

Debt Swaps Basic Theory...

- Not new mechanism/not easy mechanism
- Very widely implemented (public and private sector)
- Requires multidisciplinary approach, including diplomacy

Arguments against Debt Swaps

- Put national sovereignty at risk !
- Creates inflation !
- Legitimizes “illegitimate” debt !
- Negatively affect the balance of payments !
- Does not solve the debt problem !

Arguments in favour of Debt Swaps

- Good way to get rid of “bad” debts
- Creates resources for conservation
- Creates a favourable “cooperation” climate
- Does not have the negative side effects of “debt forgiveness”

Basic starting point

- All debts are not good for swapping operations
- Every swap is an *Ad Hoc* operation
- Good will/political will is a prerequisite
- Must be a win/win situation

Swap potential Analysis

	Low Inflation	High Inflation
Debt that would be serviced	I Very desirable	II Desirable but monetary impact needs to be regulated for large operations
Debt that would not be serviced	III Desirable only if spending priority changes are essential to justify program due to efficiency gain	IV Only desirable if conditions in both II and III are met

The mechanics of debt swaps

Figure 2. Generic commercial debt swap with third party assistance

