the citizen´s human rights today, at the expense of meeting its contractual obligations may actually come at the expense of fulfilling the human rights of its citizenry in the future. In this case, the prioritization becomes less obvious. Austerity policies are an excellent example of this. Austerity policies are not only adopted to meet the conditions of the multilateral creditors and make more resources available to service private sovereign debt, but also because of the held belief that reducing the deficit via the cutting of expenses is necessary to boost growth in the long term. Similarly, the prioritization of creditor repayment in moments of crisis could be interpreted as an attempt to maintain creditworthiness and ensure future access to credit, something which may well be in the interest of the citizenry’s medium term human rights. Since providing an all-things considered argument goes beyond the scope of this paper, here I defend a more limited claim, namely that fulfilling the human rights of its citizenry is a weighty normative concern that may trump contractual obligations, given the particular circumstances.[73]

73. Defending the fulfilment of the collective and socio-economic human rights of the state’s citizenry as a normatively weighty reason to override a binding debt contract as I do here also poses an important challenge to the question of an appropriate design of the global institutional order that is to regulate sovereign debt and credit. Elsewhere I explore how the argument defended here affects the question of the appropriate institutional design, arguing that the state’s capacity to act with its citizen’s interests in mind

Finally, nothing of what I said entails that I take sovereign debt as such to be normatively undesirable. Here my position differs from that of early to mid-modern thinkers such as Hume or Sieyès. Sieyès was hostile to the entire idea of sovereign debt and favoured a stronger system of taxation to finance public expenditure.[74] He considered the rejection of public credit fundamental to a truly responsive constitutional government. Hume, in turn, famously stated that 'either the nation must destroy public credit, or public credit will destroy the nation'.[75] The concern that Sieyès and Hume shared was that sovereign debt 'could make government officials over-attentive to the needs and desires of creditors (…). This dependence would render the state less responsive to true public need and neglectful of the greater national interest'[76].

The argument I wish to make here comes apart from that of Hume and Sieyès in that I do not wish to suggest that the acquisition of sovereign debt is problematic as such. From a normative perspective, borrowing might be justified in terms of distributive justice, the same way discounting is – if the future will be richer than the present, debt is a way of transferring money from the rich to the poor. From an economic perspective, debt contracts can be justified since they mobilize credit. In contrast to equity contracts in which the returns of the investor depend on the success of the enterprise being invested in, debt contracts promise a fixed return. Without this promise, not enough capital would be available.[77] It is difficult, for instance, to imagine the development of the British railway system, as well as the industrial development that was fuelled

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should be turned into an ex-ante consideration that creditors ought to consider (*Journal of Political Philosophy, forthcoming*).

74. Sieyès (2003).

75. Hume in Hont (2005, p. 325).

76. Lienau (2014, p. 47).

77. Turner (2016, p. 6).

by it, without debt contracts.[78] Similarly, developing states can be said to accrue debt today, to make the large investments needed to change the structure of their economy, climb up the value chain of production and service provision, and generate greater economic growth.

In sum, I neither wish to suggest that sovereign debt as such is normatively indefensible, nor that prioritizing the fulfilment of its citizen's human rights will always and at all times be the state's right course of action. What I wish to suggest instead is the following: Whenever the repayment of debt threatens the human rights of the citizenry, this provides a weighty normative reason to prioritize the fulfilment of the latter over the former.

V. Conclusion

In this paper I sought to analyse the circumstances under which weighty normative reasons exist to override a legitimate and binding debt contract. Without any claim to exhaustiveness, I argued that one such set of circumstances is when the human rights of the state's citizenry are undermined by continued debt servicing. This is particularly relevant in the context of the contemporary sovereign debt regime, since this regime is one in which the interests of the first may be juxtaposed to those of the second. Put differently, though contracts carry normative force, so does the fulfilment of the socio-economic and collective human rights of a state's citizenry. Whenever the latter are undermined, this gives us reasons to question whether the priority really ought to be meeting the state's contractual obligation. Providing a historical overview of the changes witnessed in the global economy since the early 1970's allowed me to highlight that it

78. Turner (2016, p. 35).

is not coincidental that the fulfilment of the citizens human rights may – at times – enter into conflict with those of the state's creditors. In doing so, I hope not only to have shown the importance of complementing explanatory nationalist theories with alternative, global explanations, but also to have made a case for a form of political theorizing that takes the empirics of the object of inquiry very seriously.

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