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Third-World Debt

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June, 1988

Dear Alumni and Friends,

This issue contains a special section on Third World Debt, which is based on a conference held here in January under the co-sponsorship of the Business School and Touche Ross & Co. Panelists included representatives from the World Bank, the money center banks, regional banks, and the London Merchant Bank as well as professors from Harvard and Michigan, and a representative from Touche Ross & Co. Panelists did not agree on what should be done, and the resulting discussion brought the complexities of the Third World debt crisis home to all of us. These kinds of forums help keep both theory and practice lively at the School and enrich all of our understandings of complex issues facing business and the economy today.

Our doctoral program in marketing received a special boost this spring with the establishment by Milton Kendrick and his wife Josephine of the Kendrick Award in marketing, which is meant to enhance theory development in marketing by giving support to doctoral candidates who have shown special promise in research. More about this award is on page 28.

As *Dividend* goes to press, we have just received news of two new scholarships designated for minority students at the Business School, one donated by Ford Motor Company and the other by Arthur Andersen & Co. They join another new minority scholarship which has been given by P & G. For more on this scholarship and its first winner, see page 24.

Another exciting development is the establishment of the Business School Growth Fund. Some of our alumni who wanted to contribute money to the School felt that if they managed the fonds they could do a better job and take a more aggressive stance. This new fund will be managed by five of our alumni investment managers, and will seek long-term growth through a diversified portfolio. You can read more about this on page 29. The Stanford Business School Trust, which we used as a model, has been fairly aggressive and has grown from $70,000 to $9 million in 20 years.

Sincerely,

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Gilbert R. Whitaker, Jr.

Dividend

Volume 19, No. 3 *June, 1988*

Third World Debt: A Forum
Strategies for dealing with the Third World debt crisis were discussed at the Business School in January, at a Forum held under the joint sponsorship of the School and Touche Ross & Co. Here are edited versions of what the panelists said.

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Our cover photograph was taken by Larime Photographic Studios.

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Third World Debt: A Forum

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he health of the U.S. financial system, as well as the international economy, is seriously affected by the Third World debt crisis.

A forum on strategies for dealing with the crisis was held at the Business School in January, under the joint sponsorship of the Business School and Touche Ross & Co.

Panelists examined the magnitude of the problem as well as U.S. and international economic policy implications and strategies for coping with its repercussions.

Panelists brought a wide diversity of viewpoints to bear. They included representatives of a money center bank, a British bank, the World Bank, an American regional bank, the accounting profession, and academia. Panelists did not agree on what solutions would work, and their differences helped to point up the complexities of the Third World debt crisis.

On the following pages, we bring you edited remarks of the seven panel members. We hope that reading their comments and suggested solutions will give you an enhanced understanding of the complex and difficult problem of international debt.

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Structural Crisis - Charts **in the** Way We Look at International Debt

By Geoffrey Bell
Chairman, Guinness Mahon Bank

Almost every day, when you open the newspapers, you may notice that another bank has increased its provisions against Third World Debt. This very week the Brazilian negotiations have begun, and are going to be absolutely critical. Brazil has already missed an interest payment this year. A question exists as to whether or not the U.S. regulators will have to decide to classify Brazilian debt as value impaired, which will open yet another phase in the problem of international debt. And, of course, just before Christmas, Morgan Guaranty introduced with the U.S. Treasury a scheme for dealing with Mexican debt.

These relatively new developments change the very concept of how we look at the problem of international debt, and the panel we've assembled this morning obviously reflects the different aspects of this spectrum. In my role as moderator today, I have one claim to fame. I have had the opportunity to act on both sides of the fence as a consultant regarding the problem of international debt.

In the early days of the 1970s, when money was pouring into the region at a rapid rate, I was appointed adviser to the Central Bank of Venezuela, after the oil shock when their reserves were rising at about a billion dollars a month.

"Does the old system of lending new money to pay interest on old debt make sense?"

The problem in those days was how to invest this great largesse, how to find ways of placing this money.

Well, it didn't last too long, and when that affluence had all disappeared and they were rescheduling their debts, I was asked to work on the other side of the equation. So it shows that investment bankers have to be extremely flexible about which side of the balance sheet they're addressing. Also, I have another claim. As chairman of a bank which has some debt exposure, and I can appreciate both points of view.

The important change in the status quo has been that the old collective spirit of dealing with the problem of international debt is beginning to break down. In addition, debtors now demand different treatment. For a number of years they have been paying interest, and borrowing some new money. But, once the banks began to trade their debt in the secondary market at a discount, a number of debtors have begun to say (not surprisingly) that they must also benefit from the fact that debt is trading at 50 or 40 cents on the dollar in the secondary market.

I would like now to take a few minutes to go back to the history of how this all happened and why we are here today.

The 1970s were indeed halcyon days. The Euro-markets were expanding at a truly spectacular rate. Money was easy and bankers decided to court an area they had not lended to previously, namely South America. So lending went from about $70 billion, if I remember correctly, in the early 1970s, quickly up to $300 billion in a matter of a relatively few years. It was indeed a wonderful period for bankers.

Now it's all very nice to lend money in Birmingham, England or Cleveland, Ohio, but let me assure you how much more fun you can have by going to Caracas, Rio, and Buenos Aires. So bankers had the double advantage of going to interesting places and also persuading their lords and masters that they were doing the right thing. Moreover, when this coincided with the oil shock and the whole argument of recycling, you felt you were not only doing good work for your bank, but also that you were contributing to humanity by transferring money

from the oil producers down to South America. What most of us forgot at that time though, was that there were bank balance sheets in between. This meant that the oil producers had enough sense to place deposits with the banks and the banks had already lent against their own resources. However, it was all a wonderful period of time. Lending large sums of money, making money, and at the same time doing good for the developing world.

Eventually like most parties, it came to an end, just like another party coming to an end in banking today. After the demise of lending to developing countries, bankers discovered the joys of capital markets, and for the last five years, enormous expansion has taken place in that area. London has benefited; Wall Street has benefited.

I can tell you however, I've seen the absolute litmus test that this particular party is over. The flagship of the expansion in the Euro-market was the magazine, *Euro-Money* that many of us have written for over the years. I remember at the IMF meeting this year seeing the collection of books that actually constituted that month's *Euro-Money* publication. It had become so successful with the advertising from banks that the October issue had become so big that no one could actually pick it up and take it home to look at the advertisements. I learned this week that *Euro-Money* has now reduced its staff by 50 people, because the advertising revenue has suddenly dried up. If I've ever seen an example of change in economic environment, this is it. And I can assure you that the capital market boom is gone the same way as the South American lending boom five years before it.

Now the first reaction to the ending of the boom — the liquidity crisis or the crisis of Mexico in 1982 — quickly led to a contagion around South America. Every other country quickly became affected as banks withdrew their credits, and each country was then forced to do something about its debt. The initial reaction (and the appropriate reaction at that time in official and banking circles), saw the situation as a liquidity crisis. This required a period of adjustment by the borrowers. They had to take in their belts, and undertake austerity programs, often with the help of the International Monetary Fund. However, it was felt that with some economic adjustment and with some new money from the banks, they could go back to the voluntary markets and borrow again, even if not on the scale that had been the case in the late 1970s. That view was indeed the fundamental assumption of the early years of the debt crisis. Mr. Rhodes and his colleagues managed with great skill to reschedule the debts of virtually every country in South America, and gave them a breathing space so they did not have to continue their amortization payments. Also in some cases they even achieved a reduction in interest. Both the IMF and the World Bank played very important roles here.

"Above all, what seems to be occurring is a greater and greater reluctance on the part of the collective of international banks to provide new money to debtors____If new money is not available for debtors, that raises the question of whether they can service their debt in full, and if they can't, clearly something has to give."

But what has become clear over the last five years, is that we no longer have merely a liquidity crisis. It is something much deeper. You might view it as a structural crisis — some would even say, a solvency crisis. And, therefore, we have seen more and more questioning as to whether or not the old approach of rescheduling, lending some new money and adjustment, is indeed the right approach in today's conditions. Or in brief, does the old system of lending some new money to pay interest on old debt make sense?

In this area the developments of 1987 have changed the scope of the situation. Mr. Reed, the chairman of Citibank, stunned the American banking world last summer when he took a three billion dollar provision against his South American and debt exposure to developing countries. A wave of provisioning then followed around the world, as banks in my country and your country and others also began to take provisions. Although, I think it is fair to note, many of the European banks had already gone this path and in fact many of the German and Swiss banks had increased their provisions to 70 or even 80 percent by last summer. But again, they have tax advantages which do not exist in other countries. Then, just before Christmas the Bank of Boston decided not just to make provision, but actually to write-off some of its international Latinate exposure. Finally, at the end of the year, Morgan Guaranty announced its plan for dealing with Mexican debt. The plan provides that Mexico will swap its old debt for new debt at a discount and that new debt will be given additional security by being backed by zero coupon U.S. Treasury bonds.

This new approach gives Mexico a tangible incentive. It will be one of the first countries on a voluntary basis to take advantage of a reduction in interest payments. The Morgan Guaranty proposal certainly goes in the direction that debtors have been wanting for some time. Namely, to recognize that if the banks choose to trade their debt in the secondary market at a discount, then some of that benefit should accrue to the debtor.

It also displays a growing recognition among banks that they have different interests, with the larger banks on one side and the smaller regional banks on the other.

That explains why some regional banks regard the Morgan Guaranty scheme as a way of exiting — what the jargon describes as an Enhanced Exit Bond.

Above all, what seems to be occurring is a greater and greater reluctance on the part of the collective of international banks to provide new money to debtors. Mr. Rhodes and his colleagues have done an outstanding job, along with help from central banks and the IMF, in persuading banks to come up with new money to help debtors service their debts. But it would appear that a great reluctance exists on the part of the international banking community to follow suit. If new money is not available for debtors, that raises the question of whether they can service their debt in full, and if they can't, clearly something has to give.

Finally, it's worth noting that international debt is not only about the problems facing banks. It also concerns itself with the problems facing countries affected by debt. Most of these countries have made great adjustment strides. Many of them have cut their imports in half in a very short period of time! The level of their standard of living has also been reduced. Most of them have been in recession for a number of years. So they, quite understandably, suffer from debt fatigue, the same as banks equally suffer from debt fatigue.

Of course, it's very important for the world economy to have developing countries grow again. One only has to note that, prior to the debt crisis, South America accounted for 40 percent of U.S. exports! That market has more or less disappeared with the debt crisis and hence the reduction in the standard of living.

To sum up, with all the things currently taking place on the banking front as well as with the debtors as they look for some way of reducing the debt burden in order to grow, there is no question whatsoever that we are moving into a different phase with regard to international debt.

Virginia Geren

About the Author: Geoffrey Bell is chairman of Guinness Mahon Bank, the London Merchant Bank, and president of Geoffrey Bell and Company, Inc., which advises governments and central banks in the U.S., Canada, Europe, South America, and Australia on investing international reserves as well as developing and implementing international borrowing programs. He is also executive secretary and a member of the board of the Consultative Group on International Economic and Monetary Affairs (the Group of 30); director of Lewis and Peat Holdings Limited (an international commodity company); and consulting editor of International Reports, a publication of the *Financial Times.* His book, *The Euro-Dollar Market and the International Financial System,* has been translated into Japanese, French, and Italian.

Current Overview of the

This morning I'd like to give you an overview on how we view the LDC problem and where specific countries are today in the process.

Since 1982 when the LDC problem really came to the fore, the major goal of the banks has been to maintain both the credit-worthiness of the countries as well as their ability to access international credit markets. There are two reasons for this. The first is pure self-interest, because banks know that in the long run we're not going to get repaid nor are our assets going to have any degree of liquidity, if the countries can't grow on a self-sustaining basis. The second reason is that if a developing country can no longer import resources from the rest of the world — in other words, use foreign savings, by definition it's not going to grow. Therefore, our goal has always been to try to maintain and/or to increase the credit-worthiness of the countries involved.

If you look at any of the numbers going forward, it's obvious that the demand that the developing countries are going to have for the savings of the developed world is well beyond the resources of the World Bank or the IMF or government largesse in the form of aid. Therefore, if countries are going to maintain their access to foreign savings, it's crucial that they maintain their access to the private markets, because that's the only source in the end that will provide the resources they need to grow.

The restructuring process has gone through several phases. The first was what we call the balance of payments phase. Between 1982 and early 1984, we were basically just concerned with financing the ongoing needs of each of the countries involved. By 1984, everybody began to realize that this process was going to take longer than they had hoped, and we entered into a phase of what we called the MYRAs, the Multi-Year Rescheduling Agreements. And, there have been MYRAs done for almost every major country in Latin America, with the one exception of Brazil.

In October of 1985, Secretary Baker made a speech in Seoul which has come to be known as the Baker Initiative. His basic challenge was that if the countries could maintain themselves on a basic direction of adjustment and were committed to that adjustment process, the banks and multilaterals and government's resources would be forthcoming. I think the goal for the banks was to produce something like 20 billion dollars for 1985 through 1988. 1 am happy to report that the banks through 1987 have produced roughly 14 billion dollars of that amount in new money agreements.

One of the other things that's happened with the Baker Initiative is that we have learned that there are many and varied interests within the banking community and within private markets in general, and so we've attempted to create options in people's ability to use the assets that they now hold.

For instance, in Argentina, there was a new money package of almost 2 billion dollars that was done within the context of an IMF program — an adjustment program where the

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By Robert MeCormack
Vice President, Restructuring Committee
Citibank, N.A.

"The debt has been divorced from the private sector sources that could repay it."

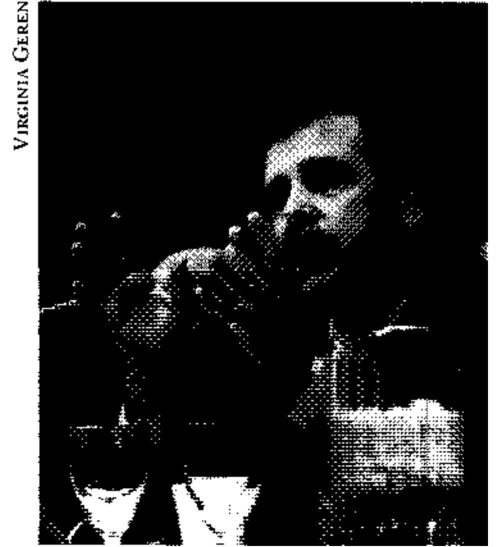
government had committed to try to manage its external and internal economy.

Within the menu of options, we have co-financing with the World Bank whereby banks will lend in concert with the World Bank on a parallel basis, basically into new projects. We created a securitization for an exit vehicle for those banks that feel they have a small exposure in Argentina and want to get out. They were offered a bond which gave them the ability to get out on a securitized basis, such that they could then sell the paper in the market place. We also have an on-lending and re-lending program whereby you can use counterpart resources — pesos in the case of Argentina — and relend them into the private sector.

One of the problems in Latin America is that the debt has been concentrated in the name of the Republics and the Central Bank. Most of the loans were not made as balance of payments finances, but were made either to projects and/or to the private sector. As the Central Banks became illiquid, the private sector and the individual parties could come up with a local currency equivalent to repay the debt, which they did to the Central Bank. The Central Bank then said, "I'm sorry, I don't have the foreign exchange available, could you refinance these liabilities to me." The effect has been that a great deal of the debt that used to be in the hands of the private sector in Latin America has now been concentrated into the Central Bank and the Republics. Unfortunately, that means that the debt has been divorced from the productive resources that could repay it. This is a problem for the banks from a regulatory point of view, but it's also a problem from a conceptual point of view. If you really want to see the private sector grow, and if you believe that the private sector is an engine for growth in these countries, then you want to see the private sector with the resources and not necessarily the Central Bank.

I guess I should mention the Morgan deal. I think the general view is that the Morgan deal could be a good exit vehicle for those who believe that they should be taking their losses at what is perceived to be the current market value. The process is now moving on. And without a doubt Brazil is going to be the watershed. There are two reasons for this: one, because it is a big number for the banks — some 500 odd billion dollars in medium term debt. The other is that Brazil isn't just a small South American country; it's the sixth largest exporter in the world, with a GNP on a par with Great Britain. Brazil has a major internal fiscal deficit in the public sector and a very strong under-leveraged private sector. It has a thriving external business. For the last 12 months, it has produced a

VIRGINIA GEREN



About the Author: Mr. MeCormack joined Citibank's Restructuring Committee in June, 1987 after more than eight years' experience dealing with soverign debt as a line officer in Central America, Jamaica, and Venezuela. His responsibilities include the representation of Citicorp on several Bank Advisory Committees, including those of Brazil, Poland, and Yugoslavia.

billion dollars a month on the trade balance. It is not a country with a tremendous external problem; it has an internal deficit financing problem. And, it is essentially financing its deficit partially by not repaying the debt.

What the banks want to see, as they've wanted to see ever since 1982, is a considered effort on the part of all of the creditors of Brazil. The moratorium in Brazil only applies to medium term debt owed to commercial banks. It doesn't apply to all the short-term trade credit and inter-bank placements to Brazil's large external banking system, which is some 15 billion dollars. It doesn't apply to over 30 billion dollars worth of other creditor type debt, including all the Paris Club and World Bank debt. It doesn't apply to servicing the IMF, to which Brazil has paid over one billion one hundred million in principal during 1987, plus all interest.

We believe that a key element is to provide new resources, understanding what the real external needs of Brazil are and understanding that Brazil is going to tap all of its resources. We think that in the new deal there will be a lot more fine-tuned menu items. Securitization in some form will obviously come about. There will be a very good debt-to-equity program. There's a tremendous amount of interest in the market place in converting debt instruments into equity in Brazil, because everybody sees Brazil in the long haul as a pretty good place to be. There also will be a re-lending and on-lending program to the extent that the Central Bank can allow the funds to flow back out into the economy.

I'll give you a quick run down on some of the other countries:

— Chile is a country that the banks view as somewhat of a success. It's also had a good deal of luck in the past year or so with the increase in copper prices. It came back last year for a little bit of new money from the banks, and got it in the form of retiming of interest payments. Since that time Chile has retired over 20 percent of its debt through a debt-to-equity program, and is now in discussions in New York and Washington about whether or not we can provide more flexibility to the package, given that they don't believe the copper prices are going to stay up forever.

— Columbia hasn't rescheduled its debt. It had five percent real GDP growth last year. It's consistently grown, and consistently manages its external position well. It is cognizant of its position, and would like to see its real debt levels maintain about the same relationship with GDP that is present today. Essentially we refinanced about 80 percent of the public sector maturities due in 1987 and 1988.

— Venezuela has never asked the banks for new money. It took us a long time to re-negotiate their debts, simply because there are lots of issues, but Venezuela is going back into the market place. The Morgan Deal, the old bond deal that they have been kicking around for the last two years, is finally going to happen.

Venezuela is a unique place. Petroleos de Venuezuela (PDV SA), the oil company in Venezuela, never borrowed a cent. It is the 17th largest company in the world and is quite well run. It never had so much as a hiccup in all of the time that they were supposedly in this debt crisis. The government of Venezuela issues "Pagares" notes in U.S. dollars, usually with maturities of one to three years. These notes have been trading in the marketplace at 90 to 100 percent on the dollar since day one. They were never in danger of being in default, and nobody ever thought they would be. In Venezuela, like other OPEC countries, the oil price is key.

— Mexico. A year and a half ago there was a multi-year rescheduling done for Mexico for some 45 billion dollars. It was probably the single toughest negotiation that the banks have ever gone through. It ended up in a major meeting in Washington, at which the banks finally committed some six billion dollars worth of new money to Mexico, within the context of a World Bank, IMF government-to-government program. That program allowed Mexico the time to change a lot of its internal policies, which it did do with some degree of pain, but it did follow through in an adjustment program.

That adjustment program led to the most significant thing of all in my opinion; namely, a vote on the part of the Mexicans with capital overseas to bring back their money. And, indeed they did, in droves. For a time, the Mexican capital market went absolutely crazy. They have recently had a reverse of that due mostly to October 19th and I think the reaction of the Central Bank in Mexico has been what one would want to see in that kind of situation. They have as a result built up significant reserves, despite the fact that oil prices have been weak. They have changed an external economy that was dominated by oil into one that is less than 50 percent oil oriented, and hopefully they have gotten themselves into a position where they can deal with their external credit situations in a much more market oriented manner than they had to up to the present.

In conclusion, we believe that the menu and the case-by-case approach to each one of the countries is key. Each country is different. Each country has its own needs. And as bankers we must, if we are going to get repaid, maintain the credit-worthiness of the countries we deal with. Without that they won't grow, and if they don't grow, they don't pay back either the banks or governments or anybody else. Worst of all, they don't provide a decent standard of living for their people.

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By William R. Flynn
Senior Vice President, International Division, NBD

To give the regional bank perspective, I think I'll present the National Bank of Detroit as sort of a case history that may be representative of other regional banks. However, we should keep in mind that the regional banks themselves have a great diversity in how they view the debts in Latin America and the Third World in general, quite apart from their differences with the Money Center Banks.

I think NBD is not terribly unusual as a regional bank in the five year Latin American history we've just gone through. To set our bank in perspective, we finished this past year with about 23 billion dollars in assets, which would put us in the top 25 banks in the country. We have branches or subsidiaries in six foreign countries, so we're quite serious about the international banking side of our business. Our international risk assets are around two and a half billion dollars, which is just over 10 percent of our total bank — not a dominant part of the bank, but also not so small that it's ignored. Our Latin America portfolio is about 215 million dollars, which represents less than one percent of our assets. About 13 percent of our capital is in loan loss provisions.

In the 1960s and '70s, we wrere active traveling in Latin America. We had an idea that we could provide a beneficial service to our mid-western corporate customers and make money at the same time by financing joint ventures in Mexico and perhaps in Brazil. And so we did that, but at the same time that we were working in Latin America, we were also opening branch offices in London, Frankfurt, and Tokyo, so that our focus was not strictly on Latin America.

"One of the difficulties we had was in accepting the concept of 'fair share.'... We thought there was probably a divergence of interest."

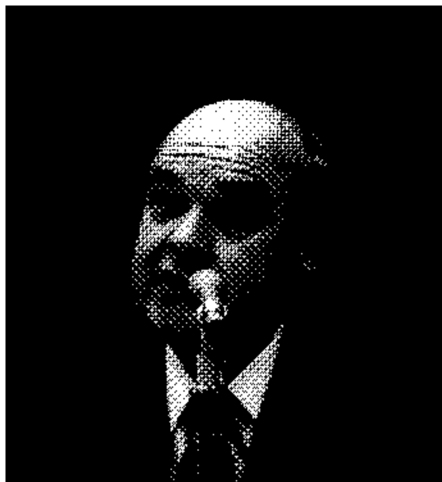
Mexico was a special case because it is a border country. A great deal of the auto industry is located in that country. It has substantial oil reserves, so we at that time felt more comfortable in building up a larger portfolio there. But we didn't want to finance infrastructure projects; we didn't want to make direct loans to governments in South America and we were able to accomplish that. We did not participate in any jumbo syndicated loans — the 500 million, the billion dollar loans. Whatever we did, whatever mistakes we made, we did on our own and through direct solicitations. And those are the loans essentially that are left with us, although some of the loans we made to private and semi-public companies are now concentrated in Central Bank obligations, which was not our original intention.

In 1982 we had a total of 25 million dollars outstanding in the countries of Peru, Ecuador, Venezuela, and Argentina — all to export or joint venture distributor type businesses, and none to government agencies. We had 80 million dollars in Brazil, which was virtually all to the private banking sector, either trade financing or interbank placements. And, the six or so million dollars that we had to finance exports in joint ventures is now owred to us by the Central Bank of Brazil in this medium term lending program.

Mexico as I said was a different situation and we had at that time over 200 million dollars in loans, over 70 percent of it to commercial banks, trade and to joint ventures, and the rest to government-owned financial institutions. We had zero debt to the United Mexican states and, except for the new money schemes, we would probably have zero today.

Now, who did we make our loans to in Mexico? Some of the names that were involved at the time were companies like American Motors,

"These Mexican joint ventures had In some cases better balance sheets than many companies in our Immediate market area, so that we could apply the normal credit rules. However, we neglected the country risk in making some of those decisions."



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Rockwell, Boeing, Libbey-Owens-Ford, Bendix, DuPont, Quaker Oats, and Dana Corp. These are names that we felt pretty comfortable with. And I might add that these Mexican joint ventures had in some cases better balance sheets than many companies in our immediate market area, so that we could apply the normal credit rules in looking at them. However, we neglected the country risk in making some of those decisions.

In any event, I should tell you our reactions to the debt restructurings. I think Bob McCormack and Citibank have done a phenomenal job in working with a very complex situation.

I guess we have come to adopt a more micro, rather than a macro view, of the debt problems in the past five years. We have done our fair share of time looking at the economics and the political aspects and the big picture, but we are concentrating more on the small picture at the present time.

One of the initial difficulties we had, even back in 1982 and '83, was in accepting the concept of "fair share" — that the banks were in this all together and that we each had to contribute according to our means, which really meant the percentage of credit you had outstanding at some particular date in 1982.

As the statistics surfaced and it appeared that nine Money Center Banks held 65 percent of the loans to Latin America and the other 200 or 300 banks had the other 35 percent, we thought there was probably a divergence of interest and that the established goal of keeping the ball in the air was probably more important to some than to others.

But as we looked at the early reschedulings that were done, we certainly had no problems with the stretch-out of maturities. In fact our early view was that these were probably not long enough. The interest rates were often discussed and comments were made that some of the margins over life or over prime had to be kept high to accommodate the regional banks and keep them interested in extending new credit or in restructuring the old.

Our view was that the margins were too high and that they should be reduced to not much over cost of funds or even to cost off funds. The new money concept gave us a great deal of difficulty from the very outset and, except for Mexico, we were essentially non-contributors. I think in several countries, we refused to participate and finally did say that if they wanted complete signatures of all banks participating, we would be happy to lend an additional ten thousand dollars. Surprisingly in most cases they told us that was totally unacceptable and unthinkable, and in the end they took our ten thousand dollars and we signed.

In the case of Mexico we did have a larger concentration and therefore felt more responsibility, so we did give a portion of our fair share in the first two restructurings and a fairly nominal sum in the last go round that was completed in 1987. But it was nominal enough that we made the Mexican black list and I guess we're not as good as we were in their eyes, although we think we've been cooperative in many other ways. We have yet to find out what the black list truly means, but I suppose we will at some time or other.

Looking at our present options I think we're prepared to let the ball fall, if that is what really must happen. But it would not appear that that is imminent by any means. We are one of a limited number of banks who have not announced in the last several weeks that we are taking extra provisions or that we are making special allocations for LDC Debt. We are relatively comfortable with our capital position and with our existing loan loss provision, which we think is quite adequate, taking into account the overall position of our domestic loan portfolio, which has typically been very sound.

If we look at our debt in an objective way we find that our exposure to the private sector in all of Latin America is relatively small; we have been dealing with this on a case-by-case basis; we have taken some modest writeoffs in several cases; we were fortunately able to induce a couple of our domestic corporate customers to guarantee loans to joint ventures that they had not originally guaranteed. We see that this private sector portfolio will probably be extinguished in one way or another within the next 12 to 18 months.

If we look at our public sector debt in South America, this has dropped to relatively small positions. We have begun to charge off our government loans in Ecuador and Brazil, since they have not been paying interest

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About the Author: William R. Flynn is senior vice president and head of the National Bank of Detroit's International Division, where he is responsible for the bank's international credit exposure, including loans to lesser developed countries.

By Joseph Wood
Vice President, Financial Policy, Planning and Budgeting
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"The World Bank operates as a market-based institution. It operates as a bank, not as a debt collection agency for the world."

hen the subject of the debt crisis is raised, we at the World Bank always have to ask some clarifying questions, because from our point of view, there are really multiple debt crises.

Today's panelists are primarily concerned with the crisis of the middle-income countries of Latin America, as well as several other middle-income countries throughout the world. There exists an equally severe debt crisis in Africa. But even if we consider only the middle-income countries of Latin America, it is not altogether clear whether the problem is that of the creditors or of the debtors.

In most debates on the subject of debt, the tendency is simply to assume that the problem is how to fix the debt overhang — that very large burden of debt owed by LDCs, or the very large claims of the creditors. The notion is that something has to be done to reduce the burden of debt. The problem is to do it in a way which doesn't impose intolerable damage, either on the financial system or on the borrowing countries themselves. With reference to the borrowing countries, the issue is to find a way of reducing the burden without impairing the prospect for restoring access to voluntary capital flows.

However, this is a seriously incomplete view of the problem. In the late 1970s and the early 1980s the conditions necessary for sustaining growth in these middle-income countries collapsed and those conditions have not yet been restored. In fact, if we could wave a magic wand and eliminate a significant fraction of the medium and long-term publicly-guaranteed debt owed to the commercial banks, we would not have solved the problem.

I think it is important to put the debt issue into some kind of perspective. The World Bank uses a grouping which we call highly indebted countries. We are referring to the 15 countries Secretary Baker mentioned in Latin America, Europe, the Middle East, and Africa, plus one or two smaller countries. Those "Baker Countries" currently have a total debt of approximately $500 billion. The medium and long-term debt to financial institutions is a little over one half of that amount — $250 billion dollars. If we could reduce the indebtedness to the banks by one half — to $125 billion dollars — the debt in relation to the output would decrease from 60 percent to 45 percent. That level is still considerably above the level of debt in relation to output these countries had in 1982 when the current crisis began. Therefore, we would improve the situation, but not radically transform it.

Debt reduction would, of course, also reduce interest payments. This issue can best be understood by considering interest as a share of exports. The Baker Countries

currently pay nearly 24 percent of their export earnings to service interest. Debt reduction of the magnitude assumed in my hypothetical example would reduce that amount to approximately 15 to 16 percent, implying an annual benefit equivalent to about one percent of the GNP of these countries.

Just the terms of trade losses for some of these Latin American countries (e.g., due to oil price changes) have been a multiple of that. Moreover, it's not at all clear that in order to achieve the benefit of that interest reduction — in terms of actual resource availability — it's necessary to wave a magic wand and reduce the debt. There are other ways of handling financing on that magnitude.

Moreover, conditions for restoration of sustained growth go well beyond the issue of the debt overhang. In particular, these economies need to be made more efficient. The stops that are within their power to take, and that can over time have an impact on their economies and on their standard of living, are a good deal more significant than one percent of their GNP.

In addition, these countries need trading opportunities. Reference has already been made to the comments of Professor McCracken — that a lasting solution to their current economic difficulties is probably not attainable without some degree of progress in dealing with the problem amongst the industrial countries. Resolving the important imbalances that exist among them must be done in a way that does not severely depress worldwide growth, and in particular does not severely depress the trading opportunities available to these developing countries.

The problem that needs to be fixed is that these developing nations need to be put back onto a sustainable growth path. To do so, one needs to keep in mind all three dimensions of the problem in developing countries, that is: 1) the debt overhang, 2) inefficiencies in their economies, and 3) inadequate trading opportunities.

The most important contribution the World Bank can make has to do with making improvements in the efficiencies of these economies. This is what we call adjustment, as opposed to stabilization. A reference was made to the progress these countries have made by cutting their imports in half. That is important progress in achieving stabilization or a reduction in resource use, but not necessarily in laying the basis for sustained growth. Much of the reduction in imports translates directly into a reduction of investment, thereby undercutting the foundation for sustained growth.

Now I would like to focus on one aspect of achieving sustained growth. It has to do with the environment affecting the private sectors in developing countries. Most of these countries have, over a period of time, developed a web of intricate regulations and controls that in many ways are stifling their own domestic private sectors. What is required is to modify those regulations so as to permit greater flexibility in allocating resources and greater latitude to the domestic private sectors. This includes, apart from reform of government regulations, financial sector reform designed to make sure that credit can go where it's needed, rather than where the political elites can command it to go. This also includes greater efficiency in the provision of government services that are often crucial to the productivity of the private sector.

These kinds of reforms are not headline grabbers, but in my view they are very important to provide a lasting solution to the problem. Their importance is illustrated by one of the phenomena that occurred during the last several years. As external resources were pumped into the economies of developing nations, almost as quickly they went right back out. Sometimes this is called "capital flight," but you should understand that this is the action of private parties pursuing their own interests. If the environment is hostile; if regulation stifles investment; if financial resources cannot be allocated to productive uses; or if the overall environment is one of crisis; then it's going to be a struggle to make certain that new money remains in the country. Dealing with the basic issues of efficiency is, in my view, the most important contribution that the World Bank can make.

Secondly, I think it's crucial that there be a strong practical and perceived linkage between the provision of external financial support and government efforts to make the economies more efficient. The World Bank is prepared to support these adjustment efforts and has, over the last few years, substantially increased its lending in support of these adjustment programs. In fact, last year the World Bank was responsible for nearly three-quarters of the net financing made available to Latin America.

Finally, I believe the World Bank should be very cautious about using its financial resources to take over, in some sense, the existing risk of other creditors. We want to see our resources used to support adjustment programs that are adequately financed. We are reluctant to see financial resources deployed in schemes which are not tied to adjustment programs and an overall financing package. Suggestions that the World Bank use its guarantee powers to permit some wholesale reduction in commercial bank claims on developing countries or to facilitate the capture of the discount available in the secondary markets raises major questions about the role of the World Bank.

The first question is, is it really necessary for the World Bank to intervene in this way? We have heard already this morning about the Mexico arrangement. The success of the deal will not be determined by the availability of a guarantee from a

third party, such as the World Bank. The most important issue will be how commercial creditors view the likelihood that Mexico will pay the interest on these *new* bonds. If they believe that Mexico is likely to service the interest, there's every prospect the deal will be successful. If they doubt that Mexico can be relied upon to service that interest, then I doubt that the tender offers will make this a successful deal. There is currently a tendency to feel optimistic about Mexico because the country is performing well and has a good record for servicing interest. However, these same conditions are not the case in all of the other heavily indebted countries.

Another issue is whether the World Bank's involvement is desirable. I don't doubt that there may be cases in which overall financing packages will require a degree of comfort from the World Bank. However, I'm questioning the notion of using World Bank guarantees as a first resort on a broad scale, independent of individual packages that include substantial adjustment and an adequate overall financing plan. The issue of the desirability of our participation has much to do with political support and capital market support for the World Bank.

Political support for the World Bank is dependent on the fact that it operates as a market-based institution. There aren't even 10 percent of the people in this auditorium who know the extent to which the World Bank operations in Latin America depend on taxpayer funds. People assume that, if it's not wholly dependent on taxpayer funds, it is at least largely dependent. The truth is, the World Bank gets shares subscribed by member countries. In the case of the United States, this subscription has been phased in over a period of years and involves a cash payment of roughly $100 million per year. Yet the World Bank commits about $15 billion a year and disburses about $11 billion a year. Thus it is obvious that the bulk of our resources does not come from government budgets, but rather from borrowings in the market place. If we were required to go to the legislatures around the world asking for a significant fraction of the resources that we need for our operations, the probability of success would be substantially reduced.

Moreover, markets attach great importance to the fact that the World Bank operates as a bank, and not as a debt collection agency for the world.

"Suggestions that the World Bank use its guarantee powers to permit some wholesale reduction in commercial bank claims on developing countries or to facilitate the capture of the discount available in the secondary markets raise major questions about the role of the World Bank."

The World Bank, unlike commercial banks, finances itself primarily in bond markets rather than money markets. Bond investors are traditionally very conservative, and look askance at an institution that exhibits a degree of flexibility about when it is repaid. It is very important to us that we're able to maintain what we call our preferred creditor status, and avoid participation in reschedulings. That posture is only credible if the World Bank share of the outstanding debt of these countries remains a small fraction of the total indebtedness. We already hold nearly 10 percent of these countries' debts. If we were to participate on a large scale, by using our own guarantee powers to shelter a large fraction of private sector debt, we would certainly jeopardize the credibility of our position as a preferred creditor.

I think these observations raise substantial questions abot some of the more sweeping proposals that have been put forward. The debt crisis is not just the problem of lightening the burden of debt. It's equally a problem of helping these countries continue on the path to improve the efficiencies of their economies. It's also a problem of avoiding steps which would further erode the trading opportunities available to these countries. The World Bank's major contribution should continue to be assisting these countries in improving the efficiency of their economies. We should try to strengthen the linkages between external finance and adjustment efforts and we certainly can do that with our own funds. We hope to be able to encourage others to join with us. Finally, our efforts to catalyse other resources, in the context of packages for countries that include substantial adjustment, should also include adequate overall financing. We should not jump to the conclusion that the only way to meet the interest burden on these countries is through a debt write-off.

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Debt Management:

After listening to the bankers and to the World Bank representative, I am reminded of the story of the British aristocrat who was walking by a pond in the woods one day. There was a man in the pond who was shouting, "Help, help, I can't swim. I can't swim." The British lord looked down at him and said, "Sir, I can't swim either, but I don't make such a fuss about it!"

There are dozens of countries that can't swim right now, and I fear that there are a lot of platitudes from the official creditor community about what they should do. All the evidence is that since the beginning of the management of this crisis in 1982, things have not gotten better, they have gotten worse. I merely need to remind you of the circumstances of the major debtor countries in Latin America right now.

Mexico, which we've heard is the success story, has a 180 percent annual inflation right now; a political system of declining legitimacy; tremendous and deepening poverty in the south of the country with real wages having declined by about 40 percent in the last five years; and a stock market which has declined by over 70 percent since mid-October. Mexico is in deep crisis, and yet is called the model debtor country, the one we've been told that represents how best things might go!

If you move down to Argentina, the current Alfonsin government (which may well be the best government that Argentina has had in 50 years), was severely defeated in an election last fall, thus undermining the capability of reform for several years. Economic circumstances have now deteriorated so far as to produce what is currently about a 300 percent annual inflation rate, a continuing decline in GNP per capita, no capacity to meet debt payments, and a Central Bank almost devoid of reserves. The Argentines are here in Washington for the N-th waiver on the conditions on their IMF and World Bank loans, as well as for an emergency loan from the U.S. Treasury, which will no doubt be forthcoming because it's the only way to keep Argentina out of overt bankruptcy and collapse. The name of the game is to keep the illusions going, rather than to look at the realities.

Next door to Argentina is Brazil. Brazil now has a 300 percent annual inflation rate and is apparently entering the deepest recession in its modern history. It has a political system in complete disarray, with a president who seems to be willing to trade anything in the country for a fifth year of office, a man who has no political legitimacy himself right now and a sitting constituent assembly which could do anything to the political system in the country.

Peru just nearby, is on its way to hyperinflation. Its president is now busy invading private firms that he thinks are violating price controls, while the whole macroeconomic

By Jeffrey D. Sachs, *Professor of Economics, Harvard*

A Hard Look at Realities

situation is so destabilized that there is probably no way of avoiding hyperinflation.

One of the very few success stories in the region is a case that I became intimately involved with as the chief economic advisor to the president in Bolivia. Bolivia reached a 50,000 percent hyperinflation in 1985, but for the last 18 months, under a stabilization program which I participated in designing, it has had an annual inflation rate under 10 percent — the lowest inflation in Latin America.

Now how did that come about? The bulk of Bolivia's success resulted from the profound fiscal and regulatory reforms which this government has instituted. But another reason was that Bolivia finally said what was unspeakable before then, which was that they could not pay the debt and they just stopped paying it. During 1986, despite the fact that the 50,000 percent inflation had only just ended, the World Bank and the IMF were insisting on a resumption of interest payments on commercial bank debt, which would have cost about 50 percent of the revenues of the Treasury of Bolivia and would have resulted, I think without doubt, in a resumption of the hyperinflation.

The key to understanding the debt crisis in my view, is that the debt is owed by governments, and the governments are bankrupt. No country, no political system, can function adequately with a bankrupt public sector. The government is simply too fundamental and central to the health of an economy to have an operational economy, much less economic growth, with a bankrupt public sector.

Moreover, the debt has a secondary effect which is extremely important. Not only is the direct burden of the debt a compelling problem, but the fact is that when governments now try to reform, they meet tremendous political opposition, because the objection is raised that the reforms are for the sake of foreign creditors, for the foreign banks. And why should the country pay more and suffer even more austerity for the sake of foreign banks? This reasoning leads to a powerful political argument against reform, and is like a bone in the throat of the political systems of the debtor countries. They cannot really reform adequately if the proceeds of the reform flow to foreign creditors.

I know in Bolivia, which undertook incredibly harsh austerities in the last few years, that the only way that reform was made politically feasible at all was by reminding the Bolivian public every day of the week that the reforms were for the sake of the Bolivian people, because not one penny was being transferred to foreign creditors in the process. You cannot pay the debt, and impose more austerity, and hope to do economic reform in these countries, all at the same time. The political system won't allow it, even if part of the money were available, and the money simply isn't available.

Between 1982 and 1987, the debt management strategy of the U,S. and the IMF has had one major success: namely, that the balls have been kept up in the air — the banks have kept most of their loans to Latin America on their books at full value, and there has been an illusion that things are okay. Also, there has been an important real improvement in the state of the banks, because the banks stopped lending in 1982 to these countries, and the banks proceeded to increase their capital base, so that the extent of their exposure relative to capital has declined significantly.

The debt management strategy which insisted that the countries must repay at any cost was probably appropriate for a few years (1982-84), because the banking system was in real crisis. After five years, the banking system is no longer in crisis. There are only two or three banks in the United States that are seriously at risk from a major decline in the values of the LDC claims. The regionals are out of the woods. It is a painful thing to write down the debt perhaps, but it is not a life-or-death issue for any regional bank in this country, and almost for no money center banks in this country. So, we've solved much of the problem. The international financial system is safe. However, unless we get off platitudinous ideas about getting the countries out of trouble, and

recognize that the debt service burden must come down substantially in order to free up resources and remove political bottlenecks to reform, we are not going to be able to move on and solve the rest of the crisis, the part involving the debtor countries themselves.

What I'm saying is widely recognized in the financial markets today. The notion that the countries cannot fully repay their debts and will not fully repay their debts is not a secret to any of you. It was a matter of conjecture and debate up until mid-1985, but now that many investment banks are sending around weekly spreadsheets on the secondary market prices of bank loans, we see quite well what the market assessments are on these commercial loans. You can get a $100 claim on Bolivia for ten dollars. Sudan is selling for a remarkable $2 per hundred. And the big debtors, Argentina and Brazil, are down to the 30s and 40s per hundred. What we're hearing from the markets is that the countries are not going to service their debts fully in present value terms.

The average secondary market price of debt when weighted by size of exposure of U.S. banks is probably 45 cents to 50 cents per dollar right now. It's been declining so fast that I have to keep on redoing the calculations. It was 55 cents in July of this year, but now it's down probably to about 45 cents because of the significant decline in the value of the Brazilian debt.

Not only is there a secondary market discount on the debt, but the New York Stock Exchange is also reflecting these discounts. The best way to see that is to examine the stock market valuation of the U.S. commercial banks. It turns out that if you compare the stock market value relative to the book value of the 40 to 50 largest banks in this country, the ratio will be closely related to the size of exposure of the individual banks in the developing countries. Banks with a large amount of Latin American debt in their portfolios show a lower market value relative to book value. Thus, the banks have been punished in the stock market according to the size of their exposure in the third world. In other words, the New York Stock Exchange is putting a price on Citicorp of 40 cents or 45 cents per one dollar of claim that Citicorp has on Brazil. Thus, the economic value of the banks is already reflecting substantial losses from their LDC exposure even though the accountants and the regulators and the banks are pretending through all sorts of extremely clever means that this debt should still be valued at its face value.

"Why should the country pay more and suffer even more austerity for the sake of foreign banks? This reasoning leads to a powerful political argument against reform, and is like a bone in the throat of the political systems of the debtor countries. They cannot really reform adequately if the proceeds of the reform flow to foreign creditors."

What that means from a bottom-line perspective is that it makes good business sense now for a bank to sell off LDC claims at a substantial discount, take the tax savings on the capital loss, and watch the stock market price go up. If a bank gets 50 cents cash for Brazil, not only does it replace a 50 cent value asset for 50 cents in cash, it also gets the tax savings on the write-down of the 50 cent capital loss. Presumably it has an effective marginal tax rate of perhaps 20 to 33 percent, so that the value of selling at 50 cents might be worth 66 cents (50 cents plus tax savings of .33 x 50 cent loss) to a bank that liquidates these claims.

There are all sorts of regulatory problems in getting this liquidation accomplished. We're seeing with the Mexico deal already that some of the regulatory problems — not the economic problems, mind you — the regulatory and accounting problems, might block good sensible economic deals now.

Since the banks would not be adversely affected, relative to their current situation, by accepting a deep writeoff of debt in return for cash (or a safe asset of equal value), there are now opportunities for reducing the debt burden on the LDCs without hurting the banks any further. Now the final point, which Mr. Woods has anticipated at considerable length, is "Where do you get the money to re-purchase the debt?" And the answer is, in the first instance, from the World Bank, or at least from the official creditor community. In fact, as I shall explain, the official creditors and the World Bank could actually make money on the transaction in the long run. Let me explain why a new role for the World Bank is beneficial from the point of view of the debtor countries; highly beneficial from the point of view of the World Bank itself, as an international institution which is devoted to world economic development; and highly beneficial for the foreign policy interests of the United States.

First, it's very important to get the right category of debt as eligible for debt relief Remember when I said the problem is bankrupt debtor governments. What we need is relief for debtor governments. So we must look at the bank lending to governments. We can ignore all of the short-term debt, which should not be re-scheduled because rescheduling short-term trade credits would create havoc with the trading system. We should focus on medium- and

long-term debt from the banks to sovereign borrowers. Such lending amounts to approximately $200 billion of bank exposure to all of the problem debtor countries in the world. In the global scheme of things, that's a "small" number. The $200 billion of debt now has a secondary market value of about 95 billion dollars of relief. By writing this debt down to market, we'd get 105 billion dollars of relief, which I believe would have tremendous beneficial "multiplier" effects in the debtor countries in a political sense in addition to the direct resource savings for the debtor countries.

There are many specific ways that the debt writeoff could be structured, but all of the most attractive ways involve the participation of the IMF and World Bank. Several proposals (such as those of the American Express Bank, Senators Sarbanes and Bradley, Congressmen Lafalce, Morrison, and others) call for the official institutions to take over the existing debt in the following manner. The World Bank (or the IMF) would give the commercial banks new World Bank bonds in return for the existing bank debt. The bonds would be swapped for the bank debt according to the current secondary market price of the debt. In other words, the World Bank would give the commercial banks $10 of bonds in exchange for each $100 of Bolivian bank debt; the banks would get about $30 per $100 of Argentine debt. Only debtor countries undertaking internationally supervised adjustment programs would be eligible to participate.

Then, the World Bank would become the creditor of developing countries, and a debtor of the commercial banks. The World Bank would then reduce the amount that the countries owe to it, conditional on the countries undertaking sound structural adjustment programs. The reduction in debt would not have to match the purchase price of the debt. For example, Bolivia's debt to the World Bank might be reduced to a level of $15 per existing $100 of debt, rather than the purchase price of $10. Argentina's debt might be reduced down to a level of $35 per $100 of existing debt. The idea here is that in the long-term the countries will be able to pay something more than the current secondary market prices once the crushing debt burden is reduced.

The World Bank would use the receipts of interest from the debtor countries in order to service the bonds that it has issued to the commercial banks. Assuming that the countries fully service the reduced amounts of debt, then the World Bank would stand to *make a profit* (for example, it would receive in present value terms $15 from Bolivia for each $100 of current debt, and use that to pay off $10 in bonds to the commercial banks, thereby pocketing $5). By acting as deal maker, the World Bank, on behalf of the world's taxpayers, would actually earn a commission.

"The average secondary market price of debt when weighted by size of exposure of U.S. banks is probably 45 cents to 50 cents per dollar right now. It's been declining so fast that I have to keep on redoing the calculations. Now it's down to about 45 cents because of the significant decline in the value of Brazilian debt."

The taxpayers would, however, bear a residual risk, if Bolivia cannot meet even $10 debt repayment (per $100 of existing debt) or Argentina cannot even pay $30 per $100. In that case, the World Bank would have to honor its bonds to the commercial banks, but would not receive an adequate cash flow from the debtor countries. The World Bank, and ultimately the creditor country taxpayers, would have to absorb the loss. Even here, however, the risks are rather modest.

As a worst case scenario, suppose that the World Bank faced, over a period of 5-10 years, a default by the debtor countries on as much as 30 percent of the reduced debt. The Bank might then lose about $30 billion in the deal, or perhaps $3-5 billion per year. The U.S. share of that would be about 25 percent of the loss (which is the approximate U.S. share of contributions to the World Bank), so that U.S. taxpayers would lose about $0.75-$1.25 billion per year. This would be less than 10 percent of the U.S. foreign aid budget per year!

Thus, at little risk, and a good chance of profit, the World Bank could effectuate a debt reduction of $100 billion on the existing bank debt. Most, or all, of the debt reduction would be borne by the banks and not the taxpayers. The commercial banks themselves would be left no worse off than they are now. And the developing world would once again have a chance to recover and grow.

About the Author: Jeffrey Sachs, professor of economics at Harvard University, is also a consultant to the governments of Bolivia and several other developing countries on macroeconomic stabilization issues; a consultant to the World Bank; a research associate for the National Bureau of Economic Research in Cambridge, Mass., and director of that organization's project on LDC debt; and a member of the Brookings Institution panel of economics. He has written extensively on macroeconomic issues.

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hen I was an accounting student a professor told me to look at a thermometer on the wall and tell him what I saw. I said, "Well, I see the temperature." And, he said, "You've made a bad mistake. What you're looking at is the height of the bar of mercury in a glass tube. It's supposed to represent the temperature, but it's not the temperature."

That's the position that we as accountants find ourselves in when we audit financial statements of companies. The financial statements are the representations of the financial condition of the company, but they are not any more than a representation. Unfortunately, we lack the ability to project the long term view that many others can take because we have to deal with financial condition and earnings from quarter to quarter in light of current conditions as our clients release results to the public. And, so we have to take a more micro view of how to deal with issues in a transactional sense.

I'd like to present the two views on the LDC debt situation that are currently held among accountants. The first view is that since we really couldn't predict the future realization or lack thereof of LDC principal and interest, the best course of action was to provide a very detailed level of disclosure. Upon listening to the investment banking community, maybe accountants haven't done such a bad job. It appears that the LDC debt disclosures made in bank annual reports have caused the share values to seek the appropriate level in the marketplace. This would imply that financial statements have communicated to the marketplace the financial condition of the companies.

VIRGINIA GEREN

"Companies actually did repay their debts. The problem was, they repaid them in local currencies."

It's important to understand why accountants can't assume a very quick position on this issue. Many sovereign LDC loans were initially extended to private corporations that were large household names. Many of the companies paid their obligations in local currency. However, the central banks didn't have the reserves to acquire dollars to turn around those local currencies and repay the dollar denominated debts.

Accountants (and bankers) hadn't seen a cycle like this, and certainly hadn't made accounting decisions based on events that were so highly influenced by economic and political conditions within a country, and so we took a very conservative and cautious view. Many believe that this is a position we should continue.

The second accounting point of view, is that the credibility of financial statements are in jeopardy if we cannot determine when to recognize economic losses and record them in

for LDC Debt

By Kenneth Cooper
Partner, Touche Ross & Co.

the proper accounting period. Those who accept this view are concerned about the wide discrepancies between the size of loan loss reserves recorded in the financial statements of different banks. Some banks have reserves of 24%; some have reserves of 60%. That's quite a difference. And when in addition to that difference, the secondary market discount can be greater, you begin to question what is credible? So the immediate result of the other point of view has been a rather large financial statement loss.

Those who do not accept that point of view note that banks cannot record a loss unless they can demonstrate it is probable. If a commercial borrower is not going to suffer a credit loss on principal, but only a reduction in interest over a long period of time, under the current accounting rules banks may not be able to record a write down of principal. They maintain that accountants would not allow loss recognition such as that recorded by the Bank of Boston in the financial statements of a Texas bank which is restructuring a real estate loan.

The other point of view maintains that accountants would also not allow that Texas Bank to capitalize interest in the way that a Money Center Bank appears to when loan interest paid is largely funded by new loans. So the accountants find themselves with a very difficult conceptual problem.

One of the critical components in assembling the recent Mexican debt swap was a very simple accounting decision. When does the accounting event occur? At the time when the bank declares its intent to make a tender? Or at the time when the actual transaction has been concluded?

Why is that such a problem? If a bank is allowed the opportunity to record an accounting event when the transaction is concluded, then it can tender at various discount rates. But, there is little risk from an accounting context until a tender is accepted. That's not the position that the SEC finally accepted. The SEC believed that on the day the institution makes a tender an accounting event has occurred. A bank must recognize that even either as an adjustment to the allowance of loan losses, if necessary, or a write-off of the loan value based on the tender price. If a tender was made at three prices, then there would be three debt prices.

When the transaction has been consummated, the new instrument must be transferred from loans to investments at fair value. If the initial accounting event created a reduced loan value to the tender price, and shortly after that trading on the new instrument occurs, a further write down is required.

The last point is that the U.S. regulatory focus is beginning to change as a result of the cooperation between the U.S and the international regulators. The new spirit, in terms of capital, has been "convergence." Capital convergence is an idea that has been promoted by the United States and the U.K. The U.S. banking community is trying to obtain convergence in order to acquire equal footing with other international banks competing in the same markets.

In the course of convergence, however, there were some things that the U.S. had to give up. One of them was the notion that the allowance for loan losses is a part of the most important type of capital. Under the new guidelines, core capital (the tier-one capital) is common tangible equity. This is quite a difference from primary capital, which banks had been reporting in past years. Primary capital included the allowance for loan losses in addition to retained earnings and shareholders equity. Although those rules are not in place currently, they are the rules by which the regulators are beginning to view the existing conduct of business. They have a tremendous impact on both the way banks and regulators view the size of the loan losses.

I believe that in the future accountants will continue to look (as bankers) on a transaction-by-transaction basis. I believe they will be influenced by events but there will also be a recognition of the strong role that the regulators have in the transaction. As accountants look for guidance on how to account for LDC debt they will listen to the institutions, the market, and regulators to make their decisions in the future.

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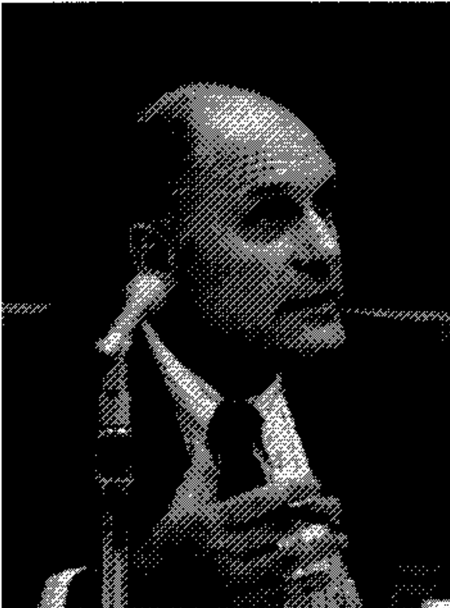
By Gueter Dufey

Professor of International Business and Finance
The University of Michigan



VIRGINIA GEREN

"We're talking about a *middle* class that has lost confidence in its own capital markets."

Today I'd like to focus on a few basics and perhaps change some of the emphasis on the question of third world debt. First of all, I think one should not lose sight of an essential part of the debt crisis — that is that many of these countries will need new money. They are countries with tremendous growth potential, a potential that they cannot realize with their own internal savings. In order to realize that growth potential they will need access to external markets over the long term.

Therefore, any proposal that we consider should be judged on what it will do to the access of these countries to new sources of funds. Or, to put it in very concrete terms, what will it take to persuade the Bill Flynns of this world and their institutions to make additional loans? If you listen to him, that is not going to be an easy chore. And surely, any proposal that will simply write these things off in one way or another, with or without the help of the World Bank, is not going to bring these institutions back as international market participants.

What is required is that these countries — as hard as it is — make a credible commitment to service debt. Here I would like to underline what has been said before: the real issue is not repayment of debt per se. There are very few people who repay their debts, including the U.S. government and any other government. What matters is paying interest without having the bankers sweat.

The point then becomes: what are the chances of serving that interest? With respect to the largest debtor countries, it takes about three to four percent of GNP because, after all, interest is paid out of GNP. So the challenge is that countries have to pursue policies that allow them to keep their own internal absorption of resources for domestic consumption and domestic investment at three to four percent below what they produce in real goods and services. This is, in other words, the equivalent of you reducing your spending as an individual below three to four percent of your income. If we put the solution in these terms, in spite of all the problems, it is possible, and a number of countries accomplish it.

I have just been in the Far East and I followed the discussion in Indonesia which has many of the problems worse than the problems that we find in South America. And yet, the Indonesians somehow manage not only to devote a portion of their meager resources to paying interest but they're also talking about making payments on principal which, under those circumstances, they would be able to refinance. So the problem is really one of generating sufficient resources to pay the interest. And this raises a further point.

There are fundamental differences

between lending to a firm and lending to a country. As we have heard, what starts out as lending to firms internationally is, *defacto,* lending to governments. And, unlike in a firm, a government's ability to pay interest is not a matter of ability but a matter of willingness. A firm confronts prices which are set by the market. In contrast, a government's payment of interest is a matter of its political willingness to keep spending at a margin of two, three, or four percent below its GNP.

Once you accept the fact that a country's debt service is a political decision, then it suddenly matters how we account for that. In politics, we often hear the question, "How does it play in Peoria?" Let me modify that slightly and say, "How does it play in Sao Paulo when people read that CitiBank has made provisions or Bank of Boston has written off the debt?" Let me assure you that those headlines in the local papers are interpreted that the banks have forgotten or "written off" the debt. Obviously, that reduces the willingness of the body politic to continue to service that debt. And the politicians in these countries, while they know exactly what the economics are, do face a lot of political pressures.

In this respect, what we debate here merely as "shadow accounting" has important signaling effects in these countries, affecting the willingness of the body politic to adjust those economies sufficiently so that they can take that 2-3 percent out of the resources that they create.

The last substantial point that I want to raise is the question of whether that adjustment is really simply a matter of austerity? I think the traditional austerity picture diverts attention from what is the other, and in my view, the more important problem. And that problem refers to the capital market policies in the debtor countries. Let me give you some of the numbers on the capital flight from those countries because they are staggering. At the same time that Venezuela borrowed 38 billion dollars, Venezuelans invested virtually the same amount outside. Mexco's data are also impressive: during the same period that Mexico borrowed a hundred odd billion dollars, Mexicans invested approximately 53 billion dollars outside.

We're not talking here about some drug barons or corrupt politicians, we're talking about a whole middle class that has lost confidence in its own capital markets. What we confront here is the complete distortion of capital markets in these countries in the widest sense. There are nice graphs available which show how a middle class saver in Brazil, in Mexico, in Argentina would fare if he or she had been imprudent enough to put their funds into the domestic savings vehicles. I can tell you these graphs all go in one direction — down.

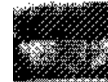
To use another example: Brazil has an ingenious system of inflation adjustment. If you look at the inflation adjustment in the capital markets, you'll find that during certain years the OTN adjustment by which savers were presumably compensated for losses due to inflation were arbitrarily held by the government at a fraction of the true inflation. In 1982, for example, when an investor in government bills and all other financial instruments that are tied to that index, came to the Treasury to get his money back, he found that the OTN factor was adjusted by only half the inflation. To put it in a U.S. context, that is the same as if you were to buy a U.S. treasury bill, and at the end of the year when you came to get your money, they said, "Well, we've had a bad year, so we'll pay you back only half— 50 cents on the dollar." Ladies and gentlemen, if you are treated like this you do like those people do and take your money out of the country!

But, it doesn't end here. I want to just remind you: each and every one of these countries has exchange controls. And exchange controls — just like market interest rates — have one purpose; that is, to give the class in power preferred access to funds, whether those are domestic loans or foreign exchange. This is where the real problem is. Because if you keep prices below the equilibrium point, somebody has to allocate credit, and this is a perfect way to reward your friends and punish your enemies even if you occasionally have the best intentions to begin with.

Finally, a significant aspect of the capital markets in these countries is that the capital assets are largely in the hands of politicians and out of the hands of competent people, whether they are domestic entrepreneurs or foreign entrepreneurs. One can argue that these policies have always been in place and they are endemic to the political structure of these countries. That is only partially true. But the point is that with the easy access to external funds, the problems have become worse, because with such distorted markets, the more money you have, the more damage you can do. And the fact is that unless something is done to change the internal capital market problems in these countries, every proposal for reform is simply a pipe dream.

To sum up: New money has to be provided, but new money will only be provided if the providers of funds can see, a) that ultimately the debt will be serviced; and, b) that by the same token the funds will not be wasted or will not simply wind up in the hands of the customers of the private banking department of the same institution that makes the loan. I think that unless we address these particular issues, the debt crisis is not going to go away!

About the Author: Gunter Dufey is professor of international business and finance at the Michigan Business School. His academic interests include international money and capital markets and the financial policies of multinational corporations. He has served as a consultant to the U.S. Capital Control Program of the U.S. Treasury Department and a member of the Economic Advisory Board to the U.S. Secretary of Commerce. He has completed research reports on international investment for the U.S. Department of the Treasury; on Japanese banking regulations for the OECD in Paris, and on the international competitiveness of U.S. Financial Institutions for the Office of Technology Assessment of the U.S. Congress.



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First year BBA student Alexandra Warren receives the new Procter & Gamble Undergraduate Minority Scholarship from Timothy MacMillan (third from left) and Norb Mayrhofer (right), both P & G District Sales Managers. To the left is William Quails, assistant professor of marketing who is working with P & Gon placing students in their sales division.

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Second in a series about Scholarships and Fellowships at the Business School

Alexandra Warren, a first-year 1~\ BBA student, has received the Procter 8c Gamble undergraduate minority scholarship of $1,000 per year for two years. This is a new scholarship established by P & G. "We would like to become more involved with the Black Business Students Association," said P & G District Sales Manager, Tim MacMillan. "We want to let minority students know about the opportunities we have to offer."

Alexandra has financed 100% of her education through scholarships, grants, and part-time employment. She worked in the personnel department at Jacobson's 20 hours a week before the Procter 8c Gamble scholarship helped make it possible for her to quit that job. She says that not having to be at work for certain specified hours was very helpful to her life as a student. She still is involved with outside activities, such as her extracurricular volunteer work, but the hours are much more flexible.

Alexandra is interested in finance, and will spend the summer in an internship in investment banking at Michigan National Corporation.

Alexandra is active in extracurricular activities. She is a member of the Black Business Students association, is on the corporate finance committee of the Finance Club, and has been appointed to the executive board of the Michigan Students Association as treasurer.

This last job involves a lot of responsibility. "I handle a budget of over half a million dollars, including all financial aspects, insurance, and IRS reporting. It's like running my own company," says Alexandra.

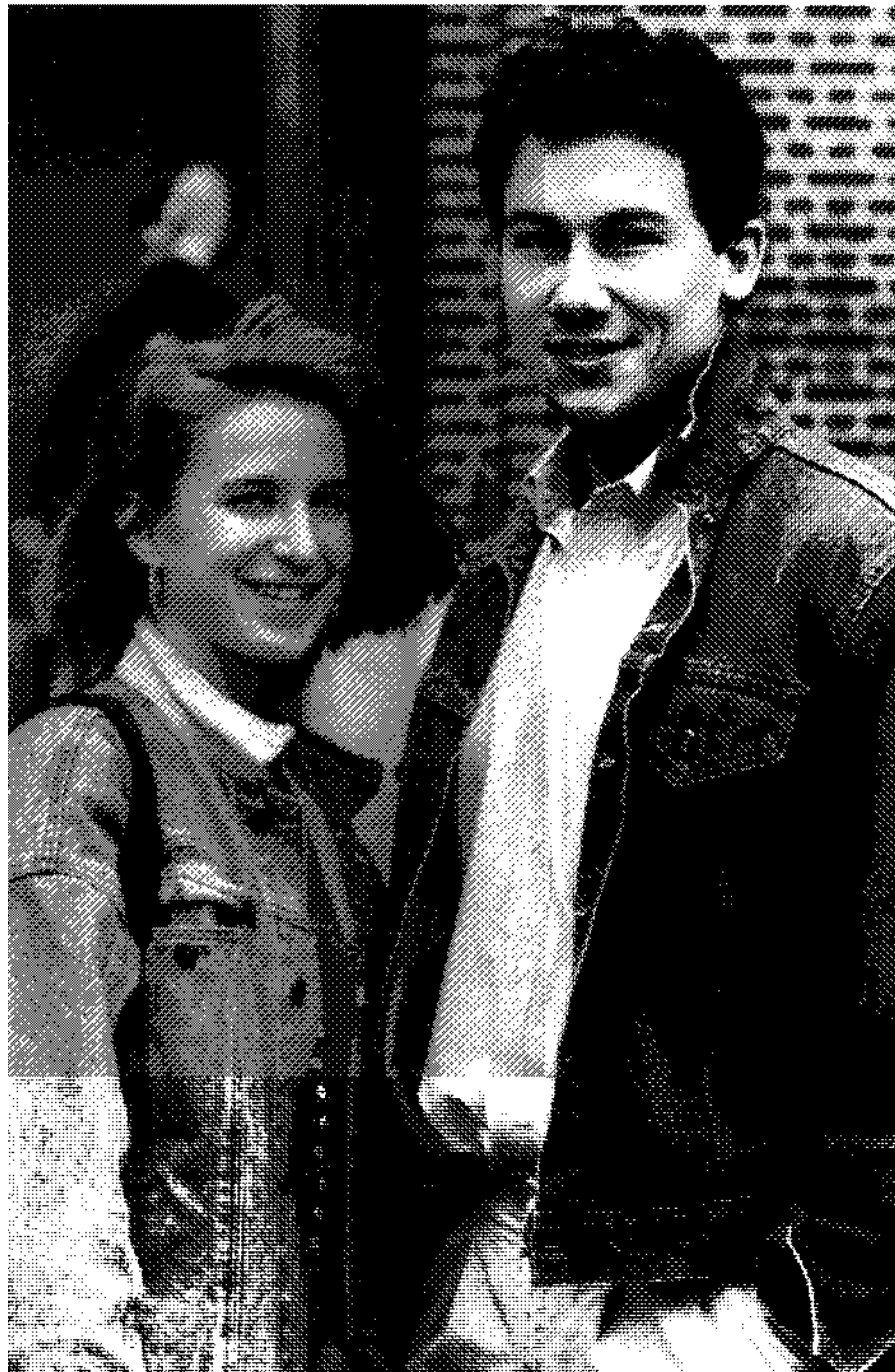
Joni and Andrew Wilkinson, recipients of the 1987-88 Pillsbury Scholarship, met when both were undergraduates at the University of Illinois, where he was studying chemical engineering and she was a marketing business major. After graduation they got married and went to Indianapolis, where both worked for Vonneget Industrial Products, she as a buyer and he as an outside sales specialist. Ever since then, they have been able to thrive as a dual career couple.

When they arrived at Michigan, each of them was able to get a research assistantship. He worked in finance and she in marketing, and they both landed summer internships at Pfizer Inc. in New York City, where Andrew did a financial analysis on possible new plant sites for the corporate finance department, and Joni did a market penetration analysis, sales forecasts, and budget preparation for the Quigley Division.

In the fall semester of 1987, Andrew and Joni participated in an international business student exchange at Erasmus University in Rotterdam, The Netherlands. There again, each had an internship. Joni worked as a student management consultant to Jonker Fris, a subsidiary of Sara Lee in Heusden, and Andrew conducted research on foreign exchange markets as a research analyst for the Rodevi Holding B.V. in Amsterdam.

After such a good track record, the Wilkinsons found themselves up against a tough problem this spring when both received their MBAs. His preferred job was in Chicago, while hers turned out to be in Detroit. What to do? "We finally decided that the only fair way we could decide," says Andrew, "was to put the names in a hat and draw." That's what they finally did, and Joni won. She is now a Product Planner in the Truck Division at Ford Motor Company, and Andrew is considering several job offers in the Detroit area.

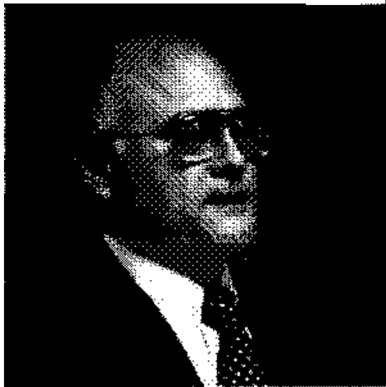
The Wilkinsons are quick to express their gratitude for the Pillsbury Scholarship. "Without it," they say, "we would have had to go to a cheaper and not as well recognized School. Pillsbury made Michigan possible for us."



Joni and Andrew Wilkinson, recipients of the 1987-88 Pillsbury Scholarship, have thrived as a dual career couple, but had to draw names from a hat to make a geographical decision when his preferred job opportunity turned out to be in Chicago, while hers was in Detroit.

Introducing the William A

Julius A. Otten
Peat Marwick Main & Co.



Charles A. Hoffman
Icerman, Johnson & Hoffman (retired)

Paul Yhouse
Arthur Andersen & Co.

Timothy R. Cash
Ernst & Whinney

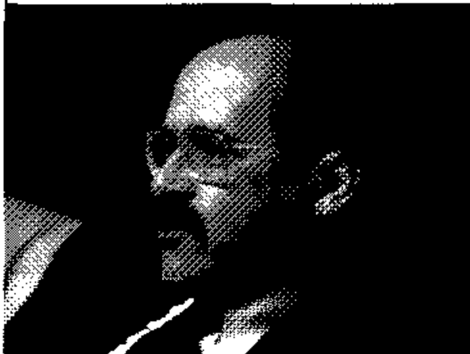
Members of the Advisory Board of the William A. Paton Fund for Accounting Scholarships, Fellowships, and Loans come to campus once a year to give help and advice in administering the fund. The last time they were here, *Dividend* took pictures at the meeting so that we could introduce the board members to you on these pages.

The Paton Fund awards annual scholarships to doctoral students planning a career in accounting teaching and research. The awards are dedicated to raising the standards of accounting instruction and research in colleges and universities. They help to bridge the gap between the remuneration of private practice and the cost of an advanced accounting degree.

One of the great tributes to Professor Paton as a teacher is the number of his doctoral students and long-time faculty colleagues who themselves have contributed to accounting education. At last count, four were awarded Outstanding Educator Awards from the American Accounting Association and eleven have served as president of the AAA. Many others have made their mark as scholars, teachers, and professional accountants. The William A. Paton Fund for Accounting Scholarships and Fellowships is dedicated to maintaining the profound impact that Professor Paton has had on the accounting profession.

Paton Fund Advisory Board

Maurice S. Hahn
Coopers and Lybrand (retiml)



William Mair
Third National Corporation

Carleton Griffin
Professor of Accounting

John J. Ifeager
Arthur Young & Company

Raymond C. Maihofer
Maifiofer, Moore & Debug (retired)

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Photos by Dean Russell

^4n *informal collection of items, including news of the faculty, of alumni, and of the school, and assorted other information, opinion or comment that we think will interest you,*

Milton and Josephine Kendrick Establish Award for Theory Development in Marketing

An award to enrich the doctoral program in marketing at the Business School has been established by Milton and Josephine Kendrick.

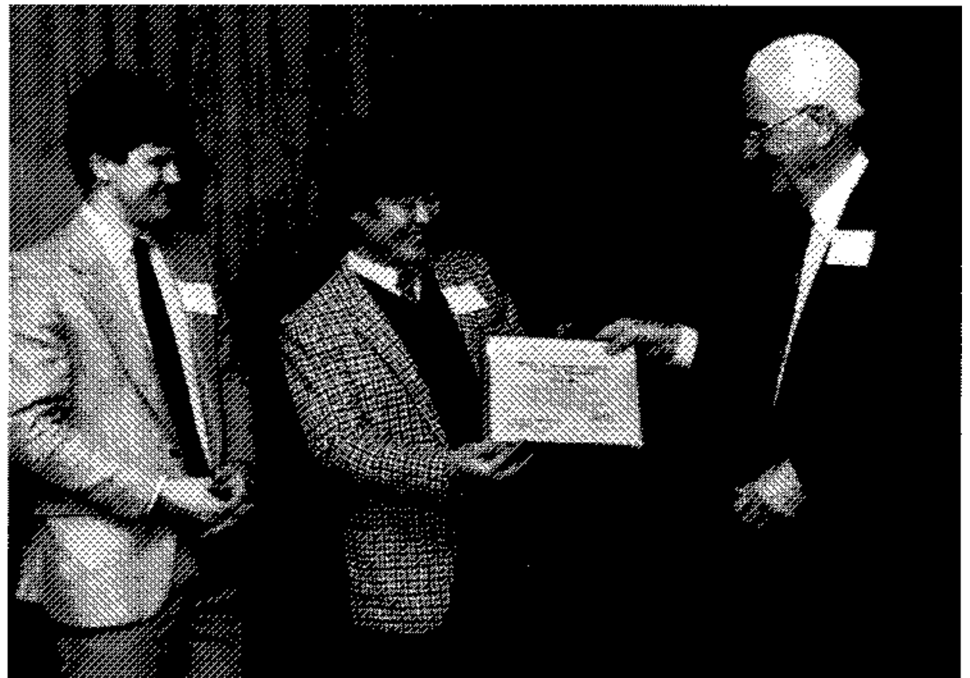
The award was established to recognize the importance of theoretical scholarly work among doctoral students in marketing. Second- and third-year Ph.D. students are eligible for the competition, which involves writing a paper on a substantive marketing topic with a strong theoretical basis. This year, the award was given to doctoral students Byong-Duk Rhee and Michael Guolla.

Mr. Rhee, who has his MBA degree from Yonsei University in Seoul, Korea, has several research interests, including mathematical modeling of consumers'judgment and choice. His work focuses on business competition and consumer welfare in marketing and on new product development.

Michael Guolla, who has his MBA from the University of Western Ontario, is currently doing research in marketing strategy with particular emphasis on industrial marketing and sales force strategy.

Mr. Kendrick, who graduated from The University of Michigan in 1929, had a distinguished career with Michigan Consolidated Gas Company before he retired in 1970. He received the U-M's Distinguished Alumni Service Award in 1961. He was national chairman of the U-M Alumni Fund in 1963-64; chairman of the "Select Gifts" project in the University of Michigan's $55 million program in 1965, and has a long list of community agencies for which he has been a valued volunteer. In 1986 and '87, he received the Volunteer Service Award of the Washtenaw United Way.

D. C. GOINGS



Milton Kendrick (right) presents the newly-created Milton and Josephine Kendrick Award for theory development in marketing to doctoral students Byong-Duk Rhee (center) and Michael Guolla.

Business School Growth Fund Established by Our Alumni

A special investment fund, managed by our alumni, has been created for the benefit of the Business School. Approval to establish the fund was granted by the Regents at their February meeting.

The fund will seek long-term growth of capital through a diversified portfolio consisting mainly of securities of developing companies with long-range potential.

"During the capital campaign," explained Dean Gilbert R. Whitaker, Jr., some of our alumni expressed a desire to contribute funds, but felt that if they managed the funds they could do a better job and take a more aggressive stance. The Stanford Business School Trust, which we used as a model, has been fairly aggressive and has grown from $70,000 to $9 million in twenty years.

"We don't see the fund as growing rapidly," Whitaker added. "For the first 10 years, we'll probably reinvest any proceeds to build a bigger base."

The fund will be managed by a nine- to 15-member board of trustees, recommended to the president by the Business School dean and the University's vice president and chief financial officer, and approved by the Regents. Board membership will include the dean and the University investment officer.

Trustees will be responsible for soliciting contributions for the fund, recommending fund investment policy and guidelines to the Regents, reviewing activities of the fund's investment managers and providing consultation on the timing and recommended distributions from the fund.

Day-to-day investment decisions and implementation of the fund's investment policy and guidelines will be the responsibility of five alumni investment managers. Like the trustees, they will be recommended to the president by the dean and vice president and must be approved by the Regents.

Investments by the fund will be subject to regental approval and will follow the University's policy on investments in companies doing business in South Africa.

The Regents also stipulated that no other funds of this nature can be established until there has been an opportunity for evaluation of the Business School fund.

Those interested in further information about the Fund should get in touch with Frank Wilhelme, director of development at the Business School, Room 2215 — Telephone (313) 763-5775.

How is Technology Best Transformed into Products and Services: A Colloquium

How are technological innovations best transformed into products and services? Why are some organizations better at this than others? A colloquium series expanding on these questions is being sponsored this spring by the Cognitive Science and Machine Intelligence Laboratory, which has its headquarters at the Business School.

The colloquia are a follow-up to a major symposium which was held last fall on the Commercialization of High Technology. The symposium and the colloquia will form the basis of a book on this topic.

Talks given in the colloquia series included: "Technological Discontinuity, Organizational Evolution and Executive Succession: Mini-Computer Industry as a Case in Point" by Michael Tushman of Columbia University; "Capture Value from Technological Innovation" by David Teece of the University of California at Berkeley; and "Product Development in the World Auto Industry" by Kim Clark of Harvard University.

Other talks given in the colloquia series included "The Evolution of Standards and Its Competitive Consequences in High-Tech Industries" by C. K. Prahalad, professor of corporate strategy and international business at the Business School; and "The Influence of Buyer-Seller Relationships on the Adoption of New Industrial Products: A Decision-Based Perspective" by Roger More of the University of Western Ontario.

June Osborn Discusses the Politics and Science of AIDS as the 21st Mclnally Lecturer

The AIDS epidemic continues to engender controversy, from the Masters and Johnson claim that the virus is "running rampant" to the Moral Majority's objection to civil rights legislation which they claim would force institutions to hire AIDS victims.

June E. Osborn, dean of the University of Michigan School of Public Health and a national authority on acquired immune deficiency syndrome, spoke on the need for an AIDS policy in business and government, April 5, in Hale Auditorium. Her speech, "The AIDS Epidemic: Politics and Science," was the 21st annual William K. Mclnally Memorial Lecture.

Dr. Osborn addressed the way in which scientific information can allow the nation to create a sound AIDS policy in both government and business. Ignoring the epidemic, she said, will result in "enormous societal costs in terms of unwarranted panic and abuse of infected individuals."

Dr. Osborn became dean of the U-M School of Public Health in 1984. She was elected a member of the Institute of Medicine of the National Academy of Sciences in 1986, has served in a number of advisory roles concerning the AIDS epidemic to federal agencies, private foundations, and the World Health Organization, and was a member of the National Academy of Sciences/Institute of Medicine Task Force on AIDS in 1986.

The Mclnally lectures began in 1966 to honor the memory of U-M Regent William K. Mclnally.

The five winners of this year's Unisys MBA scholarships are pictured above. They are (seated left to right) John J. Mannebach, Jeffrey S Miller, Edwin L. Miller, associate deanfor research, and Ann J. Williamson. Standing, left to right, are Samuel K. Miller James A. Veraldi, and Richard Bierly, Unisys senior vice president for human resources.

Unisys Continues Its Scholarship Support to the Business School

The Unisys Corporation has given five MBA students one-year scholarships of $5,000 each this year. The scholarships are part of a $250,000 grant from the corporation for master's and doctoral students in the Business School and the College of Engineering.

Three doctoral fellowships, each $25,000 a year for three years, have been given to students pursuing academic careers. Two of those went to Business School doctoral students and one to engineering.

This is the third consecutive year Unisys has made scholarship donations to the U-M as part of its corporate educational relations program. In addition, Unisys and the Business School have an ongoing multimillion dollar cooperative program to study methods of integrating computing into business education.

Ferocious Global Competition in the Auto Industry is the Topic of U-M Conference

"The Auto Industry Ahead: Who's Driving?" was the title of the eighth International Automotive Industry Conference at the U-M in March. The conference was jointly sponsored by the Business School, the Center for Japanese Studies, the Office of the Study of Automotive Transportation, and the Industrial Development Division.

With Asian manufacturers building cars in the U.S. and new competitors from Malaysia, Yugoslavia, and elsewhere setting their sights on the American market, global competition in the industry- is far more ferocious than it was in 1980, according to Peter J. Arnesen, director of the East Asia Business Program and the conference director.

In past years, the conference addressed the competition between the American and Japanese auto industry. Changing the focus to the international auto industry reflects the dramatic changes that have overtaken the field in the 1980s.

The dollar's decline and the Big Three automakers' search for cheaper sources of supplies have also caused upheavals in the American automotive industry, says Arnesen.

The conference consisted of a general forum March 22, followed by specialized workshops March 23 in the Michigan League.

The conference began with a panel discussion on foreign investment in the American automotive industry. The panel was led by Martin Zimmerman, chief economist at Ford Motor Company (and now on leave from the Business School, where he is associate professor of business economics).

Addressing the forum on various aspects of competition were Osainu Nobuto, president of Mazda Manufacturing (USA) Corporation; C. K. Prahalad, professor of

corporate strategy and international business at the Business School; Christopher J. Steffen, executive vice president for finance at Chrysler Motors Corp.;
J. D. Power, president of the automotive research firm J. D. Power and Associates; and David I. Verway, director of the Bureau of Business Research at Wayne State University.

Eleven specialized three-hour workshops were held the following day, and covered such topics as the impact of Mazda's new assembly plant in Flat Rock, Mich., challenges facing small suppliers in the auto industry, labor relations in the late 1980s, new developments in the East Asian auto industry, and the role of the "prestige" vehicle.

When an Organization is Not Growing, It is More at Risk Than You Think

Administrators should expect serious problems and low morale to develop whenever an organization is not growing, according to research done by Kim S. Cameron, associate professor of organizational behavior and industrial relations.

Cameron says that he was very surprised at the results of his research: "We had expected to find major distinctions between colleges that were suffering from budget cutbacks and shrinking student bodies and those that were holding their own. Instead, we found that both kinds of schools had many similar negative attributes."

Cameron says that both stable and declining schools tend to ignore long-range planning, make across-the-board rather than selective budget cuts, blame their leaders, resist change, and are fragmented and politicized.

"Stability is a form of stagnation," Cameron explains. "When revenues aren't rising, there are few pay raises. Research opportunities are restricted, and conflicts arise over the resources that are available. The upshot is that administration and faculty begin to operate the same way they would during a decline.

"These responses are dysfunctional," he adds. "They are just the opposite of what organizations should do if they expect to thrive or grow."

Cameron also reports that upper-echelon administrators experience the impact of a decline differently than lower-level workers.

"Top managers are most affected by the turbulence at the onset of decline," he says. "The rapid changes create an environment of uncertainty, so decision-makers fall into a threat-rigidity response." As a result, he says, managers centralize the decision-making process, replace long-term planning with crisis management, and make across-the-board cuts rather than selective cuts in the budget to reduce conflicts between groups. They also start looking for new jobs at this point.

Lower-level employees bear the brunt of the full decline. When that time comes, Cameron says, they turn administrators into scapegoats, resist change, fail to be innovative, and fall into conflict with each other over the scarce resources that are left.

"Our study makes it clear that the decision-makers at colleges must take corrective action earlier in the down-cycle than we previously believed," Cameron concludes. "Indeed, the dysfunctional behavior we assumed to be the consequence of decline is actually the consequence of non-growth. Decrease in the rate of growth rather than the decline is the real point of risk.

Cameron studied data gathered between 1977 and 1982 from college presidents, academic officers, financial officers, department chairmen, and trustees at 334 four-year colleges of various sizes throughout the United States. Nearly 40 percent were public schools and about 60 percent were private. About 15 persons at each school participated in the study.

Professor George Siedel Says "Minitrial" Mediation Offers a Faster and Cheaper Way to Settle Disputes

Executives, with a little help, can arrive at legal as well as business solutions, says George Siedel III, professor of business law, in a paper examining the intersection between business and legal approaches to dispute resolution.

By using day-to-day experience in informal conflict resolution, managers often can play key roles in out-of-court settlements, says Siedel. Mediation, in which a third party helps disputing parties reach an agreement, is especially effective.

"For example, the 'minitrial,' a form of mediation first used in 1979, offers an opportunity to use creative problem-solving and negotiations in shaping a 'win-win' resolution of a dispute," he says, "as opposed to the 'all or nothing' solutions often rendered in litigation."

Siedel estimates that the cost of a minitrial is about ten percent of the cost of a civil lawsuit, and also cheaper than arbitration, in which a third party issues a binding decision. "To arbitrate a $1 million international dispute costs about $120,000, not counting legal fees," he says.

In a "minitrial," lawyers act mainly as advisers while the managers themselves are the primary negotiators. Despite its name, the minitrial is not a trial, but an information exchange, Siedel explains. It may involve a neutral adviser and may be held under court supervision, but it requires neither.

"The key factor that distinguishes the minitrial from a real trial is that it allows face-to-face contact between executives, while the lawyers remain in the background," Siedel says.

The original minitrial, described in Seidel's paper, was between Los Angeles-based Telecredit, Inc. and TRW Inc. In 1974, Telecredit sued TRW for patent infringement, seeking an injunction and $6 million in damages. "After three years had

passed and 100,000 documents had exchanged hands, no agreement had been reached," Siedel says.

At that point, the parties began to develop a procedure they called an "information exchange," now known as the minimal. After each side had disclosed facts and documents relevant to the dispute, attorneys presented their best cases in a four-hour period. A neutral party moderated a short reply and rebuttal session. The executives then met for thirty minutes and quickly reached an agreement, "thus saving an estimated $1 million in lawyer's fees," according to Siedel.

Since the TRW-Telecredit precedent, minitrials have been used in more than 100 cases, he adds, and probably could have worked for many more, had executives been aware of the advantages of the procedure. Siedel predicts that minitrials will soon be used for other types of cases such as those involving claims of wrongful discharge and product liability.

Rent-a-Judge

New versions of arbitration also are growing in popularity. (Arbitration requires a third party to receive pertinent information and arguments from two contending parties and to render a binding decision.) Some, such as the "rent-a-judge" system, also have gained some notoriety as a form of "rich man's justice," Siedel notes.

To rent a judge, contending parties agree upon and hire a retired judge, usually with special expertise in the area of the dispute.

People like television talk show host Johnny Carson, who rented a judge to settle his contract dispute with NBC, have found that the procedure helps them keep cases low-key and relatively free of publicity, Siedel says. "Hiring a private judge also speeds up the process, as the parties don't have to wait months to get on the crowded court docket."

The rent-a-judge system is different from some other forms of arbitration in that rules of evidence may apply to the proceeding and the judge's decision may be appealed on the basis of errors of law.

The trend toward out-of-court settlements reflects "people's desire for certainty about the outcome of a case," Siedel says. "I equate litigation with roulette because the outcome often depends on the jury members. In out-of-court settlements — especially those resolved through mediation — the parties have much greater control over the resolution process as well as the result."

When the rented judge, the minitrial and their many variations do not produce a satisfactory settlement, businesses can, of course, resort to litigation. But the alternatives — especially new forms of mediation — are worth trying first, since they allow the parties so much more control over the negotiations and settlement.

Are You Moving to a New City? A New Country? Global Blue! Contacts Are Ready to Help.

In 25 states, 12 foreign countries, the District of Columbia, and Puerto Rico, you have a friend! Over 250 graduates from the classes of 1985 and since are ready and willing to answer your questions about where to live, where to eat, where to unwind, and where to meet with other Michigan fans to watch a UM football game!

Below is a list of all the states and countries with Global Blue! contacts. Call the Alumni Relations Office at 313-763-5775 to get the names and numbers of the contacts in your area.

Arizona
California
Colorado
Connecticut
District of Columbia
Florida
Georgia
Hawaii
Illinois
Indiana
Louisiana
Maryland
Massachusetts
Michigan
Minnesota
Missouri
New Hampshire
New Jersey
New York
North Carolina
Ohio
Pennsylvania
Tennessee
Texas
Virginia
Wisconsin

Argentina
Canada
Denmark
Finland
France
Hong Kong
Japan
Korea
Nigeria
Puerto Rico
Spain
Taiwan
United Kingdom

Class Notes

'34 Bruce S. Shannon, MBA '34, has been appointed chairman of the financial advisory committee of the Community Foundation of Collair Co. in Naples, Florida. Bruce retired in 1966 from the Drackett Company of Cincinnati, Ohio, where he was financial vice president.

'42 I. D'Arcy Brent, MBA '42, is president of High Technology Leadership, Inc., which is a management consulting business. He writes that he has lived and worked all over the U.S. and Western Europe. From 1950-61 he was a science and technical executive with the CIA, and during that time spent three years in disarmament negotiations. He attended the Advanced Management Program at Harvard Business School in 1960. From 1962 to 1986 he was vice president and general manager of the Government Systems Division and the Spectrochemical Products Division of Baird Corporation. He now lives in Carlisle, Mass.

Gordon H. Buter, MBA '42, writes that he retired as chairman of the board from Zondervan Corporation in 1982. Prior to that time he served in the U.S. Army as captain; taught at Calvin College from 1946 to 1956; and worked for Associated Truck Lines from 1956-82, serving as president and chairman of the board. Gordon and his wife, Rose, live in Grand Rapids, Michigan, and have five children: Tom, Barbara, David, Joan, and Jack.

John A. Damgaard, Jr., MBA '42, writes that he is now retired after 34 years of university teaching. He spent 20 years on the faculty of the University of Northern Colorado, and also taught at the University of New Mexico, College of Southern Utah, and was principal of the Utah State Industrial School. He and his wife, Thelma, are living in Sun City, Arizona. They have a son, John III.

John H. Harwood, MBA '42, is now retired from A. G. Edwards & Sons, Inc., St. Louis, Missouri, where he served as their vice president. Jack has 32 years in the metals industry, including service as a personnel director, corporate secretary, corporate financial officer, and director. He has 10 years experience as a financial consultant and investment banker, specializing in business valuation. Jack says that his U of M education stood up well over the years, "especially," he says, "when I consider how rapidly and significantly many things have changed." Jack and his wife, Betty Ann, live in Sarasota, Florida. They have four sons: John, Nevin, James, and Christopher; 10 grandchildren, and 2 great grandchildren.

Hugh L. Head, Jr., MBA '42, has retired from J. J. B. Hilliard, W. L. Lyons, Inc., of Cincinnati, Ohio, an investment company. Hugh and his wife, Patricia, live in Ft. Thomas, Kentucky, and have four children: Hugh III, Amy, James, and William.

Alfred T. Joldersma, MBA '42, is now retired from Hubbell, Inc., an electrical equipment firm in Orange, Connecticut, where he was senior vice president of finance. Alfred started out in public accounting and then decided to go into industry. He joined a firm in Detroit in 1943 and was made treasurer in 1948. From 1956-62, he worked for Kawneer Company of Niles, Michigan, and became vice president of finance before moving to Hubbell, Inc. in 1962. Alfred and his wife, Grace, live in Sarasota, Florida, and have three children: Diane, Tom, and Jane.

Robert E. Johnson, MBA '42, retired in 1987 from Metra Tool Company of Livonia, Michigan, a company he owned. Robert and his wife, Peggy, live in Boynton Beach, Florida, and have two children: Barbara and Julie.

William M. Kramer, MBA '42, retired in 1986 from Kramer, Smith & Bish (CPA) where he was a partner. After serving in the army air corps during World War II, he became a partner in a family retail fur business from 1945 to '59, and from 1960 to 1986, served in public accounting. Bill was also treasurer and co-founder of Fairview Casting Company (Grey Iron Foundry Job Shop) of Fairview, Pennsylvania, from 1964 to 1987. He and his wife, Ruth, live in Erie, Pennsylvania, and have one daughter, Susan.

Charles H. LeClaire, MBA '42, retired in 1981 from A. O. Smith Corporation where he was vice president of employee relations. He and his wife, Betty, have six children and nine grandchildren. He served 21 years in the U.S. Marine Corps, and 20 years as an officer in a major manufacturing corporation. Charles and Betty live in Elm Grove, Wisconsin.

Frederick K. Rabel, MBA '42, is retired from the U.S. General Accounting Office in Washington, D.C. Before joining the GAO, he worked for Arthur Andersen & Company in Chicago, and Peat, Marwick, Mitchell in Chicago. Since retiring he is doing voluntary auditing and financial work. Fred and his wife, Harriet, live in Bethesda, Maryland and have two daughters, Alice and Carol.

Doyle W. Selden, MBA '42, retired in 1986 from McDonnell-Douglas Astronautics Company, Huntington Beach, California. He served as their director of material and then as senior staff manager. After graduation from Business School, he worked for General Motors, spent 20 years in the Navy, and then went to McDonnell-Douglas. He also taught a material management course part time for 12 years at St. Louis University. He writes that he is now president of the U of M Alumni Club in Leisure World, Laguna Hills, California where he and his wife, Ruth, are now living.

John P. Strouss, MBA '42, has retired as general sales manager of Dow Chemical Company in Southfield, Michigan. From 1942 to 1947 John served in the supply corps of the United States Navy where he retired as lieutenant commander. From 1947 to 1984, he worked for Dow Chemical Company in various marketing and management positions in Midland, Washington, D.C., New York City, Hong Kong, and Detroit. He and his wife, Moni, live in Ann Arbor, and have four sons: John, Jeffrey, Mark, and James.

EUGENE C. YEHLE, MBA '42, has retired as director of investor relations and pension investments of the Dow Chemical Company, Midland, Michigan. Before joining Dow, he was professor of statistics at the Michigan Business School. He has served as a member of the board of trustees of Alma College, chairman of the Charles J. Strosacker Foundation, and serves on various committees at the Midland Center for the Arts, Inc., and Memorial Presbyterian Church. Gene and his wife, Mildred, live in Midland, Michigan, and have three children: Richard, Janet, and Donald.

GERALD M. WATER, MBA '42, has retired from accounting, public and private. He and his wife, Olivia, are living in Fort Myers, Florida.

ROBERT C. ZWINCK, MBA '42, retired from Ervin Industries, Inc., Ann Arbor, in 1982. He and his wife, Marian, live in Whitmore Lake, Michigan, and have two sons: Robert and C. Edward.

'48 JAMES NORDLIE, BBA '48, president of Nordlie, Inc. has received the LTK Distinguished Service Award given in March, 1988 for "long-term contribution to the floral industry, integrity, fairness, perseverance, and decisiveness." Jim joined the floral industry in 1948, and his company has grown from 12 employees to a business that includes wholesale houses in Michigan, Ohio, and Florida plus rose farms in Ohio and Guatemala. He has been active nationally in his field, and has served on the boards of SAF, WF&FSA, Michigan State Florists, and Roses Inc. He lives in Birmingham, Mich.

JOSEPH H. BASSETT, BBA '47, MBA '48, started out in the banking business, and after a few years decided that was not his calling and hooked up with an entrepreneur. For 35 years he worked with Ebbert Engineering Company, a design and manufacturing firm in Troy, Mich. where he is presently administrative manager-treasurer. Joseph and his wife, Luella, live in Royal Oak, and have two children: Lawrence and Cynthia.

MAURICE F. GARTNER, JR., BBA '47, MBA '48, writes that he retired as manufacturing controller, construction equipment group of International Harvester (now Navistar International) after working there for 32 years in various management positions. For the last five of those years he had jurisdiction over nine plants located in North America, England, France and Germany. Maurice and his wife, Marjorie, live in Downers Grove, Illinois, and have four children: Karen, Robert, Glen, and Susan.

MARTIN J. KABCENELL, MBA '48, is vice president-secretary at the Novo Corporation, a holding company in Scarsdale, New York. Martin and his wife Pauline live in Ridgefield, Connecticut, and have three children: Dirk, Andrea, and James.

PAUL C. STAAKE, JR., BBA '47, MBA '48, writes that after 37 years he retired in 1985 as senior vice president of Babson College, Babson Park, Massachusetts. He now travels and does alumni work. Paul and his wife, Margaret, spend their winters in Florida and summers in Maine.

'52 DAVE FREEMAN, BBA '52, writes that his active representation of public sector and private sector management in labor and employee disputes and contract negotiations ended in 1980 when he returned to the academic world. He explains that he had been associate dean of the Stanford University Law School for many years in the late '50s and early '60s, before devoting 10 years to work in Washington, D.C. as an appointee in the Kennedy and Nixon administrations and as a consultant to local governments. In 1980-81 he was vice president of a small private college in Orange, California, and then moved on to a visiting professorship at the Willamette College of Law in Salem, Oregon, and from there to a professorship at McGeorge Law School at the University of the Pacific in Sacramento, California.

'57 JAMES B. RUPPRECHT, BBA '57, is corporate services officer of Great Lakes Bancorp in Saginaw, Michigan. James and his wife, Nancy, live in Saginaw, Michigan, and have two sons: James and Geoffrey.

RICHARD H. SCHACHT, MBA '57, is general manager with James River Corporation, Norwalk, Connecticut, a paper products company. Richard writes that he was with Procter & Gamble, Cincinnati, Ohio from 1958-69; Great Western United, Denver, Colorado, from 1969-73; Martin Brower Corporation, Chicago, Illinois, from 1973-78, and then in 1978 joined American Can Company, which was purchased by the James River Corporation.

EDWARD J. SHANNON, BBA '57, is president of Shannon Lumber Company, Chicago, Illinois. Edward writes that he and his wife, Joan, live in River Forest, Illinois, and have four children: Edward, John, Brigit, and Jane.

FRED SCHATZ, BBA '57, is director of human resources of the First National Trading Corporation, Southfield, Michigan, which is a commodity brokerage firm. Fred is active in the U of M Club of Detroit, and is national vice president (and president-elect) of Zeta Beta Tau fraternity. He and his wife, Susan, live in West Bloomfield, Michigan, and have three children: Michael, Lisa, and Richard.

NEILL R. SCHMEICHEL, BBA '56, MBA '57, spent 25 years as partner with Ernst and Whinney, 2 years with a start up venture in telecommunications, and 3 years with CEO-CFO Associates, a company in Ann Arbor of which he is president. Neill and his wife Joan live in Ann Arbor.

JAMES E. SEITZ, MBA '57, is vice chairman and associate managing partner of the southwest region of Touche Ross & Company, a public accounting firm, in Los Angeles, California. He and his wife, Dolores, live in Los Angeles, California, and have two sons, David and Donald.

DONALD L. SHUMAKER, BBA '54, MBA '57, has retired from his position of director of compensation and employee benefits with Aerospace Corporation after 23 years of service. Donald is living in Redondo Beach, California.

LLOYD D. SLAGHT, BBA '57, has been in the personnel field for the entire time since graduating from the University of Michigan, with the exception of one year with Coldwell Banker in residential home sales. He worked for Consumers Power for 10 years, in the hospital field for 10 years, and in industry 10 years. At present he is the personnel director at Tasty Frozen Products of Lenexa, Kansas. Lloyd and his wife, Joan, live in Independence, Missouri.

GERALD A. SOLOMON, BBA '57, is vice president of Imperial Bag and Paper Company, Inc. of Bronx, New York.

NORTON A. STUART, JR., BBA '57, is president and COO of Banc Tec, Inc., of Dallas, Texas, a business equipment manufacturer.

EARL SUNDERHAUS, MBA '57, is an ophthalmologist and has a practice in Asheville, North Carolina.

JOHN THIEME THOMAS, BBA '57, MBA '58, writes that from 1958-63 he worked for Procter and Gamble; 1964-73 Glendinning Associates; 1974-76 Ero Industries; since 1977 he has been with

John W Lawrence, MBA '50, Gives Students Tips on Pitfalls that Await Entrepreneurs

John W. Lawrence, MBA '50, is no stranger to Murphy's Law. The axiom, which claims that in any situation anything that can go wrong will, seemed to be the guiding principle when Lawrence and a group of investors formed a corporation back in 1968 to run southwestern Michigan's first UHF television station.

The venture, which he described to a group of MBA students at a recent Dean's Seminar, is only one of a number of enterprises in which Lawrence has a hand. He is presently founder and CEO of MCE, Inc., of Kalamazoo, which develops educational software; founder and CEO of Lawrence Productions, Inc., a film and video tape production company; secretary-treasurer of Superior Pine Products Company, a timber company with headquarters in Fargo, Georgia; and president and CEO of Channel 41, Inc., of Battle Creek, Mich. From 1958 until 1985, he served as CEO of Illinois Envelope Company.

The story of Channel 41, he said, is the story of a "fantastic business failure that we managed to pull up by its bootstraps." He told the students that his talk, which he titled, "So You Want to Be in Television ... (or How Not to Go into a Second Business)," was an example of what they should avoid if they decide to become entrepreneurs.

He had specific bits of advice for the students who might someday consider an entrepreneurial venture: no matter how well you think you have planned, you always will underestimate the need for cash; if you do not fund for all the things that can go wrong, you may lose everything, including your life savings; be prepared for times when you will seriously question your sanity for getting involved in the project in the first place.

Lawrence said the television industry had always interested him, ever since he saw his first TV show — Howdy Doody — in the basement of the Michigan Union, while he was a student at Michigan. So, in 1968, when a promoter came along selling a proposal for Michigan's first UHF television station, Lawrence and 16 other investors responded and formed a corporation to run the station.

Getting a broadcast license from the Federal Communications Commission was the first time-consuming obstacle to overcome. Then the planned site for the transmitting antenna had to be abandoned because it was near a new airport and the antenna was too tall for the airspace.

Finally, the station went on the air in July 1972. "Then everything started going wrong," said Lawrence. Slides of advertisers' products were shown upside down the first day of broadcasting. The signal was hard to pick up, so viewership was sparse. Furthermore, a March ice storm brought a lightning strike which hit the antenna and destroyed its capacity to transmit. Of course, the company that made the antenna had gone out of business, and it took until the following November to get a new one.

On top of these problems, it turned out that the promoter, who had become general manager, had no qualifications for the job. That resulted in serious personnel conflicts among the staff and a suspension of board of directors' meetings for several months.

The general manager was fired at about the same time that the antenna went. Lawrence was then named president, and he remembers "the station was losing money like crazy."

Lawrence said that 1973 was the station's first real year of operation, and it proceeded to lose money for several years thereafter. One of the stockholders did the station's accounting, using his own system, similar to what he used for his lumber business. There was one line on the budget for all of the station's equipment.

By 1974, the original investors, who were tired of putting more and more money into the station, pulled out. But while the station lost credibility with the advertisers and viewers, the sales staff remained loyal, and Lawrence credited marketing as the biggest factor in the station's ultimate success.

In 1978, Channel 41 saw its first profits.

"It was not what we had dreamed of, but we had turned the corner," Lawrence told the students. "This business would have submerged if we had not been so persistent. By 1982, it was worth enough so that if we had wanted to sell it, we would have turned a profit."

By Kathy Hulik

executive search firms, including Lamalie Associates, Inc. and Wilkins 8c Thomas, Inc. He is now a partner with Ward Howell International, Inc., Chicago, Illinois. He organized in 1958 and continues to head the Procter & Gamble Marketing Alumni Association, a national group of over 1,000 business executives who once were marketing managers at P&G.

DON K. VANCE, BBA '57, MBA '58, is a management consultant with Vance Associates, Darien, Connecticut, a food marketing and manufacturing firm.

ROBERT A. WEIMER, MBA '57, writes that he is now? manager of the National Capital Reinsurance Company, Inc., of Washington, D.C. He says he has enjoyed an actuarial career with three life insurance companies, specializing in group life and health coverages. He joined National Capital Reinsurance Company in July, 1987. It is a newly formed subsidiary of Blue Cross and Blue Shield of Washington, D.C, and is licensed in Barbados. Its main function is to support the international marketing efforts of BCBS NCA.

he chose the telephone industry because it was stable. He says, "Ten moves and deregulation later, I'm still in it."

EDWIN H. SCHRADER, JR., MBA '67, is president of Schrader Funeral Home, Inc., and also owner/operator of Colonial Monument Company, Plymouth, Michigan. Win served in Viet Nam from 1968 to 1970. Win and his wife, Susan, live in Plymouth, Michigan, and have a daughter, Sarah.

JAMES H. SEASON, MBA '67, writes that he is group vice president of Golodetz Trading Corporation of New York City, New York. James has also served as director of Memtech Technology Corporation, Folsom, California; director of American Homestead, Inc., Mt. Laurel, New Jersey; executive vice president/chief financial officer of MGC Leasing Corporation, New York City; and president of Compass Capital Corporation, New York City, NASD member.

JOHN SMARTT, MBA '67, writes that he is a partner with Price Waterhouse, San Antonio, Texas. He spent the last 20 years with Price Waterhouse in Nashville, Tennessee, and moved to San Antonio a year ago. John and his wife, Linda, have a daughter, Janet.

BARRY W. TIMM, MBA '67, writes that he is senior economics engineer with Phillips 66 Company in Sweeny, Texas. Barry has lived in the midwest, Virgin Islands, east coast, and Texas. He and his wife, Kristine, live in Lake Jackson, Texas, and have two children, Lynda and Bryan.

HARVEY S. TRAISON, MBA '67, is vice president/treasurer of Daimler-Benz of North America Holding Company, Inc., New York, New York. Harvey lives in New York City.

GERALD M. VAN VLIET, MBA '67, writes that he is department head of the transportation and distribution operations of Eli Lilly 8c Company, Indianapolis, Indiana.

ARNOLD VAN ZANTEN, MBA '67, is senior vice president at Coastal Corporation, Houston, Texas. He spent the first 10 years of his career working at Arthur Andersen; then took the information systems vice president position at Michigan Wisconsin Pipeline, a subsidiary of American National Resources, spending 10 years with them. After ANR was purchased by The Coastal Corporation, Arnold went with them. He is now in charge of the newly-formed

*Lawrence Goldstein, MBA *5<V, Finds Good Bargains Where Most Investors Fear to Tread*

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retail division which currently has 800 branded gas stations and convenience stores.

H. CURTIS WOOD III, MBA '67, is an operations analysis associate on the engineering staff at Ford Motor Company.

Lucius B. MCKELVY, BBA '67, is president of Synthe Cramer Company realtors in Cleveland, Ohio.

y £Z O ARTHUR L. SCHWARTZ, JR., UO BBA'67, MBA'68, is professor of finance and real estate at the University of South Florida in St. Petersburg. From 1968 to 1972 he was securities analyst with Prudential Insurance and a NYSE member firm; in 1973-75 he received his Ph.D. in finance from the University of Oregon; from 1975-80, he was professor of finance and real estate at California Polytechnic State University; in 1981-82 he was visiting professor of finance at the University of Hawaii, and in 1982 he joined the University of South Florida. Arthur lives in Tierra Verde, Florida.

J. D. WILLIAMSON II, BBA '67, MBA '68, is vice president/co-owner of WKBN, AM/FM/TV, in Youngstown, Ohio. He and his wife, Judy, live in Poland, Ohio, and have three children: John, Brad, and Sheri.

* P"7 "1 HAROLD I. ABRAMSON, BBA f A '71, associate professor at the Touro Law Center in Huntington, New York, has been appointed the law school's associate dean for academic affairs. Harold earned an MPA from John F. Kennedy School of Government at Harvard University and an LL.M. from Harvard. He and his wife, Margaret, reside in Huntington, New York, and have two children, Todd and Elizabeth.

THOMAS KURLAK, BBA '69, MBA '71, is a security analyst for Merrill Lynch in New York where he follows the electronics industry. He writes that in 1987 he was voted the number one analyst in his field by Institutional Investor Magazine's all American research team poll of institutional investors. He is a first vice president at Merrill Lynch, holds a CFA, and is a member of the New York Electro-Science Analyst Group and the Electronics Analyst Group, as well as the FAF and New York Society of Securities Analysts, where he serves on the program committee. He lives in Chatham, N.J. with his wife, Candy, daughter Hedy, and son Russell.

5 ^ 7 0 CLAIRE N. THAIN, MBA '72, • *mq* is president and publisher of *Entrepreneur Magazine* in Irvine, Calif.

RICHARD J. PASKY, MBA '72, is design engineer of truck axles at Ford Motor Company, Dearborn, Michigan. His first year after graduation was spent at White Motors, Cleveland, Ohio, and the remainder of his time has been spent in body engineering (instrument panels) and truck operations at Ford. He and his wife, Elaine, live in Willis, Michigan, and have two children, Sara and Michael.

RICHARD E. POSEY, MBA '72, writes that he has worked for Johnson Wax Limited since graduation, but that his career has been quite varied. He says he has lived twice overseas and has held a succession of increasingly responsible international and domestic management positions. After six years in the U.S. marketing department, he was appointed marketing director of Johnson's Italian company and lived six years with his family in Milan. Three general management positions followed: area director of Latin America; general manager of a U.S. Division and managing director of British Johnson. He was appointed an officer of the corporation in June, 1985, and lives with his family in Surrey, England.

LYN RUPPRECHT, BBA '72, is manager of general accounting/credit at Rockwell, International in Newport Beach, California.

GERALD SAJEWSKI, BBA '72, is a computer systems analyst for an agency in international development of the U.S. government. For the last 11 years he has worked in Washington, D.C. for the U.S. Department of Labor, the U.S. Department of Commerce, and currently the Agency for International Development. In 1982 he earned his MBA at George Washington University. He and his wife live in Arlington, Virginia.

JEFFREY B. SCANLAN, BBA '72, is a major projects procurement representative of Arco Petroleum Products Company in Los Angeles, California.

PIERRE SICE, MBA '72, is senior vice president of finance and chief financial officer with Dataline Service Company, Covina, California.

DOUGLAS SCHRANK, MBA '72, is senior vice president of Haagen Dazs Company, Inc. in Teaneck, New Jersey.

EDWARD W SMITH, MBA '72, writes that he worked several years in investment banking and financial consulting after getting his MBA. In 1975 he co-founded a machine tool remanufacturing business, became majority owner, and sold it in 1985. He says he is now semi-retired and owns and manages commercial property investments. He lives in Chagrin Falls, Ohio, and has two children, Maressa Ann and Brant.

CHARLES W. SNYDER, MBA '72, is managing principal and chief financial officer of Bechtel Investments, Inc., of San Francisco, California, and Sequoia Ventures, Inc., both separate affiliated companies of Bechtel Group, Inc. Charles joined Bechtel in 1973, and spent the next six years in finance working on worldwide project financing and investment activities. In 1979, he was named an executive assistant to S. V White, now president of Bechtel Investments, Inc.; in 1981 became deputy manager of Bechtel's Executive Office in Washington, D.C, and assumed his present position in 1982.

RICHARD L. STED, MBA '72, is now senior vice president and deputy general manager of the Chicago branch of Banque Nationale de Paris. He spent 12 years with Continental Illinois National Bank & Trust Company, which included four years in Tokyo and two years in Singapore and has lived in Chicago since 1980.

D. J. STORTEBOOM, MBA '72, is manager of computer integrated manufacturing at Ford Motor Company, Dearborn, Michigan.

LARRY J. SVOBODA, MBA '72, is vice president of finance and chief financial officer of the Florsheim Shoe Company in Chicago, Illinois. Larry worked for Arthur Andersen & Company from 1972-84, Sara Lee Corporation from 1984-87, and joined Florsheim in 1987.

JIM TOLONEN, MBA '72, serves as vice president of finance and chief financial officer with Excelan of San Jose, California, a computer/software firm dealing in local area networks. After Jim received his MBA, he worked for Arthur Andersen for four years and became a certified public accountant. He then went into industry in small "start up" companies, several of which have been very successful. He writes that he took his current company public in 1987.

DAVE TOPOLSKI, MBA '72, is president and owner of Temporary Team Employment Services of Phoenix, Arizona. He has

held personnel generalist positions with Trans-Union Corporation, Air Products & Chemicals, Inc., and Greyhound Corporation.

MICHAEL D. WAARA, BBA '72, is now the accounting manager for Fluorocarbon Company in Los Altamitos, California. From 1972 until April of 1987, Michael worked for General Motors Truck and Bus Group, and then joined Fluorocarbon.

74 BRIAN BRANDT, MBA '74, is now vice president, management supervisor with Jack Levy & Associates, Inc. in Chicago, where he is assigned to the accounts of Apple Computer, Aurora Venture, On-Cor, Sears Communications, Shure Brothers, and USRobotics accounts. Previously, Brian spent several years with Leo Burnett, Rust-Oleum Corporation, and Barton Brands.

9 *I fj PATRICK NILAND, BSE '71, MBA § %} '75, has become a partner in Colonial Group, Ltd. — a commercial mortgage firm based in Larchmont, N.Y. It arranges financing for investment grade real estate throughout the U.S. for property acquisition, project construction, permanent mortgage needs or refinancing. Colonial also arranges joint ventures and provides equity through syndication programs. Loan limits are from one million to two hundred million dollars.

9 ^7 ^7 EDWARD H. NOLAN, MBA '77, § § has been appointed senior manager in the audit division of the Detroit office of Ernst & Whinners international professional services firm. Nolan joined Ernst & Whinney in 1977 as a member of the audit staff and in 1983 became controller of the Beznos-Beztak Companies in Farmington Hills. He recently rejoined Ernst & Whinney. He is a member of the American Institute for Certified Public Accountants and the Michigan Association of Certified Public Accountants. He lives in Rochester Hills, Michigan.

JAN LAWRENCE, MBA '77, has followed her entrepreneurial talents and is now part of a start-up company called Simpson & Fisher of which she is vice president. The company has opened four retail stores called "Westminster Lace" which feature lace dresses, blouses, lingerie, bedding and dining room linen. She savs they were written up recently in NRMA's Stores Magazine as one of the "hot new retail concepts." Jan spent 8 years with Eddie Bauer, with a final

Harold Hughes, MBA 77, is Redefining the Role of (lorfHimte Trcanrer in his fob a! Intel

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director of merchandise control. She then joined Bob Camp, the former president of Pier I Imports, in beginning Simpson & Fisher. She lives in Seattle, Wash., and has climbed Mt. Rainier, participated in triathalons, and was the team captain for a team competing in a 180-mile relay race from Jasper to Banff, Canada. Then, when it was over, she biked back to Jasper to get the full experience.

5 ^ 7 0 JOHN L. DALY, MBA '78,
• O has been promoted to vice president of finance of the Edgewood Tool & Manufacturing Company, a Taylor, Michigan automotive supplier of stamped assemblies, hood hinges, and muffler hangers. John last appeared in *Dividend* as co-author of the one-act comedy "Frontier Accountant" which deals with the stereotypes surrounding the accounting profession. As a frequent speaker before student groups, he says that "accounting is never dull or boring to those who have the vision to see beyond the bottom line."

CRAIG SCHEPELER, MBA '78, spent eight years with IBA before joining CMI Corporation as their director of strategic planning. CMI is a computer leasing company in Bloomfield Hills, Mich. Craig has now been promoted to vice president of strategic planning, and has a staff of five. He and his wife, Elise, who graduated from U-M in 1977, are expecting their first child in July.

9 *7 Q RON HELL, MBA '79, JD '80,
§ *J recently became a partner in the Honolulu law firm of Torkildson Katz Jossem Fonseca & Moore. He continues to concentrate in the areas of taxation, including contested tax cases and business litigation. He is a CPA, and often teaches continuing professional education courses for both attorneys and CPAs. He and his wife, Shirley Ann, are actively involved in community theatre in Hawaii.

l O A ROBERT A. GILSON, MBA '80,
C^ vr writes that he is president of Nova Financial Design, Inc., of Farmington Hills, Michigan, which provides fee-only financial planning for individuals and small corporations. In 1987, Robert and two associates founded Nova. Bob recently completed certification courses for certified financial planner and chartered financial consultant.

5 0 1 WILLIAM WATCH, BBA '75,
OX MBA'81, has been named president of First Commercial Realty and Development in Warren, Mich., a company which handles commercial leasing and development and property management. Before joining First Commercial, Bill was Midwest real estate manager for Clothestime, a ladies' apparel retail chain. Before that, he was assistant vice president of real estate for the Auto Works division of Pontiac-based Perry Drug Stores, Inc.

'82

SARA RENDER, BBA '82, is accounting manager with the Michigan Educational Employees Mutual Insurance Company of Birmingham, Michigan, an automobile insurance company. Sara spent three years with Peat Marwick in Detroit and obtained her CPA. In 1985 she went with MEEMIC. Sara lives in Farmington Hills, Michigan and writes that she is active with a charitable organization of drivers' wives on the Indy car auto racing circuit.

CATHERINE WEISSENBORN, BBA '82, is audit manager with Price Waterhouse in Detroit, Michigan. Catherine spent the last five years with Price Waterhouse in Houston, Texas. When her husband, James, recently accepted a position with Pulte Home Corporation in Bloomfield Hills, she transferred to the Detroit office in 1987. Catherine and James live in Bloomfield Hills, Michigan.

BARBARA W^ORLAND (BRADEN), BBA '82, writes that she is a pricing analyst with Mayflower Transit, Inc., of Carmel, Indiana, a moving and transportation company. Barbara and her husband, Bill, live in Brownsburg, Indiana.

TONY ZAMBELLI, BBA '82, is a corporate financial consultant with Tunstall Consulting, Inc., of Tampa, Florida, which specializes in the creation of comprehensive business plans used to obtain financing and for management control. Tony spent 3'/2 years with Peat, Marwick, Mitchell & Company directly out of school, and then became an accounting manager in external reporting for Michigan National Corporation. Tony and his wife, Melinda, live in Tampa, Florida, where she is working on a Ph.D. in clinical psychology. He is a certified public accountant in Michigan and Florida.

y w ~£ RICHARD JAY NEWMAN, MBA
C^ «Lr '83, is vice president of Bear Stearns, Inc., in Chicago, Illinois where he manages the options and futures department. He and his wife, Barbara, live in Crystal Lake, Illinois, and have a daughter, Hannah. He says he has still not quite adjusted to being out of the Ann Arbor/Detroit area after five years, but "fortunately, WJR carries across Lake Michigan, and at night I can still get Ernie and the Tigers."

DAVID and JANINE SEEMAN BUSS, BBAS '83, are living in Port Washington, New York where David is a tax associate with the NYC law firm of Milgram, Thomajan & Lee, and Janine is audit supervisor with Coopers & Lybrand. They write that they proudly announce the birth of Arielle Lauren (BBABY '88) on January 20, 1988.

SARAH ULMER, BBA '83, worked for Deloitte Haskins & Sells for four years, and is now pursuing an MBA in finance at Indiana University, Bloomington. She writes that she is engaged to marry PHILIP HALLSTEDT, B.S. Chem. '82, M.S. Industrial Hygiene '84.

LAURA (BASSO) VAN PARYS, BBA '80, MBA '83, is currently the product planning manager for International Cellular telephones at Motorola Inc. Laura and MICHAEL VAN PARYS (MBA '79) had their second child in February and live in Inverness, 111., a suburb of Chicago. Michael is manager of industry analysis for Motorola's Corporate Strategy office.

9 0 ^ DEBRA A. FELTON, MBA '84,
%J JL has been appointed product manager of bathing products in the plumbing and special products group at Kohler Company. She is responsible for bath, whirlpool and shower product lines, and also development of new products within these lines. Kohler Co. is the nation's leading manufacturer of plumbing and leisure products.

* CJ pT JENNIFER E. NOLTE, MBA '85,
CJ %J writes that in August 1987 she left Clorox and started working as assistant product manager for the Pacific Bell Directory, San Francisco, California, She is responsible for marketing the Pacific Bell SMART Yellow Pages in California and Nevada, and is also responsible for the development of specialty directories. She was back in Michigan in April for the wedding of MARK ZOLNA, MBA '85. Also here for the wedding were MICHAELBARRY FINK, MBA '85, and LAIRD STEIFVATER, MBA '85.

'85

KAREN KNOBLE and BARRY BOBROW, both MBAs '85, were married May 8, and took their honeymoon in Nepal and Thailand. They will return to Chicago, where Barry will be transferring from banking officer to the commercial finance lending group at Continental Illinois Bank, and Karen will

be working as a decision support manager at Baxter Travenol's Parenterals Division in Deerfield, Illinois. They will be living in Evanston, and invite classmates to call them when in the Chicago vicinity.

9 O £1 DREW PATERSON, MBA '86, \J Vr has just been promoted to supervisor of intercompany accounts for the Europe/Africa division of Unisys Corporation. He says he will be traveling to almost every country in Europe during the next year. He now lives in Lansdale, PA, where he moved with the treasury operation after Sperry and Burroughs Corp. merged to form Unisys.

SUSAN LANG TAGUE, MBA '86, is now a senior financial analyst with Franciscan Health System (FHS) in Chadds Ford, PA. She will provide decision management information systems support and financial analysis services to FHS's corporate office and member organizations. FHS is a multi-hospital national health system with 3200 beds and $750 million in annual revenue. Susan was formerly senior product analyst with Shared Medical Systems.

9 O ^T BRANDON CROCKER, MBA '87, C^ • has been named assistant vice president/finance at Nexus Development Corporation, Southern Division. Nexus develops and manages commercial real estate in San Diego County, Calif. He writes that he also has an article appearing in the April issue of "The Freeman," the monthly publication of the Foundation for Economic Education, entitled "The Fallacy of Japanese Industrial Policy."

THOMAS R.JACOB, MBA '87, has been promoted to assistant vice president in the capital markets group of Heller Financial, Inc. in Chicago. He is currently involved in the private placement of debt and equity products, and writes that he has also made three recruiting trips back to the U of M since graduation.

ARIE Z. NEUMANN, BBA '87, was hired by Essential Resources Inc. of New York City in October of '87. ERI is the major competitor of Digital in the DEC training industry. He became a computer software instructor and also joined the corporate strategy group. He has now been promoted to the leader of the USDA training project which will involve 9 months of intensive training for the USDA in Washington, D.C. in business applications. He writes that he is also an account executive with responsibilities for marketing of training products, including on-site courses, video-based instruction, and public seminars around the country.

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Ph.D. Notes

9 Kj. O AMNUAY VIRAVAN, MBA '58, %J *J MA '57, Ph.D. '59, is chairman of the executive board of the Bangkok Bank, a position he has held since 1984. He has served as Thailand's Minister of Finance, Permanent Secretary for Finance, Director-General of Customs, and as an economic advisor to Thailand's prime minister. He is also chairman of the Asian Bankers' Association, director of the Asian Pacific Banking Council, governor of the Asian Institute of Management, and chairman of the Saha-Union Group of companies. Dr. Viravan was at the Business School in March, and spoke here on "Thailand Into the 1990s." His talk was the third of a series of Southeast Asia Business Lectures sponsored by the Business School and the Southeast Asia Business Education and Resources Program.

'fiQ KEN HARDY, MBA '66, PhD. '69, vF *y has just been promoted to full professor of business administration at the University of Western Ontario, London, Canada, where he teaches marketing management. He has also been a visiting professor at NEMI in Norway and INSEAD in France. His new book, Marketing Channel Management: Strategic Planning and Tactics, was published by Scott, Foresman in 1987. He has published more than 70 cases and written numerous articles in the academic press. He is a reviewer for the Journal of Marketing.

ERIC FLAMHOLTZ, Ph.D. '69, and Yvonne Randle are co-authors of a new book, *The Inner Game of Management,* published by AMACOM. The book is a guide to attaining the self-knowledge that can make you a better manager. It includes ways managers deal with the need for self-esteem, the need for control, and the need to be liked. Eric is Professor of Management at UCLA and president of Management Systems Consulting Corporation, which he founded in 1978.

'74 Louis W. PETRO, MBA '68, Ph.D. '74, is consulting editor for the recently published Volume V, Manufacturing Management of the fourth edition of The Tool and Manufacturing Engineers Handbook. The book was published by the Society of Manufacturing Engineers in Dearborn, Mich. Louis is dean of the School of Management at Lawrence Institute of Technology in Southfield, Mich.

'*7*7 H. MICHAEL HAYES, PhD. '77, • § is the newly-appointed Director of Graduate Programs and professor of marketing and strategic management at the University of Colorado at Denver. In August, he will take up a one-year appointment as visiting professor of business administration at the International Management Development Institute (IMEDE) in Lausanne, Switzerland.

Iwo Recent Ph.D. Graduates Win Annrds for Outstanding Research

Don Kuihi\. PhD. *Sl>. and (l.ir\ S. Hansen. Ph.D. XT. have won awatds lot outstanding dissertations. Don won the I9.H7 Dissolution Competition of the American .Matketini; Association. I lis dissertation was entitled "Hie Impat! of the ()i^.tni/.t-tionai (.ontext on (!onllii t in ()t''.mi/attonal Buvin«i: A Svsieni.s View." He isuinentlv assistant proit ssor at the I'niversiiv of Western Ontario.

Gaiv Hansen received the I**S7 award (ot Outstanding Roseau 11 in Sit atomic Management. His dissertation was one of 'JI entt ies to the business poli< \ and plan-ning division of the Atadetm of Management. He is now assistant prolessot of sti atomic manage-ment .it theSthooloi Business Administi.ition. I'niversitv of Washington. Seattle.

Deaths

LESLIE A. BRANDT, MBA '31, retired vice chairman of the Peoples Gas Light and Coke Company and the utility's parent company, died February 4,1988, following surgery. He was 82.

Brandt became associated with Peoples Gas in 1934 as a junior staff auditor and was promoted through the ranks of the Accounts Division of the Chicago utility company. He was elected vice president of industrial relations in 1952, and in 1957 became vice president and controller.

In 1961, he was named president of Peoples Gas, and nine years later was promoted to vice chairman of the utility and its then parent firm, Peoples Gas Company, which later became Peoples Energy Corporation.

During his 36-year career, Brandt was active in numerous civic and industry affairs. Among them were two terms as president of United Charities of Chicago, and 14 years as a director of that agency. He also was a director of the Chicago-based Institute of Gas Technology, the natural gas industry's research arm; and the Gas Development Corporation, the Institute's licensing and management consulting subsidiary. He was also a director of his industry's national trade organization, the American Gas Association.

Survivors include two brothers, Irving W. of Royal Oak, Mich., and Robert E. of Hale, Mich.

JOHN E. SLYKHOUSE, BBA '81, died March 9,1988, at the University of Texas System Cancer Center in Houston. He was vice president of Entela Inc., a former coach of the East Grand Rapids Age Group Swim Team, coach of the Ottawa Hills High School Men's Swim Team, and a member of the Greenridge Country Club, Trinity United Methodist Church, and the Grand Rapids Economics Club.

He is survived by his wife Pam and his parents George and Joyce Slykhouse.

While at Michigan John was a member of the Varsity Swim Team and was elected captain in his senior year. In John's honor, the athletic department has established a permanent fund, interest from which will be used to help worthy student-athlete swimmers at Michigan. Donations to the fund (which are tax deductible) should be made payable to The University of Michigan, and directed to the John Slykhouse Memorial Fund, Michigan Athletic Department, 1000 S. State Street, Ann Arbor, Michigan 48109.

Tracy Williams, vice president of Chase Manhattan Bank.

Deborah Chatman, vice president of J. P. Morgan.

D. C. Goin

Cleve Christophe, MBA "67, senior vice president, TLC Group.

s Talk to Students
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The story of how Cleveland Christophe, MBA '67, and his partner in TLC Group accomplished a 985 million dollar leveraged buyout of Beatrice International Foods Co. was told by Christophe at a business colloquium sponsored by the Black Business Students Association at the Business School, the Michigan Student Assembly, and the Office of Minority Affairs.

Christophe was one of three young Black Wall Street executives who spoke at the colloquium. The other two speakers were Tracy Williams, MBA, Columbia University, vice president of Chase Manhattan Bank; and Deborah Chatman, MBA, The University of Chicago, vice president of J. P. Morgan.

The Colloquium was held Friday, March 25, and was part of Alumni Weekend for Black alumni of the Business School. A dinner-dance was held Saturday at Sheraton University Inn for returning alumni. The dinner speaker was Sharon Reed, MBA '81, Manager, Strategy Development, Scott Paper Company.

Williams' talk included a personal account of the atmosphere on the Street during the Oct. 19 market crash, along with a discussion of how world markets have become interlocked in the 1980s.

Chatman talked about careers on Wall Street, and gave tips on how to develop a clear-cut strategy in terms of what you want to do. She cautioned against vagueness in goals, and pointed out that firms are specialized now on Wall Street. You need to research firms thoroughly and have a clear idea of whether you want corporate finance, sales positions, or trading positions, because different positions require different skills and personalities.
Christophe gave an absorbing description of the step-by-step process by which he and his partner, Reg Lewis, a graduate of Harvard Law School, accomplished the largest international leveraged buyout that has ever been done.

The enterprise began after Lewis acquired McCall's Sewing Pattern Company from Esmark for $20 million and later sold it for $65 million. After much soul searching, Christophe decided to leave Citicorp where he had spent 20 years, and join Lewis in forming the TLC Group, a firm which engages in leveraged buyout investments. His experience at Citicorp had included everything from being head of an investment research unit, to being Citibank Country Operations Head for France, to heading Citibank's Corporate Banking Team for High Technology Industries; to being Citibank Country Head for Jamaica and for Colombia.

Christophe told the story of teaming with Lewis, borrowing close to $1 billion and outmaneuvering large finance firms to acquire Beatrice, a corporation with $2.5 billion in revenues.

Some of the rules which the pair followed to outbid established financial conglomerates were: 1) keep it simple, 2) understand how the firm will be paid for; their goal was to complete a leveraged buyout, servicing the debt out of pre-tax cash flows, 3) understand the motivation of the players, 4) contain the costs (legal expenses and accounting fees amounted to $53 million), and 5) maintain credibility. (They made a conscious effort to make measured statements and to avoid overselling.)

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A Regional Bank's Perspective: NBD as a Case History

Continued from page 12

since last February. We certainly would explore the cash market, the secondary market for selling debt — since we are charged down, this would have very little impact. We have not considered seriously the debt-equity swaps that have been much talked about. We have no desire to own hotels anywhere in the U.S., or in Mexico, or Chile.

So essentially we're down to looking at a larger Mexican government portfolio that has been developed through these restructuring. I think we have somewhere in the area of 115 million dollars that would perhaps be eligible for this Morgan U.S. Treasury proposal. That does not strike us initially as being terribly attractive.

We think Mexico, by the way, is one of the LDC countries that is most likely to be able to service its debt over time, and over time is a long time after I retire. But nonetheless we think that interest can be paid in some proportion for a long time into the future.

We don't really think we have a solution to the debt crisis. Even though we haven't agreed with the Money Centers, we think a valuable service has been provided by keeping countries alive through this last five years. The focus now may be moving away from the commercial banks to what must be done with the developing countries. Despite the Federal Reserves' great concern about the systemic risk which was their great inducement to contribute new

We certainly are prepared to stay and see what happens, since we have no other choice. But we will be very difficult to convince in the next negotiations of the steering committees that we should contribute much in the way of new money to Brazil. I think we will be difficult even to convince if Mexico comes back to the table again in the next year or two, that we should provide significant new money. We would be much more prepared to look at interest capitalization; to taking a portion of the portfolio that might be serviced and accepting interest on that; than in making arrangements on a portion that cannot be serviced. We think there are other ways to do it. I'm sure we're going to hear more this morning from people far better informed than I on how this can be worked out in more of a macro sense, and we are prepared to address it.

Calling All

We arc I bin king of starling a "Letters to the Ldilor" column in *Divhisiitt.* If you have any comments, afterthoughts, or disagreements abnit articles that you read in these pages, let us bear from vou.