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August 4, 1983

To: Members of the Executive Board

From: The Secretary

Subject: The Fund, Commercial Banks, and Member Countries

In view of the coming external difficulties, already perceived in the first part of 1982, the Managing Director felt it would be useful to ask an external consultant, with a personal knowledge of Fund procedures and methods, to prepare a report on "The Fund, Commercial Banks, and Member Countries." Mr. Paul Mentré, a former Executive Director, conducted the study from April to December 1982 within the European Department in close association with the Exchange and Trade Relations Department, and as and when needed in consultation with other departments. It was based on discussions with officials, central bankers, members of international organizations, and commercial bankers in industrialized countries and on missions in European borrowing countries at various stages of their debt cycles (Portugal, Turkey, Yugoslavia, Hungary, and Romania).

This report, which was preceded by interim documents and supplemented by some individual studies, was made available to the Managing Director at the beginning of 1983. It was thought that it might be useful to give it a wider diffusion, as soon as the final figures for end-1982 would be available, with the deletion of some confidential information provided by commercial banks or central banks.

The Executive Directors will find attached this updated and revised version of Mr. Mentré's report. It is to be supplemented by an annotated bibliography which, after September 1, 1983, will be made available on request to the Secretary's Department.

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It should be stressed that, while some of the findings of this report have been used to help formulate Fund policies, notably as a contribution to Board discussions on external debt matters, the report is of a personal character and does not represent Fund policies or judgments. It constitutes an attempt to give some general background to ongoing developments which will continue to be addressed, in due course, through the permanent staff structure and through appropriate Board actions.

Att: (1)

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Department Heads

July 1983

The Fund, Commercial Banks, and Member Countries

Main Report
(Revised)

P. Mentré

The rapid increase in the external debt of nonindustrialized countries since 1973-74 and the corresponding rapid growth in transborder claims of commercial banks had led to a vulnerable structure of international indebtedness. The risks inherent in the system had been pointed out by many observers for many years. These risks materialized in 1982 when the persistence of high positive real interest rates, the deepening of the recession in the industrialized world, and political tensions in several regional areas combined to induce a series of adverse developments:

- a liquidity crisis in Eastern Europe, in the wake of the Polish crisis, with the rescheduling of the debt of Poland and Romania and increased uncertainties in the liquidity situation of other countries in the area;

- a debt crisis in Latin America, in the wake of the South Atlantic crisis, with the postponement of debt service obligations by Mexico and Argentina and heightened debt servicing difficulties in other countries in the area; and

- a confidence crisis on the interbank market, in the wake of the Ambrosiano crisis, with a contraction of the London interbank market in the second quarter and the re-emergence of tiering between banks.

These developments have already led to a reduction in the rate of increase of net international bank credit which grew by US$50 billion in the first half of 1982 (annual rate: 11 percent) against US$65 billion (annual rate: 16 percent) in the first half of 1981, and US$45 billion in the second half of 1982 (annual rate: 9 percent) against US$100 billion (annual rate: 25 percent) in the second half of 1982. 1/ For 1982 as a whole the rate of increase was 10 percent but a further slowdown is widely expected in 1983. Preliminary figures for the first quarter of 1983 show, for instance, that new lending by banks to borrowers outside the BIS area was down to US$0.5 billion against US$9 billion in the fourth quarter of 1982. For its part, the most recent IMF World Economic Outlook contemplates a rate of growth of bank lending to non-oil LDCs of 9 percent in 1982 and around 7 percent in 1983 against 22 percent in 1981. Such a slowdown of international bank lending will reinforce the pressure on borrowing countries, notably on non-OPEC developing countries and on East European countries, to adjust their economies more severely, thus hurting prospects of a widespread and sustained recovery in 1983-84. In addition, while the international monetary system has again shown its resilience in 1982 by coping with simultaneous crises in 4 or 5 of the 20 largest non-BIS borrowing countries, there remains a need to address some of the systemic problems which have emerged during the last 12 months.

1/ These figures are based on the quarterly reports published by the BIS. Quarterly figures at end-1982 are used in the 1982 Annual Report released by the BIS on June 13, 1982, and in the text of this report unless indicated otherwise. As described in the footnote on page 22, semiannual figures at end-1982 give a somewhat more encouraging picture for credit expansion to non-BIS countries.

The Fund, whose primary purpose is monetary, financial, and economic stability in the world, has to play an active role in avoiding or mitigating adverse developments in international bank lending activities. During recent years, the Fund has already felt the need to develop and strengthen its relations with commercial banks: periodic meetings with commercial banks and annual publication of a study on international capital markets; ad hoc discussions on problem countries with the concurrence of the country concerned; and active participation in rescheduling negotiations. This function widened and intensified in 1982 when the Fund, in close association with the BIS, played a leading role in the coordinated handling of actual or potential crises in Mexico, Argentina, Hungary, Yugoslavia, and Brazil.

The present report is an attempt to summarize recent developments in relations between the Fund, commercial banks, and member countries with specific reference to five individual European borrowing countries. It addresses four interrelated issues which could be relevant for possible Fund action in the future:

- how to assess better the attitude of commercial banks toward individual countries;

- how to assist better member countries in the management of their external debt;

- how to develop constructive relations between the Fund, member countries, and commercial banks in the course of regular Fund activities; and

- how to handle better actual or potential crises.

In the conclusion and recommendations, specific suggestions are listed.

It should be stressed that these conclusions and recommendations are largely based on recent Fund experience and current practices. They should therefore be considered as a part of an evolutionary process and not as a change in the overall policy stance which has demonstrated again in 1982 its ability to cope with major difficulties and to serve the international community.

Part I. How to assess better the attitude of commercial banks toward individual countries

A. The setting

1. During the 20 years from 1960 to 1980, transborder bank claims as reported by the BIS have grown at an average annual rate of about 25 percent. As of December 31, 1982, they stood at US$1,950 billion (about US$1,000 billion excluding redepositing among reporting banks). Banks located in the United States, the United Kingdom, and offshore centers play a leading role, while the dollar remains the predominant currency representing more than four fifths of total claims (Table 1).

The international banking system now plays a fundamental role in *the functioning of the international monetary system, extending credits* to deficit countries and collecting funds from countries whose surpluses mirror the deficits financed by bank credits (Table 2). 1/

The pattern of net financing is evidently evolving over the years, but basically the overall system is channeling funds from OECD countries and from Middle Eastern and other OPEC countries to the other industrialized countries, Eastern Europe, and non-oil developing countries, notably Latin American countries. 2/

2. As pointed out by the Task Force on nonconcessional flows in its report to the Development Committee, commercial bank loans in particular have played a fundamental and growing role in the financing of current account deficits of non-oil developing countries, notably middle-income countries (Table 3).

International bank lending now represents more than 50 per cent of total international capital flows and more than 50 per cent of total LDC long-term external debt (out of a total debt of US$425 billion, as of end-1981, against US$97 billion, as of end-1973, which represents an increase of 330 percent in eight years).

The development of medium-term international bank credits through publicized syndicated loans or direct transactions has been one of the most striking features of these financing patterns. Claims with a maturity of more than one year now represent about 50 percent of total bank claims, thus contributing fundamentally to the medium-term financing of current account deficits. The Fund, in its overall assessment of the international financial and monetary situation and of

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1/ The terms "credits to deficit countries" and "funds from surplus countries" need to be interpreted on a net basis. The international banking system collects funds from entities throughout the world (including from deficit countries) and grants credits to entities throughout the world (including from surplus countries).

2/ The narrowly defined Euromarket, as calculated by the BIS (banks of the reporting European countries, after elimination of redepositing), displays the same overall picture (Table 4).

Table 1. Transborder Bank Claims (BIS Reporting Area)
Amounts Outstanding December 31, 1982

(In billions of U.S. dollars)

	United Kingdom	Other European	Canada	Japan	United States	(Of which: IBF)	Offshore branches of U.S. banks 1/	Total	Other offshore banks 1/	Grand total
Claims in domestic currency	26	130	2	25	354		159	709		
Claims in foreign currency	432	435	37	66	7		13	978		
Total	458	565 2/	39	91	361	(144)	172	1,587	260 3/	1,947
Total non-U.S.	........1,153 4/...............									
Of which: claims in U.S. dollars	.........(707).................				(354)		(159)	(1,220, i.e., 72%) 5/		

Source: BIS, Quarterly Report.

1/ The column "offshore branches of U.S. banks" includes the Bahamas, the Cayman Islands, Panama, Hong Kong, and Singapore; the column "other offshore banks" includes claims by other banks in these offshore centers plus bank claims in two other offshore centers: Bahrain and the Netherlands Antilles; the column "offshore centers" in Table 2 includes also: Lebanon, Liberia, Vanuatu, Barbados, Bermuda, and other British West Indies.

2/ The breakdown of continental European banks' claims is as follows:

	France	Luxembourg	Germany	Netherlands	Switzerland	Belgium	Italy	Austria	Others (Ireland Sweden, and Denmark)	Total
Foreign currency	124	89	21	49	30	58	33	18	13	435
Domestic currency	24	1	49	13	32	2	1	7	1	130
Total	148	90	70	62	62	60	34	25	14	565

3/ Estimate.

4/ Excluding position in foreign currencies vis-à-vis residents: US$429 billion (of which US$323 billion in U.S. dollars and US$106 billion in other foreign currencies. U.S. dollar claims represent also 72 percent of total claims in foreign currency (US$978 billion).

5/ The other currencies playing a significant role are the deutsche mark (12 percent), the Swiss franc (6 percent), the yen (2 percent), the pound sterling, the French franc, and the Dutch guilder (about 1 percent each).

Table 2. External Positions of BIS Banks Vis-à-Vis Individual Groups of Countries
Amounts Outstanding December 31, 1982

(In billions of U.S. dollars)

	BIS area	Offshore centers (excl. Bahrain)	Other developed countries	Eastern Europe	OPEC countries (incl. Bahrain)	Other developing countries	Of which: Latin America	Of which: Middle East	Of which: Other Asia	Of which: Other Africa	Unallo-cated	Total	Of which: vis-à-vis nonbanks
Assets	894	268	112	53	79	247	169	13	47	18	34	1,687	550
Liabilities	1,027	250	49	16	135	101	37	21	34	9	42	1,620	313
Net position vis-à-vis banks	+133	-18	-63	-37	+56	-146	-128	+8	-13	-9	+8	-67	-187

Source: BIS, Quarterly Report.

Table 3. Net Capital Flows to Non-Oil Developing Countries

(In billions of U.S. dollars)

	1970	1975	1978	1980	1970	1975	1978	1980
	Low-income countries				Middle-income countries			
Current account deficit	3.6	7.0	5.1	9.1	14.9	42.8	20.4	48.9
In per cent of GNP	(1.4)	(3.9)	(2.5)	(4.5)	(2.5)	(5.5)	(2.3)	(4.0)
Net capital flows ODA	3.4	6.6	5.1	5.7	3.3	5.3	6.5	7.9
Private direct investment	0.3	0.4	0.2	0.2	3.4	3.8	4.6	4.5
Commercial loans	0.5	0.8	0.9	0.7	8.9	21.0	29.4	27.1
Change in reserves and ST borrowing	-0.5	-0.7	-1.1	2.4	-0.8	12.7	-20.1	9.5

Source: Development Committee, Task Force on Noncommercial Flows.

Table 4. Euromarket Positions: Amount Outstanding December 31, 1982

(In billions of U.S. dollars)

	Reporting European area	United States	Canada and Japan	Other developed countries	Eastern Europe	Offshore centers	OPEC countries	Other developing countries	Unallo-cated	Total
Uses of funds	275	54	55	69	33	82	37	85	12	702
Sources of funds	265	114	31	33	14	87	89	46	23	702
Net use	10	-60	24	36	19	-5	-52	39	-11	--

Source: BIS, Quarterly Report.

individual member countries' external positions, had therefore to pay increasing attention to international bank lending and to the changing characteristics of the Eurodollar market.

3. The international bank credit market can be characterized by the existence of three circles:

a. The inner circle, which consists of about 25 large banks based in OECD countries. These banks are able to use their deposit base for transborder domestic currency lending, notably dollar-denominated loans for the big U.S. banks and their subsidiaries or branches in London and in offshore centers and deutsche mark-denominated loans for the major German banks and their subsidiaries in Luxembourg. In addition, they have a sufficiently strong capital base, a sufficiently diversified portfolio, and a sufficiently large international network to attract deposits from the main international depositors (non-G-10 central banks, OPEC countries, and multinational corporations shifting their assets from domestic assets to Eurodollar assets or to other Eurocurrency assets) and from the other banks for which they act as correspondents. They normally have the capacity to be simultaneously the main participants in credits to final borrowers and the main suppliers of funds, through interbank placements or deposits, to other banks in the market.

b. The intermediate circle, which consists of about 2,000 or 3,000 banks all over the world and includes three main categories:

- small or regional banks from industrialized countries which use either their domestic deposits, notably for regional U.S. banks, 1/ or interbank credits to fund their participation in syndicated credits or bilateral transactions with final borrowers;

- consortium banks associating banks of similar characteristics (a group of industrialized country banks, a group of OPEC or Arab banks) or associating one or two industrialized country banks and developing country banks; and

- commercial banks from developing countries or centrally planned economies which, in addition to some direct deposits, use interbank borrowing, either directly or through their branches or subsidiaries abroad, to fund loans to their own countries or to participate in credits to third countries, notably in connection with their own countries' exports.

The intermediate circle is thus heterogeneous, and the distinction between participants somewhat blurred: the large Arab consortium banks have a capital and a deposit base which are gradually bringing them into the "inner circle"; the central banks of Comecon countries, and their network of associated banks in Moscow (International Bank for Economic Cooperation), London, and Paris, act both as intermediaries and as final

1/ Fifteen hundred U.S. banks presently have transborder claims among their assets.

borrowers. But basically this intermediate circle is a channel through which large deposits collected by the inner circle and not used directly by the leading banks are relent to final borrowers.

c. The external circle, which consists of final borrowers. It includes a large variety of entities: private enterprises in industrialized countries borrowing in foreign currencies from their domestic banks or from international banks or borrowing in their domestic currency from international banks (Eurodollar borrowings by large multinational U.S. corporations with a growing integration between domestic dollar borrowings and Eurodollar borrowings); public entities and notably sovereign states among the industrialized countries; private enterprises in developing countries borrowing in foreign currencies from their domestic banks or from international banks in addition to direct borrowings from their commercial suppliers or, for subsidiaries, from their parent companies; public entities and notably sovereign states among the developing countries and centrally planned economies. 1/ While the characteristics of these final borrowers are thus quite diversified, there is a tendency to group them according to the locus of the final sovereign risk, after reallocation of guaranteed loans, under a general country risk assessment.

Thus, the stability of the market depends on three components: the quality of final risks, i.e., the quality of country risks, which is in turn related to the adequacy of economic policies; the attitude of the large banks, which are the key actors in the market; and the stability of the intermediate circle and of the interbank market. Even if final risks are sound and large banks cautious on country risks, the instability of the intermediate circle could well shatter the overall structure.

4. A more detailed analysis of participants in international bank lending and on the interbank market is given in the annotated bibliography together with some statistical data. In summary, at the beginning of 1982, and after 20 years of rapid expansion, the market was characterized by:

- the leading role played by 25 banks 2/ representing 60 percent of total lead management; 15 to 20 banks with international assets greater

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1/ The relative proportion of the various types of borrowers varies over time, but a standard pattern for banks within the BIS reporting area is one third private entities, one third governments, and one third public entities (and on the deposit side one third banks, one third non-banks, and one third central monetary authorities).

2/ The list of the 25 most active banks in international lending activities, as indicated, for instance, by Institutional Investor, varies slightly each year, but on average is as follows:

7 American banks: Citibank, Chase Manhattan, Morgan Guaranty, Bank of America, Manufacturers Hanover, Bankers Trust, Chemical (plus Irving Trust in some years).

4 British banks: Lloyds, National Westminster, Barclays, Midland.

3 German banks: Deutsche Bank, Dresdner Bank, Commerzbank (or some

than US$20 billion would account for about 50 percent of total international bank lending, while 50 to 70 banks with international assets greater than US$10 billion account for about 85 percent of total international bank lending;

- the fundamental role played by interbank transactions, which gives "breadth and depth to the market"; 1/ approximately 2,000 banks participate in the market; the largest banks redeposit about 60 percent of their deposits; interbank transactions represent about 45 percent of total international bank lending (60 percent if transactions within BIS countries are included; see page 22);

- the growing involvement of second-tier banks: small banks from industrialized countries, notably for loans to neighboring countries (Mexico for U.S. banks, Eastern Europe for German banks); banks from developing countries (the share of nonindustrialized countries' banks in the list of banks included in the first ten participants of all publicized Eurocredits has grown from 5 percent in 1973 to 10 percent in

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2/ (cont'd from p. 5) years Westdeutsche Girozentrale).
4 Canadian banks: Royal Bank of Canada, Canadian Imperial Bank of Commerce, Bank of Montreal, Bank of Nova Scotia (or some years Toronto Dominion Bank).
3 Japanese banks: Bank of Tokyo, Industrial Bank for Japan, Fuji Bank (or some years Sumitomo Bank or Dai-Ichi Kangyo Bank).
3 French banks: Banque Nationale de Paris, Société Générale, Crédit Lyonnais.
3 Swiss banks: Union Bank of Switzerland, Swiss Bank Corporation, Credit of Switzerland.
1 Belgian bank: Société Générale de Belgique (or some years Kredietbank or a Dutch bank, Algemene).
Twenty-three of these banks, including all leading American, German, U.K., and French banks, plus the leading Japanese bank (Bank of Tokyo) and the leading Canadian bank (Royal Bank of Canada), were consulted in the course of the mission. In addition, discussions were held with one Chicago bank (First National), one Arab bank (UBAF), and one Austrian bank (Creditanstalt).

1/ Transactions in dollars between banks are now fully integrated through the "clearing house interbank payments system" (CHIPS), which, since October 1, 1981, has been operating in New York as an electronic credit transfer system for worldwide settlement of dollar accounts and gives special responsibilities to the seven largest New York clearing banks.

1980 (27 out of 332). 1/ In all, about 65 new participants have been entering the international syndicated loan market every year during the last ten years; 2/

- the shifting pattern of funding on the market, depending on the magnitude of OPEC surpluses and the effects of relative current account positions, of national monetary policies, or specific restrictions on international lending in various industrialized countries; and

- the concentration of sovereign risks on a limited number of countries. Thus transborder claims on BIS countries represent about 50 percent of total transborder claims of BIS banks (compared with 30 percent for non-BIS countries, 15 percent for offshore centers, and 5 percent unallocated). Among claims on non-BIS countries, 20 debtors accounted for about 90 percent of total claims (Table 5).

These evolving patterns have shaped the attitudes of commercial banks. The banks have tried to improve their assessment of country risks, especially for the largest borrowers, which explains the growing sophistication of assessment procedures. They are now trying to improve their knowledge of the interbank market and their assessment of risks on the individual banks that are participants in the market, a reappraisal that is reflected in recent developments.

B. Country risk assessment

1. With their growing involvement in international lending, commercial banks have felt the need to develop more sophisticated techniques of country risk analysis. This entails an analysis of sovereign or transfer risks which are the risks of default by all borrowers from the same country when, due to the external situation, the monetary authorities are not in a position to supply individual borrowers the foreign exchange needed to meet their external debt obligations.

With very limited exceptions, banks engaged in international lending set limits for overall risks on a given country and reappraise their limits quarterly, or at least once a year, with interim revisions in the meantime for specific countries. These country limits are based on an overall perception of the risks attached to a given country. Country

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1/ These 332 banks (out of an overall total of 380 banks having participated in 1980 in syndicated loans for a total number of individual participations of 4,918) comprised: 54 U.S. banks, 24 Japanese banks, 21 German banks, 19 French banks, 18 British banks, 15 Italian banks, 14 Austrian banks, 11 Swiss banks, 9 Canadian banks, plus 60 other European banks (of which 22 were from Spain or Portugal), 25 banks from the Middle East, and 62 banks from other countries or consortium banks.

2/ For some observers (see G-30 report) this expansion of the number of participants had been an important element in the growth of the market which might well disappear in view of present difficulties.

Table 5. Twenty Principal Non-BIS Borrowers 1/

(In billions of U.S. dollars, end-December 1982)

	Amounts of claims by BIS reporting area
Industrial countries	68
Spain	23
South Africa	13
Australia	12
Norway	11
Finland	9
Eastern countries	41
U.S.S.R.	14
Poland	13
German Democratic Republic	8
Hungary	6
Developing countries	
Europe	28
Yugoslavia	9
Greece	9
Portugal	10
Latin America	170
Mexico	59
Brazil	56
Argentina	22
Venezuela	23
Chile	10
Others	34
South Korea	19
Philippines	8
Nigeria	7
Total	341

Source: BIS, Quarterly Report.

1/ Other non-BIS borrowers with bank debts greater than US$4 billion: Israel, Romania, Peru, Colombia, Ecuador, Egypt, Algeria, Indonesia, Malaysia, and Taiwan (the Taiwan Province of China).

risk assessment methods vary across banks but basically belong to three main categories (see bibliography and the studies mentioned in it, particularly the G-30 study):

a. the unstructured approach in which a series of ad hoc decisions are taken on the basis of individual country reports without any codified format;

b. the fully quantitative approach in which countries are automatically classified in different categories according to the results of a model based on a set of economic indicators; and

c. the qualitative/structured approach in which decisions are based on standardized reports including a homogenous list of relevant indicators.

There is a clear tendency, as international bank lending develops, to move from (a) to (b) or (c) with a majority of major banks using (c). Hence the set of indicators used by individual banks will have some automatic bearing on their lending attitudes and policies.

2. The sets of variables taken into consideration by individual banks differ from bank to bank. But basically they fall into the following categories:

- domestic economy (GNP, inflation rate, exchange rate);

- balance of payments (reserves, trade balance, current account balance, capital flows);

- external debt (total external debt, ratio to GDP, debt service ratio); and

- political situation (internal stability, attitude of various groups and parties on economic issues, external threats).

Some systems are more comprehensive than others (with particular reference to resources, including energy), some are more forward-looking, and some are based more on year-to-year comparisons than on absolute amounts, but they have many characteristics in common. In particular, they all stress *the debt service capacity as the key variable in assessing potential* transfer risks. In some cases, there are even models which try to derive a list of potential problem countries from a set of selected indicators. Clearly, the quality and the timeliness of the information injected into the system is crucial. For that reason, all commercial banks stress the need to improve information disclosure by borrowing countries, either in their own statistical publications or in IFS. A specific area of concern relates to shortcomings in external debt data: delays in the production of BIS data on banks claims; 1/ inadequate coverage of short-term debt to nonbanks; inadequate coverage of military debt; and undue delays in the collection of statistics on long-term public debt (World Bank) and on export credits (OECD).

In addition to better information gathering, efforts under way in banks to improve their country risk assessment systems have three main aspects:

- a trend toward computerization with a large use of data banks;

- a trend toward the inclusion of a judgment on potential political developments, through the hiring of political specialists, which might imply a loss in both the objectivity and the intercomparability of country risk assessments; and

- a trend toward a greater weight being given to "vulnerability to random events," which means the capacity through an adequate liquidity situation to cope with unexpected adverse developments or "contagion" effects.

3. In spite of recent improvements in country risk assessment systems, the translation of country risk assessment into actual country limits remains ambiguous. Whether country risk assessment through a formalized set of data is an integral part of the country limit-setting process (some U.S. banks) or whether its results are synthesized by a rating of the country or its classification in one of five or six groups (most other large banks), in all cases other elements have an important bearing on the end-result.

First, external judgments are introduced into the system either in the rating or in the setting of limits: rating by external consultants or by publications (Institutional Investor); experience of the bank's industrial customers in the country, with a tendency, notably in Japanese banks, to pay growing attention to delays or modifications of financing patterns in relations with suppliers (and trading companies) as early indicators of coming difficulties; attitudes of official agencies, such as governments, export credit agencies, supervisors, and central banks (see below); and the judgment of the Fund or of the World Bank as determined by effective policy actions (stand-by arrangements, SALs) or by informal contacts.

1/ The BIS publishes quarterly data on bank transborder claims and more detailed semiannual data. But these data are not fully comprehensive (exclusion of trust funds and fiduciary accounts in Swiss banks, partial coverage of offshore centers). In addition, in spite of recent efforts, they are made available about four months after the end of the period covered (July 18, 1983 for data to end-March 1983), while bankers would need them in time to feed them into their systems before fixing their new quarterly limits (which would imply having data as of March 31, 1983 available on June 15, 1983).

Second, the banks' commercial strategy has to be integrated into the process: relations with exporters eager to see credits granted to their customers; desire to maintain or establish a presence in the country. Finally, market conditions play a role notably in ad hoc revisions of ceilings: high spreads improve the closely watched "rate of return on total assets" and send a signal of adjustment to borrowing countries; low spreads bear testimony to the quality of the signature as perceived by the market. 1/

Overall country limits are largely based on past experience adjusted according to market trends (share of the bank in overall BIS claims or, for a U.S. bank, in all U.S. banks or in its "peer" group) and the results of the country risk assessment are continuously balanced against commercial considerations. In addition, the monitoring of lines is not always fully adequate: setting of limits within the international department which leads to undue weight being given to commercial aspects; exclusion from country limits of interbank placements which are not transborder claims (placement by the London branch of an American bank with the London branch or subsidiary of a Latin American bank); distinction between medium- or long-term claims (more than one year) and short-term claims with a tendency to be less strict on the latter category, in spite of the illiquidity risks attached to a rapid growth of short-term indebtedness.

On all these aspects improvements are under way:

- computerization of all interbank relations in which the whole bank network is engaged;

- objective definition of country limits by formulae based on GNP, total BIS claims, and total national claims as a starting point to which country risk assessment and commercial opportunities apply; 2/ and

- setting up of a portfolio target in which the weights given to individual countries and individual regions take into account their relative importance and the potential medium-term risks resulting from individual countries' policies or from "regional contagion effects" with a view to moving gradually in the direction of the portfolio target in actual decisions regarding country limits.

Above all, the functioning of the market itself leads to a "herding effect": if other banks are in a country, the risk of an isolated error is limited; if other banks start to cut their lines, maintaining its exposure would in fact mean bailing them out. Small banks in all

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1/ An analysis by the Fund staff shows a highly positive correlation between the level of spreads and the availability of credits. Similarly, a Bank of America study shows that the correlation between debt movements, reserve movements, and GNP movements is greatly enhanced by the inclusion of a "SCORE" element (rating by Institutional Investor).

2/ One bank, as a new participant in the market, used Fund quotas as a starting point for the initial allocation of country limits.

countries are reportedly the more likely to shift abruptly from a position of open lending to a position of rapid reduction of exposure, facilitated by the predominance of short-term claims, but such behavior is rapidly spreading in the market.

4. In view of the growing share of external claims in the overall assets of individual banks, supervisors and central banks are paying growing attention to the quality of external portfolios.

Under the aegis of the BIS "Committee on Bank Regulations and Supervisory Practices," set up in 1974 (first, the Blunden Committee and, since 1978, the Cooke Committee, the names of its chairmen), major efforts have been undertaken to pay greater attention to country risks by individual supervisors and to achieve a greater uniformity of supervisory practices (see bibliography).

First, there is now an agreement to require worldwide consolidated data from individual banks to get a clear picture of their overall results; unfortunately, the agreement is still not fully implemented in some major countries.

Second, there is a movement toward a greater consistency in capital adequacy requirements (where large differences still exist), and, possibly, toward a greater similarity in provisioning policies.

Third, there is a growing tendency among supervisors to look at the adequacy of country risk assessment systems by individual banks and even to check their results against those of an independent system managed by the supervisor itself. It is a process which started in 1977 in the Federal Reserve Bank of New York (Interagency Review Group) with a screening process, a grouping of countries according to potential risks, and a process of comparison for individual banks with its peer group. 1/ In addition, the classification of loans as performing or nonperforming assets has a direct effect on the lending attitude of American banks.

Other central banks are less advanced in this area, either because they rely more on qualitative or semiquantitative techniques and on informal discussions with bankers or because supervisors and central bankers consider that they do not have themselves to pass judgment on individual countries. But within the Cooke Committee, an agreement was reached on "country risk analysis and country exposure measurement and control" which stresses the need for banks to have a system of country limits, to separate the marketing function from the limit-setting

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1/ The screening process is based on five ratios: current account deficit/exports (most recent year); current account deficit/exports (cumulative); reserves/imports; and exports/net interest payments; official debt service ratio. Countries are classified in three groups (top quartile of two of the indicators, top two quartiles of two of the indicators, and others) and detailed studies are conducted for countries identified through the screening process.

function, to relate the country exposure pattern to the total foreign indebtedness of borrowing countries and to the overall exposure of international banks as reported by the BIS.

While playing a quite positive role in forcing individual banks to improve their systems of country risk assessment, this growing involvement might reinforce the "herding" effect if all banks submitted to the same supervisor or if all supervisors adopted the same attitude toward a given country. There might be, in addition, a contradiction between the attitude of central banks stressing the need for commercial banks to maintain an adequate flow of international lending and the attitude of supervisors, a danger underlined by Mr. Volcker when proposing recently that, in assessing loans, supervisors take into account the adjustment efforts of problem countries, under IMF programs. Such a proposal could imply a greater involvement of the Cooke Committee in country risk assessment.

5. Through its overall approach to adjustment policies, stressing domestic imbalances as the source of future external imbalances, and its intimate contact with member countries through the consultation process, the Fund has played a fundamental role in the overall trend toward a better working of the country risk assessment process. Further progress could be contemplated in three areas:

a. Statistics: Comprehensive, timely, and accurate statistics are at the heart of an adequate country risk assessment process. The Fund should therefore in its consultation reports, describe more extensively the attitude of member countries to the release of information on domestic and external developments and, if necessary, insist in its programs on additional commitments to that effect. In addition, the Fund should contribute to a better knowledge of the external debt situation of member countries. Such is the purpose of the statistical project launched by the Bureau of Statistics aimed at a breakdown of debt between banks and nonbanks and at a reconciliation of data between creditor and debtor countries. The project deserves the highest priority since some recent cases have highlighted the deficiencies of the present reporting systems. It implies further cooperation between the Fund and the BIS.

b. Country risk assessment models: The Fund has always stressed the specificity of individual member countries and the need to take into account a diversified and interrelated set of unique economic, social, political, and external variables before passing any judgment on the viability of the balance of payments of any country and on its ability to service its external debt. Any temptation to move toward a purely mechanistic approach based on a computerized model or to rely, as an early warning system, on a set of predetermined and uniform indicators would thus run counter to Fund philosophy. To be sure, in terms of staff months, the input of the Fund in the economic analysis of any given country is probably 5 times the input of any of the largest banks and 20 times the input of any small bank. The reliance on rating systems or on early warning systems, while improving the intercomparability of country risk assessments, would be an unjustified mutilation.

Nevertheless, there is a case for having the Fund experiment with a country risk assessment model. The rationale for this can be found in the need to improve the Fund's ability to assess the likely attitude of bankers toward an individual country. Of course, their attitudes are not predetermined by numbers: the "herding" effect, marketing opportunities, and rates of return play a fundamental role, and the translation of country risk assessment into country limits remains the weak point in the present process. But a synthesis of individual country risk assessment systems would provide an objective and rational base for more sophisticated projections of private financial flows, with possible satellite models on regional contagion and on correlation between variables. It would need an in-depth study of industrial country risk assessment systems by leading banks in the United States, Japan, Canada, the United Kingdom, Germany, France, Switzerland, and one or two other European countries (about 25 banks representing about 50 percent of total international bank lending) for which some information is already available. On this study could be built a central country risk assessment model which would reflect a kind of weighted average of leading indicators as used by banks. It could be used, together with direct market indicators (spreads and maturities) as an early warning system of banks' attitudes toward a given country. As a by-product, it would give, at the Fund management level, an additional degree of intercomparability between member countries' external situations.

c. <u>Cooperation with supervisors</u>: There is a tendency toward a growing involvement of supervisors in country risk assessment, be it through the treatment of certain categories of loans or through the checking of a particular bank's exposure in a given country against the average exposure of all banks. The Fund could be more actively involved in actions under way to improve the coordination of national efforts in this field. Through adequate contacts with the Fund, which is already present as an observer in Berne Union meetings, the Cooke Committee could secure a greater degree of consistency between the attitudes of supervisors, central banks, and export credit agencies. Some recent cases show how delays on the part of supervisors and export credit agencies to adjust their negative attitude to the positive results of an adjustment policy can hurt a country in its recovery phase.

C. <u>Recent developments</u>

1. The international banking system was profoundly and lastingly hurt in 1982 by the conjunction of a series of events:

a. High real positive interest rates (on average in 1982 LIBOR exceeded the U.S. rate of inflation by about 8 percent), initiating a series of adverse developments for borrowers until then accustomed to automatic debt relief through inflation;

- bankruptcies or quasi-bankruptcies of large corporations in industrial countries (International Harvester, AEG, AM International, Dome Petroleum, GHR Company), most of them associated with losses in international lending;

- failures of banks or of financial intermediaries (Drysdale Securities, Penn Square Bank of Oklahoma, Banco Ambrosiano); these failures were due to large exposures to borrowers running into difficulties or to managerial errors in the assessment of collateral when energy prices were falling, or in the adaptation to a greater volatility of interest rates; and

- arrears or interruptions of payments by developing countries hurt by a deterioration of their terms of trade and by the impact on their exports of a worldwide recession and of specific protectionist measures after a period when, confronted with an increasing oil burden, they had delayed adjustment and rapidly accumulated external debt, thus building up a highly vulnerable debt and liquidity situation.

b. The impact on international bank lending of a series of political developments:

- escalated East-West tensions and martial law imposed in Poland in December 1981 which amplified in 1982 the trend toward an abrupt suspension of all new credits to Eastern European countries and toward a rapid reduction of existing exposure. This trend started in 1981 when the first rescheduling of the Polish debt made it clear that not only was there no Comecon umbrella, but that other Comecon countries were suffering from a contagion effect ("reverse umbrella theory"). The possibility of a formal default by Poland and the interruption of the Fund program and of debt servicing by Romania shattered the confidence of bankers and led to associated crises or near crises in Hungary, Yugoslavia, and to some extent East Germany;

- the South Atlantic crisis which highlighted the vulnerability of the external financial situation of Argentina and introduced a "Latin American syndrome," similar to the Eastern Europe syndrome, in which all major Latin American borrowers (Mexico, Brazil, Chile, Venezuela) were included; and

- the freeze on Argentine assets by the U.K. authorities which demonstrated that, in addition to political risks attached to the use of a given national currency (the freeze in 1979 of Iranian assets denominated in dollars), there were in interbank transactions political risks attached to the location of activities (the freeze in 1982 was applied to all Argentine assets in London, whatever their currency denomination).

c. The new funding patterns in the Euromarkets inducing a more cautious attitude by continental European bankers:

- the disappearance of OPEC surpluses in connection with the energy situation and the war between Iraq and Iran (US$3 billion of an identified deployed net cash surplus in the first half of 1982 against US$54 billion for 1981 as a whole and an overall decline in 1982 of OPEC deposits as reported by the BIS of about US$22 billion), which implied a greater reliance in the Euromarket on funding by the U.S. banks using their domestic dollar base. Thus, the U.S. net position in the Eurodollar market (the difference between sources and uses of Euro-currency funds of banks of BIS reporting European countries) which stood at US$33 billion at end-1981, rose to US$51 billion at end-June 1982 and US$61 billion at end-December 1982. This growing reliance on the U.S. domestic market was underlined by the growing proportion of credits including two tranches or a dual pricing, one based on LIBOR, one based on the U.S. prime rate; 1/

- the setting up, starting in late 1981, of "International Banking Facilities" (IBFs) located in the United States, mainly in New York, which amplified this trend. Initially, IBF deposits largely represented a repatriation of bookkeeping operations of U.S. branches in the Caribbean area, but in the wake of the South Atlantic crisis there was some additional shift, later partially reversed, from the London Eurodollar market to the New York market. More recently, political uncertainties on the future of Hong Kong have led to some shift from the Hong Kong/Singapore Asiadollar market to the New York market, a trend to which Japanese banks have contributed but which might be reversed by the setting up of an international banking facility in Tokyo. Overall, the growth of the IBFs has been more rapid than initially contemplated, from US$62 billion as of end-December 1981 to US$118 billion as of end-June 1982 and US$144 billion as of end-December 1982; and

- the growing perception of the risks attached to inter-bank funding which led European banks to protect their medium-term funding through the issuance of floating-rate notes, notwithstanding the additional cost, 2/ and to reduce maturity mismatching which, if they had been obliged through tiering to pay a premium on their resources, could well have led them to register heavy losses.

2. These adverse developments came to a head in July and August 1982. The handling of the Ambrosiano crisis by central bankers and especially the debate among the Italian, Swiss, and Luxembourg authorities on their relative responsibilities added to the overall uncertainty among Euromarket participants. The losses incurred by some large U.S. banks in connection with the Penn Square failure cast doubts on their management and led to a massive shift, notably by money market funds, from bank certificates of deposit to treasury bills and to the emergence of a tiering between U.S. banks themselves. The most serious blow came when in August 1982 Mexico, the largest single borrower (BIS banks' claims of US$62 billion), asked for a 120-day moratorium, later extended by 90 additional days, on its debt repayment obligations to banks. As had happened in the wake of the Herstatt crisis in 1974, sizable tiering reappeared on the interbank market, starting with a "Latin American premium" but spreading to other banks as well. As reported by

1/ While a LIBOR-related rate implies Eurodollar funding, a rate derived from the prime implies domestic dollar funding.

2/ This additional cost has, however, been reduced by the development of interest-swap transactions under which a bank may issue a fixed-rate bond and swap it against a floating-rate liability of another borrower.

Institutional Investor in July 1982, the tiering scale, taking prime U.S. banks as the base level, was as follows: 1/16 percent for prime U.K. banks and some large continental European banks; 1/8 percent for other large continental European banks and Japanese banks; 3/16 percent for many smaller banks; 1/4 percent for Latin American and Third World banks; and 1/2 percent for Eastern European banks. 1/ Since some banks were not ready to pay additional premiums, there was a net contraction of the London interbank market, which could have been the forerunner of a cumulative reduction of international lending and even of a worldwide banking crisis.

3. Central bankers and international organizations perceived the danger thus looming and took a series of measures which helped reassure the market:

- a shift in the U.S. monetary policy by the abandonment of strict reserve growth targeting, leading to a rapid decline of short-term U.S. dollar interest rates (for LIBOR from 15 percent in July 1982 to 9-10 percent at the end of the year);

- some monitoring by the Bank of England of banks' attitudes on the London interbank market, notably on transactions with London branches of Latin American banks; and

- joint action by the Fund, the BIS central banks, and commercial banks to handle the most acute cases in a coordinated way:

  - Hungary, where a commercial bank loan (US$260 million), a Fund program (US$500 million over three years, plus a US$80 million compensatory financing facility loan), and a BIS bridging operation (US$510 million) combined to avoid a liquidity crisis;

  - Mexico, where the announcement of a US$1.85 billion bridging loan by BIS banks (the first of its type for a non-BIS central bank) and the adoption of a Fund program (US$4 billion) paved the way for an agreement on a standstill by bankers and for an agreement on joint credits involving net new lending by commercial banks of about US$1.5 billion in 1982 and about US$5 billion in 1983;

  - Argentina, where the BIS granted a US$500 million credit facility while the Fund approved the use by Argentina of Fund resources totaling US$2.2 billion including US$1.6 billion under a stand-by arrangement; at the same time the central bank has proposed to take over about US$5 billion of private debts to be repaid after four or five years; and

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1/ On the Eurodollar CD market, which is, after the interbank market, the second largest external funding source available (with an established total size of US$90 billion against US$120 billion for U.S. banks' domestic CDs), the tiering was still larger. When compared with the rates obtained by the largest U.S. banks, other banks had to pay a premium of about 20 basis points (regional U.S. banks), and 40-60 basis points (Canadian banks, European banks, Japanese banks and some U.S. banks).

- Brazil, where a US$1.45 billion bridging loan from the BIS and use of Fund resources amounting to US$5.4 billion, including US$4.6 billion under the extended Fund facility, were combined with new short-term credits by banks in 1982 (US$1.2 billion) and a combination in 1983 of refinancing of maturities falling due, extension of short-term credit, reconstitution of interbank positions, and new money from commercial banks amounting to about US$6 billion;

At the same time, individual actions by borrowing countries to adjust their economies, improve their debt profile (Venezuela, through a series of medium-term operations, trying to re-fund short-term borrowings by public entities), or to come to terms with their bankers on rescheduling agreements (Poland, Romania) also contributed to some restoration of confidence in the marketplace. The joint action on Mexico was looked upon by many bankers as a turning point.

4. After the contraction of the London interbank market in the second quarter of 1982, there was indeed a resumption of its growth in the third quarter which offset this contraction.

In addition, the widespread fear that this contraction would lead to a marked contraction of international bank lending proved to be not well founded. Nevertheless, on the basis of the quarterly results, it appears that BIS banks' lending stood at end-1982 no more than 10 percent higher than at end-1981, a notable slowdown from previous trends (about 20-25 percent per year until 1980 and 17 percent in 1981). The slowdown was particularly characterized for transborder interbank claims (Table 6).

In particular, net lending to non-BIS countries registered a limited increase (US$2 billion) in the second half of 1982 with a quite limited increase of claims on non-oil developing countries (US$5 billion against US$28 billion during the second half of 1981) and a further reduction by US$1 billion of claims on East European countries (total cumulative decline in 1982: US$4 billion). 1/

Developments in the first quarter of 1983 confirmed this trend with new lending to non-oil developing countries amounting to US$1.6 billion against US$5.4 billion in the previous quarter), new lending to non-BIS developed countries amounting to US$300 million (against US$3-5 billion

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1/ It should be noted that a rather large discrepancy appears for the second half of 1982 between quarterly figures and semiannual figures. In particular, the semiannual figures released in July 1983 indicate an increase of international bank claims on non-BIS countries of US$22.6 billion for the second half of 1982 and of US$52.9 billion for the year as a whole, against US$12.5 billion and US$39 billion, respectively, for quarterly figures. As indicated in the BIS communiqué, these differences are due to a broader coverage of offshore countries and to the reallocation to individual countries of fairly large residuals contained in the quarterly figures. These differences should be kept in mind when assessing recent trends in the market.

Table 6. Claims by Banks in the BIS Reporting Area

(In billions of U.S. dollars)

	Changes					Amounts outstanding end-1982
	1981		1982			
	Full year	4th qtr.	First nine months	3rd qtr.	4th qtr.	
Interbank market						
Cross-border claims of reporting banks on one another 1/	153	63	98	49	20	938
Interbank claims in foreign currency within individual reporting centers (mainly London)	43	4	37	35	(-2)	283
Net international bank credit	165	55	95	25	20	1,020
Of which: to the non-BIS area	(65)	(24)	(39)	(4)	(9)	(491)

Source: BIS, Quarterly Report.

1/ Transborder claims between branches of the same bank are included in those figures. The trend toward a 24-hour market operating on a world basis, in spite of time zones, fuels the expansion of such intranetwork transfers of positions.

in the previous quarters), and a further reduction by US$1.4 billion of outstanding claims on Eastern Europe (putting the decline since the end of 1981 to about US$6 billion).

In addition, 1982 registered a sharp reduction of syndicated medium-term loans to non-oil LDCs, which was reflected by an increase from 41.4 percent at end-1981 to 42.2 percent at end-1982, of the proportion of short-term debt in individual countries' external debt, and a decline in banks' total undisbursed credit commitments from US$103 billion at end-1981 (21 percent of outstanding claims) to US$91 billion at end-1982 (17.2 percent of outstanding claims), adding to the vulnerability of the system. At the same time, there was a tendency to stress trade-related credit operations which, in the years to come, might adversely affect the availability of funds through syndicated Euroloans.

There is a feeling in the market that the rate of expansion of international bank lending might well be reduced by more than one half and stay well below 10 percent in future years. This would have an immediate impact on the financing of middle-income countries, which would have to adjust their economies accordingly, acting as a deterrent to a lasting and widespread recovery in the world. It is therefore of the utmost importance that international organizations, and particularly the Fund, expand their resources (through a quota increase and borrowing) to fill part of the gap. At the same time, the Fund should stand ready to help commercial banks remain active participants in the funding of external requirements of borrowing countries, a point stressed by the Managing Director in his November 1982 speech in Philadelphia when he said that "the Fund, as the agent of adjustment, and the banks, as the major source of international financing, have a vital and common interest in supporting efforts on the part of developing countries to tackle their balance of payments problems."

This implies that, in the months to come, the Fund should pay additional attention to the funding side of the market: the BIS study on the interbank market could be supplemented by a Fund study on non-BIS banks; there might be a reappraisal of the G-10 central banks' commitment not to place their reserves on the Eurodollar market; a fresh look might be taken in Fund consultations with major industrial countries at factors which through legal, informal, or supervisory requirements might impede adequate international bank lending. These analyses and a more direct perception of the banks' attitude on the lending side (country risk policy) would help the Fund to assess the attitude of commercial banks in the years to come and develop means to assist member countries in their debt management, to build constructive relations with commercial banks, and to handle potential crises in the system.

Part II. How to assist better member countries in the management of their external debt

1. As a counterpart to the rapid increase in international bank lending, the external debt of borrowing countries, and especially that of non-oil LDCs, has risen dramatically in recent years. As of end-1981, the total reported external debt of non-oil LDCs stood at US$440 billion (plus about US$100 billion of unreported short-term debt, mainly to suppliers and parent companies of subsidiaries) compared with about US$100 billion in 1973, that is, more than a quadrupling in eight years. To be sure there has been a rapid growth of exports, and the ratio of total external debt to exports has not increased as rapidly as the ratio of total debt to GDP. But since the origin of borrowed funds has shifted during the period from official sources to private sources 1/ with market-related variable interest rates, and since interest rates have increased sharply, there has been a rapid deterioration of debt service ratios (the ratio of interest plus amortization to exports standing at 20 percent in 1981 against 14 percent in 1973) and of the ratio of interest to current account receipts (11 percent in 1981 against 5.5 per cent in 1970). 2/ Repayment obligations will thus represent a growing proportion of gross external financing requirements, more than one half of gross external financing requirements of non-oil LDCs in the next five years (US$750 billion), according to a European bank internal study (in billions of U.S. dollars):

1/ The respective shares of official debt, debt to private banks, and debt to other private creditors were as follows (in percent):

	Official	Banks	Other private	Total
End-1973	50	35	15	100
End-1981	42	49	9	100

2/ According to the *World Economic Outlook*, the figures for total external debt on non-oil LDCs have developed as follows:

	1974	1978	1979	1980	1981	1982	1983 Proj.
Total outstanding debt (in billions of U.S. dollars)	162	337	392	460	543	594	645
Ratio of external debt to exports of goods and services (in percent)	103.5	130.2	118.3	110.1	122.0	137.4	136.9
Ratio of external debt to GDP (in percent)	21.6	28.6	27.2	26.8	30.3	33.7	33.7

	Five years 1977-81	Five years 1982-86	Difference
Net borrowing requirements	280	360	+80
Repayment obligations (medium- and long-term debt)	200	390	+190
Gross borrowing requirements	480	750	+270

Finally, the proportion of short-term debt in total debt has increased rapidly (it represented 44 percent of banks' claims on the 20 largest borrowers as of end-1981 against 39 percent as of end-1970--see Table 7). 1/ This means that, in addition to gross borrowing requirements, there is a growing need to roll over short-term debt (about US$200 billion for non-oil LDCs), thus adding to the total gross borrowing requirements of non-oil LDCs and to the vulnerability of the overall system.

2. During the last ten years, the international monetary system has shifted from an "assets settlement system" to a "liabilities settlement system" in which reserve creation takes place through the expansion of international bank lending and where adjustment is forced on countries by constraints on the liabilities side of their balance sheets. This means that countries, and the Fund in its relations with member countries, have to pay growing attention to external debt management. Recent trends in the market have reinforced this necessity since crises are no longer exclusively related to the judgment passed by creditors on the adequacy of policies and the creditworthiness of a given country but may be initiated by "contagion" effects, which will have a more immediate bearing on countries that have made themselves vulnerable to external shocks by inadequate reserves and external debt management. Clearly the situation of each individual country is unique and its debt management should be tailored to its medium-term balance of payments prospects, its banking and industrial structures, and its access to alternative sources of funding. Some general lessons may, however, be drawn for the roles of central banks and of the Fund, from the experience of five borrowing European countries at various stages of their debt cycle.

A. The experience of five European countries

A borrowing country normally passes through three phases in its debt management cycle:

(i) a phase of rapid expansion when credits are available, with a growing proportion of short-term debt as borrowing requirements increase and doubts on the debt service capacity spread;

(ii) a phase where medium-term credits are no longer available and short-term credits are not renewed; a crisis phase, overcome either through severe adjustment, or through a debt rescheduling, or both; and

1/ Source: BIS, semiannual reports.

Table 7. Indebtedness of Major Borrowing Countries to BIS Reporting Banks, 1978-1981 1/

(In billions of U.S. dollars)

Country	Mid-1978: Total banking debt	Mid-1978: Of which: Debt with a residual maturity of up to one year	Mid-1978: Percentage share of short-term debt in total banking debt	End-1979: Total banking debt	End-1979: Of which: Debt with a residual maturity of up to one year	End-1979: Percentage share of short-term debt in total banking debt	End-1981: Total banking debt	End-1981: Of which: Debt with a residual maturity of up to one year	End-1981: Percentage share of short-term debt in total banking debt	Memorandum item: Exchange reserves as percentage of short-term debt at end-1981
Mexico	21.0	7.8	37.1	30.9	10.7	34.6	56.9	27.7	48.7	13.4
Brazil	27.6	8.0	29.0	38.6	11.3	29.3	52.7	18.3	34.7	32.2
Venezuela	11.4	6.4	56.1	20.8	11.7	56.3	26.2	16.1	61.5	44.1
Argentina	6.1	3.0	49.2	13.4	6.9	51.5	24.8	11.6	46.8	22.4
Chile	2.3	1.1	47.8	4.9	2.0	40.8	10.5	4.2	40.0	73.8
Subtotal Latin America	68.4	26.3	38.5	108.6	42.6	39.2	171.1	77.9	45.5	28.8
Spain	12.8	4.9	38.3	16.9	7.1	42.0	23.2	9.3	40.1	109.7
Norway	8.3	2.4	28.9	9.7	2.8	28.9	10.7	3.9	36.4	148.7
Yugoslavia	4.8	0.8	16.7	8.2	1.9	23.2	10.7	3.0	28.0	50.0
Greece	4.9	1.9	38.8	6.2	2.5	40.3	9.8	3.6	36.7	22.8
Portugal	2.3	1.3	56.5	4.1	1.3	31.7	7.5	2.8	37.3	12.9
Finland	4.7	2.1	44.7	6.0	2.6	43.3	7.3	4.1	56.2	29.3
Subtotal Western Europe	37.8	13.4	35.4	51.1	18.2	35.6	69.2	26.7	38.6	25.7
South Korea	6.1	3.5	57.4	12.0	6.7	55.4	19.9	11.5	57.8	22.6
Philippines	4.3	2.2	51.2	7.4	3.9	52.7	10.2	5.8	56.9	37.9
Australia	4.3	2.3	53.5	6.6	2.5	37.9	9.9	4.0	40.4	32.5
Subtotal Far East	14.7	8.0	54.4	26.0	13.1	50.4	40.0	21.3	53.3	28.6
U.S.S.R.	12.8	6.0	46.9	13.0	5.0	38.5	16.3	8.2	50.3	106.1 2/
Poland	10.7	3.6	33.6	15.8	6.2	39.2	15.3	5.5	35.9	14.5 2/
Germany, Dem. Rep. of	6.0	2.8	46.7	8.6	3.7	43.0	10.7	4.6	43.0	42.8 2/
Hungary	5.7	3.1	54.4	7.9	3.8	48.1	7.7	3.1	40.3	29.0 2/
Subtotal Eastern Europe	35.2	15.5	44.0	45.3	18.7	41.3	50.0	21.4	42.8	58.9 2/
South Africa	8.3	4.0	48.2	7.3	2.8	38.4	11.2	6.0	53.6	6.7
Algeria	6.0	1.2	20.0	9.0	1.3	14.4	8.4	1.5	17.9	226.7
Subtotal Africa	14.3	5.2	36.4	16.3	4.1	25.2	19.6	7.5	38.3	50.7
Total of countries listed	170.4	68.4	40.1	247.1	96.7	39.1	349.9	154.8	44.2	42.1

Source: BIS, quarterly report.

1/ The countries shown in the table are the reporting banks' 20 largest gross debtors outside the BIS reporting area as at end-1981. In the case of the German Democratic Republic, data do not include debt to banks in the Federal Republic of Germany.

2/ For these countries, no data on exchange reserves are available. The figures therefore show their total deposits with the BIS.

(iii) a phase in which creditworthiness is restored, usually some years after the crisis, and the country gradually regains access to the market.

During the course of the present study, special missions were devoted to five European countries at varying stages of this cycle: Portugal, in a phase of rapid expansion of its debt; Turkey, which, after a major debt crisis, is re-entering the market; Romania, moving out of the second phase with the help of severe adjustment measures and debt rescheduling; and Hungary and Yugoslavia, which both faced severe external liquidity strains. The findings of these special missions may be summarized as follows:

1. Portugal

In 1978-79 Portugal was able to implement a Fund program successfully, but since 1980 it has registered growing deficits on current account, which explains stabilization efforts being implemented by the new Government.

	1976	1977	1978	1979	1980	1981	1982	1983 Proj.
Deficit on current account (in billions of U.S. dollars)	-1.3	-1.5	-0.8	--	-1.3	-2.8	-3.2	-2
(in percent of GNP)	(8)	(3)	(5)	(--)	(5)	(11)	(13)	(9)

As far as past policies are concerned, the success of the Fund program against the skepticism of many external advisors is a lasting example for other countries at a comparable stage of development. It shows how adequate exchange rate incentives can rapidly affect export and import trends, how a decline in real wages induced by price developments associated with a devaluation can allow a rapid transfer from domestic demand to external demand, how an appropriate interest rate policy can modify attitudes toward savings and toward the building up of inventories of imported goods, and how a credible preannounced policy on exchange rates may induce a resumption of workers' remittances and stabilize external financing flows.

Conversely, recent developments in Portugal show the limits of the role of the Fund when readily available external financing is at hand. The large gold stock which reassures bankers, the integration of the Portuguese banking system in the European banking system, and the growing "regionalization" of the international market making all West European borrowers relatively attractive combined to allow a rapid rate of increase of external debt to banks. Financing the deficit in the public sector by borrowing abroad adds to the country's debt service burden without necessarily contributing to the growth of its debt servicing capacity, and the widening of the current account deficit through ever larger interest payments adds to borrowing requirements and thus to the future debt service.

Fundamentally, the deterioration of the public sector situation is at the heart of the overall imbalance of the economy: its growing deficit feeds the external deficit which has to be financed. But, in addition, a too automatic access by various entities to external borrowing eliminates any built-in incentive to reduce the current account deficit. Portuguese banks have been able to borrow dollars on the London and New York interbank markets, relending them in short-term credits to Portuguese borrowers. The prescription by the Portuguese authorities of minimum proportions of foreign financing (all imports of crude oil and essential goods have to be financed by external credits) has contributed to the buildup of a significant external short-term debt by the public enterprises in charge of oil, cereals, and oleaginous imports. The Bank of Portugal has established a regulatory framework to monitor new indebtedness, but there is a natural tendency to roll over short-term debt falling due, thus contributing to a deterioration of the debt profile (with short-term debt now representing 30 percent of total debt, in spite of Portugal's continuous access to medium-term syndicated loans).

The new Portuguese Government is aware of this situation and is presently undertaking a program of adjustment. Strict standards for external debt management will have to be an integral part of such a program. They would constitute a valuable precedent for other countries at a comparable stage of development.

2. Turkey

In 1977-80 Turkey faced a highly critical debt situation which required massive debt reschedulings by official creditors and commercial banks, emergency aid by OECD countries, and successive adjustment programs. Starting in 1980, Turkey reversed its policy stance, making a deliberate shift toward a more market-oriented economy under a three-year stand-by arrangement with the Fund, and succeeded in gradually restoring its current account deficit to a more sustainable level. It is now entering the phase of re-entry into the international credit market, which will require some additional Fund assistance:

	1976	1977	1978	1979	1980	1981	1982	1983
Deficit on current account (in billions of U.S. dollars)	-2.3	-3.4	-1.5	-1.7	-3.7	-2.3	-1.2	-0.6
Debt relief			+0.3	+0.9	+1.5	+0.8	+0.8	+0.9

The debt crisis of 1977-79 was largely due to inadequate adjustment policies but clearly poor debt management and the attitude of bankers contributed to the acuteness and the duration of the crisis: the buildup of an unsustainable level of short-term debt through the unsound convertible Turkish lira deposit (CTLD) scheme; 1/ inadequate information on the debt situation; the prolonged negotiations on the rescheduling agreement; and the exclusion from the rescheduling of large acceptance credits which had to be repaid at a time of major external constraint. The Fund, which could have stated more explicitly in its consultation reports the dangers associated with external debt management in 1973-77, was also less involved in debt rescheduling negotiations than in subsequent negotiations. This might have contributed to the inadequacy of their end-result, at least as far as the initial agreement was concerned.

During the period 1979 to 1981 external debt management did not play a major role since short-term trade-related credits were not resumed until 1982. But it is again one of the major components of the present overall economic strategy. The Fund program has been a success: a rapid export growth induced by the adjustment of the exchange rate contributed to a GNP growth of 4-4.5 percent in 1981 and 1982; a rapid increase in workers' remittances in connection with the freeing of interest rates occurred; a sharp reduction of the rate of inflation took place in spite of some slippages in the implementation of monetary policy; and there were improvements in the financial situation of the State Economic Enterprises.

In view of the resumption of large debt service payments in 1985 and the reduction of foreign aid, Turkey will have to continue to adhere to tight demand management policies and to restore its ability to tap medium-term credit markets. Turkey first approached the market in 1982 with some medium-term financing for the acquisition of airplanes, for the prefinancing of agricultural exports, and with the help of IFC for the financing of Turkish building companies' activities on foreign markets. But clearly Turkey has to strengthen the financial basis of its industrial groups and of its banking system (whose fragility was displayed by the Kastelli crisis) if it is to re-enter the market in a more substantial way. Through technical assistance to the Central Bank and through policy measures, within the stand-by program, aiming at a modification of financial instruments, the Fund should play a role in this process. Further involvement by the Fund could be associated with medium-term bank financing which could be channeled through a "cofinancing" approach in which discussions among the Fund, a group of leading banks, and the Turkish authorities would yield a common assessment of needed financial

1/ Convertible Turkish lira deposits (CTLDs) were deposits of foreign banks with Turkish banks, denominated in Turkish liras, and benefiting from the high interest rates, but with an exchange rate guarantee (principally in deutsche mark and Swiss francs) given by the Central Bank of Turkey. These deposits, which enabled foreign bankers to obtain an effective interest return of 20 percent on Swiss franc deposits, were marketed to over 200 foreign banks and stood at US$2.3 billion in August 1979.

flows in 1983-84, a precise timetable for various types of credits (including trade credits through adequate consultation with Berne Union members), and possibly an agreement on phasing.

3. Romania

Romania is presently in a phase of emergence from a debt and liquidity crisis comparable to the Turkish crisis of 1977-79. After a period of rapid economic growth fueled by a large investment program conducive to growing current account deficits and a rapid buildup of its external debt, 1/ Romania was hurt by the interruption of foreign short-term credits in the wake of the Polish crisis. It had to enter into agreements with its creditors for the rescheduling of its debt falling due in 1982 and 1983 and to implement a massive domestic adjustment, under a Fund stand-by arrangement, aimed at a surplus on current account.

	1976	1977	1978	1979	1980	1981	1982	1983
Current account in convertible currency (in billions of U.S. dollars)	-0.1	-0.3	-0.3	-1.7	-2.4	-0.8	+0.6	+0.8

Clearly the large deficits of the 1978-80 period were induced by shortcomings in the management of the domestic economy: a too rapid rate of expansion; a much too ambitious investment program; the difficulty for a heavily centralized economy to adjust rapidly to external developments; and an inadequate energy policy contributing to a shift from a net oil exporter position to a net oil importer position and to the perpetuation, during this period, of unprofitable processing and petrochemical activities.

But these difficulties were compounded by inadequate external debt and reserves management: a low level of foreign exchange reserves representing only four to five weeks of imports and less than 25 percent of short-term external debt; an inadequate flow of information; insufficient monitoring of short-term buyers' credits; the use of interbank short-term credits, notably through consortium banks in Paris and London, to avoid the cost of medium-term borrowings at a time when they could have been obtained; and an inadequate maturity profile with a high proportion of short-term debt and a peak of repayments in 1981. Thus, when the situation deteriorated in the second half of 1981, there was a built-in

1/ Among Comecon countries (see annotated bibliography) Romania was characterized by a high level of external debt in relation to GDP (18.4 percent at end-1980 against 20 percent for Hungary, 18 percent for Poland, and about 10 percent or less for the others). Due to the large oil processing trade, the ratio of debt to exports (217 percent against an average of 274 percent for Comecon countries) and of debt service to exports (21 percent) was less unsatisfactory.

vulnerability which was aggravated by delays in the opening of the discussions with bankers which were clearly needed. Finally, in the second half of 1982, the Romanians reached an agreement on debt rescheduling with governments (US$0.3 billion), excluding, however, officially guaranteed short-term debt which was US$0.2 billion, Arab and Moscow banks (US$0.4 billion), commercial banks (US$1.5 billion), and suppliers (US$0.6 billion)--all on comparable terms (80 percent of debt falling due rescheduled and a repayment period of six and a half years with a three-year grace period). Except for a larger down payment (40 percent against 20 percent in 1982), Romania was able to obtain similar terms for the rescheduling of the debt falling due in 1983. But credit lines have now been cut by bankers all over the world and normal banking operations are unlikely to be resumed on a significant scale for the foreseeable future.

The Fund, for its part, faced a dilemma in drafting its adjustment program for Romania, as for other centrally planned economies. Either it used the standard instruments such as credit ceilings which had a limited meaning, or it relied upon the instruments used by the country itself, with no built-in incentives to move in the direction of more market-oriented mechanisms. The use of external quantitative criteria was a substitute for other criteria, but may have appeared to financial markets as not putting sufficient emphasis on the needed internal changes. In addition, with hindsight, it was unfortunate that the Board approved the stand-by arrangement in June 1981 at a time when more intimate contacts with bankers would have already revealed the existence of arrears. All bankers, however, praised the role played by the Fund staff in the 1982 negotiations of the rescheduling agreement, which might constitute a model for the role of the Fund in other countries.

If Romania is to restore its ability to attract capital flows and return to a more adequate medium-term growth path after a period of severe adjustment from 1981 to 1984, it will have to continue to implement fundamental changes. In association with the World Bank, the Fund should therefore stress the need for profound changes in the financial system through decentralization, in the foreign trade system through the revision of the role of foreign trade enterprises and a move toward multilateral trade relations, and in the productive sector by a decentralization of decisions on prices and investments. Such a process should be an integral part of an overall strategy aiming at a more balanced, more diversified, and more market-oriented economic policy.

4. Hungary

Since 1979 Hungary has been pursuing an adjustment policy aiming at reducing its current account deficit. But in the wake of the Polish crisis in 1982, it faced a severe liquidity shortage and had to adjust its economy more severely under a Fund-supported program:

	1977	1978	1979	1980	1981	1982	1983
Current account in convertible currencies (in billions of U.S. dollars)	-0.8	-1.2	-0.8	-0.4	-0.7	-0.1	+0.6

The 1982 crisis was largely the result of debt management in previous years. Since 1968, with some setbacks from 1974 to 1978, Hungary had been moving in the direction of a more market-oriented economy with a view to replacing plan directives by market relations among firms, limiting the scope of central price determination, linking the domestic prices of exports and imports to world market prices, and decentralizing a major part of investment decisions. But these efforts had not affected the financial system which remained totally centralized, the central bank performing all the functions of a commercial bank and most of the functions performed in other similar countries by foreign trade banks. This centralization was reflected in the overall debt structure. The high level of external debt was in itself bound to lead to difficulties: the ratio of debt to exports was 240 percent (against 333 percent for Poland, 223 percent for the German Democratic Republic, and less than 200 percent for other Comecon countries); the ratio of debt to GNP was 20 percent (against 18 percent for Poland and Romania, and 10 percent or less for the others); and the debt service ratio (35 percent in 1981) was one of the highest among Comecon countries. But the looming difficulties were compounded by the structure of the debt: the policy of the National Bank was to prohibit direct uses of suppliers' credits by industrial firms except under highly concessionary terms, and to limit the use of documentary credits. It relied entirely on financial credits, notably syndicated loans, bank-to-bank credits, and deposits of non-resident banks, with some associated advantages in terms of spreads and currency composition. But this policy contained a built-in vulnerability to a change in the attitude of Western bankers, which materialized in 1982 when the withdrawal of short-term foreign deposits began.

A coordinated action by the BIS (US$510 million), the Fund (a US$520 million stand-by plus a US$80 million compensatory financing facility loan), and commercial banks (a US$260 million three-year loan syndicated by Manufacturers Hanover) avoided a major debt crisis in 1982. However, commercial arrears accumulated from time to time; they peaked at about US$170 million in the middle of the year but were eliminated by December. The well-coordinated approach between the BIS, the Fund, and commercial banks can be considered as a model for other collective actions: a short-term facility in the BIS, based on immediate action on the exchange rate and interest rates and an assessment that negotiations with the Fund on an adjustment program were likely to succeed; intimate contacts between the Fund and commercial banks; and a lead given to other commercial banks by a group of major banks. Nonetheless, the situation remains fragile: the debt service burden remains high through 1985; the level of reserves is currently low; and the attitude of commercial banks has improved only moderately. Present policies under the Fund program are consistent with a current account surplus compatible, under normal circumstances, with foreseeable capital flows.

Hungary re-entered the international capital market with a US$200 million three-year loan syndicated in April 1983 and has started to address, in collaboration with the Fund and the World Bank, some fundamental issues. These issues include a transformation of the banking system to diversify the channels of savings, invetment financing, and external borrowing; a more direct relation between the domestic economy and the external environment, to encourage suppliers' credits and project financing; and a new approach to the use of macroeconomic policy instruments to ensure the effectiveness of changes in the exchange rate and interest rates.

5. Yugoslavia

After a period of rapid growth from 1970 to 1977, Yugoslavia had to adjust its economy. The widening gap between domestic production and demand and the associated inflationary pressures made it necessary to shift to restrictive demand management policies associated with Fund programs, currently a three-year stand-by arrangement (1981-83):

	1977	1978	1979	1980	1981	1982	1983
Current account in convertible currency (in billions of U.S. dollars)	-1.0	-1.3	-3.3	-2.2	-1.8	-0.2	-0.7

Unfortunately, the measures taken proved to be insufficient in 1982 when the shift in the commercial banks' attitude toward East European countries materialized. Even in 1981, Yugoslavia had been unable to raise on the market the medium-term syndicated credits it had been contemplating and had to rely on a rapid growth of short-term indebtedness. The vulnerable liquidity situation was compounded by the overall inadequacy of the foreign exchange and external debt management systems: inadequate supervision of the Yugoslav commercial banks which entered into massive foreign borrowing; inadequate handling of the foreign exchange assets of Yugoslav citizens, who were entitled to hold freely usable foreign currency deposits with Yugoslav banks; and inadequate pooling within the system, with foreign relations decentralized at the level of individual republics monitoring their own balance of payments. In the absence of a national foreign exchange market, each bank had to rely on its own foreign exchange resources. The whole system was therefore dependent upon a continued increase in external borrowing by those banks that were actually running a foreign exchange deficit.

Privredna Bank Zagreb (PBZ), which was engaged in the financing of a several major projects and which was financing a large part of oil imports of Yugoslavia, turned out to be the weakest element in the financial system. To meet its external obligations in 1981, PBZ had to engage in short-term foreign borrowing, mainly on the interbank market. These credits were not renewed and PBZ had to repay in 1982 its normal 1982 obligations plus short-term credits obtained in 1981. It ran into arrears and delays of payment seriously harming the image of Yugoslavia in the world banking community.

To overcome the crisis, a series of measures was adopted: better pooling of foreign exchange and greater control by the National Bank of foreign borrowing; reinforcement of restrictive demand management policies associated with wage and price controls; devaluation of the dinar and increases in interest rates; and restrictions on the use of foreign currency deposits. But, in spite of a deal arranged with Arab banks for the financing of oil imports (US$100 million), a syndicated loan managed by a group of American and Japanese banks led by Citibank of New York (US$200 million), and the extension of additional trade-related credits by German, French, Italian, and Austrian banks, the inflow of private capital was insufficient to enable Yugoslavia to meet its repayment obligations, which were amplified by the withdrawal of short-term credits and deposits.

Yugoslavia drew down its already depleted reserves and asked the BIS to step in with a US$500 million medium-term facility. Since the BIS was unable to arrange such a facility, there was a need to obtain pledges of governmental assistance by OECD countries, which could be prefinanced. In January 1983, the Fund succeeded in obtaining commitments to that effect by major OECD countries (US$1.3 billion) which, supplemented by an agreement with commercial banks to roll over short-term debt, to refinance longer-term debt maturing in 1983, and to grant US$600 million as medium-term "fresh money," and by a US$500 million BIS credit, would allow Yugoslavia to meet its commitments in 1983.

Although a general rescheduling operation has been avoided, there remains a need to address the medium-term debt problems of Yugoslavia. There is a good case for an innovative approach under which, in connection with the pledging of governmental assistance, foreign banks, in addition to the refinancing of debt already agreed for 1983, would agree to negotiate the partial restructuring of the debt of certain Yugoslav entities. Such an approach would help to restore Yugoslavia's borrowing capacity and would introduce some discipline into the marketplace. The ratios of foreign exchange borrowings to total liabilities or to foreign assets of a bank like Privredna Bank Zagreb were totally out of line with the corresponding ratios of other Yugoslav banks. Foreign banks should have been aware of the risks attached to this structure and should be prepared to correct this midjudgment, a line of reasoning that is valid for other heavily indebted Yugoslav entities.

In any event, Yugoslavia is faced with a prolonged period of adjustment of its economy. During this period, the Fund should stress the need to help restore Yugoslavia's creditworthiness by structural measures in the field of debt management: strengthening of the financial structures by the merger of some banks; development of a unified foreign exchange market and modernization of monetary instruments; and a move toward project financing and greater use of suppliers' credits. At the same time, the Fund should, in its discussions with the World Bank, emphasize the need to postpone the graduation process presently contemplated.

6. Common features

Clearly the experience of each individual country is unique and the lessons to be drawn from debt management in five European countries are not immediately applicable to other countries in another area or at another stage of development. Nevertheless, some conclusions may be drawn from these experiences. In particular, there is a need:

- to diversify the types of borrowers and the types of borrowings to reduce vulnerability risks, and, to that effect, to strengthen the financial viability of potential borrowers;

- to introduce some form of centralized monitoring of external debt, based on adequate information, aiming at a sustainable debt burden, a viable debt maturity profile, and a manageable liquidity position where foreign exchange reserves are compatible with possible adverse developments in the short-term debt; 1/

- to obtain greater discipline in the international marketplace to avoid unsound banking schemes, such as CTLDs in Turkey, unsound interbank lending without adequate attention paid to individual risks, and the destabilizing alternation of overlending and abrupt cuts of existing credit lines; and

- to envisage greater involvement by central banks and the Fund to help reduce vulnerability, improve the assessment of financial flows, 2/ and obtain a more orderly process.

B. The role of central banks

The debt crises of 1982 have underlined the need to strengthen and stabilize the system of liability settlement through improved debt management. Central banks of both debtor and creditor countries, through their monitoring of bank lending and borrowing, should be the key actors in this collective endeavor.

1/ As mentioned by the World Bank, efforts in the direction of a better monitoring of private sector external debt have, however, to be balanced against the need, in an export-oriented development strategy, to strengthen the ability of the private sector to mobilize directly the financial resources it requires.

2/ There is in particular a need for better knowledge of financial flows among Comecon countries and between oil producing and oil consuming countries (oil trade financing patterns). In addition, a compara-- tive study of the various schemes by which countries attract remittances from their expatriate workers would help the countries concerned.

1. Debtor countries

Central banks in many borrowing countries are playing a limited role, dominated as they are by governments in the decision-making process and, in some countries, by private interests and private banks in the implementation of monetary policy. Yet they have an essential role to play in external debt management and the Fund should try to help them to fulfill their responsibilities better.

This implies, first of all, a strengthening of their ability to monitor external financial relations: a centralization of foreign exchange proceeds through market transactions or compulsory requirements; a comprehensive system of external debt reporting by individual corporations, banks, and public entities; and a system of authorization for borrowing operations, either by approving individual transactions or by setting ceilings by categories of external debt for each borrowing entity. These debt and foreign exchange monitoring instruments should be used to obtain a better debt maturity profile and a better balance between short-term assets and short-term liabilities. Adequate release of information and, if and when needed, partial refunding operations, should be an integral part of this active external debt management policy.

For middle-income countries with a diversified network of foreign commercial and financial relations, arriving at a more effective external debt management policy cannot be dissociated from overall efforts to adapt financial instruments and policies to external developments: realistic and predictable exchange rate policies; realistic interest rate policies; diversified savings instruments and diversified channels for financing investment; and improved liquidity control by setting up a foreign exchange market and a money market.

Finally, there is a need to strengthen the supervisory capacity of central banks in borrowing countries. Interbank transactions are an essential part of the external debt picture and the maintenance of confidence in these transactions should be a fundamental objective of the central banks of borrowing countries. It is clear, for instance, that the bankruptcy of Banco Intercambio in 1980 had adverse consequences for the overall credit rating of Argentina. Central banks of borrowing countries should be seen by the market as being ready to act as lenders of last resort and to impose on individual banks the discipline of solvency and liquidity requirements. For countries with a diversified export-oriented industrial base, it should also include adequate monitoring by the central bank of net creditor positions of individual commercial banks. The exposure of some middle-income developing country banks involved in recent rescheduling negotiations underlines the need for central banks in large developing countries to join the central banks in creditor countries in their efforts to strengthen their analytical capacity and their instruments of action in the field of country risk assessment and transborder lending.

2. Creditor countries

Efforts under way among BIS central banks to coordinate and improve supervisory capacities in the field of international bank lending are a key element in an overall strategy aiming at better control of external debt developments in borrowing countries and greater stability in the system as a whole avoiding the alternation of phases of overlending and underlending. To that end, the Cooke Committee has launched studies or reached conclusions in several interrelated fields: consolidation (a matter dealt with at the same time by the contact group and the advisory committee within the European Community); solvency and liquidity ratios; country risk assessment; early warning systems (an idea now discarded); and information flows. In addition, through international conferences in 1979 (International Conference of Banking Supervisors, London), 1980 (meeting with central banks of offshore centers, Basle), and 1981 (International Conference of Banking Supervisors, New York), the Cooke Committee tried to spread its doctrine to nonparticipant central banks and supervisors, especially in offshore centers, thus strengthening the overall monitoring system. In view of recent developments, there seems to be a need to address more explicitly three specific issues: the interbank market, unsound banking practices, and provisioning.

a. A study group of the standing committee of the BIS on international capital markets has prepared a report on the interbank market for consideration by the Governors. This was a most welcome initiative since interbank transactions are the weak element of the integrated network of transborder financial relations. There is a need for a better flow of information on interbank transactions, particularly through offshore centers. There is a need for requirements by supervisors in the main financial centers of a sufficient portfolio diversification of borrowing countries banks' branches or subsidiaries, so as to avoid them acting as a mere channel for balance of payments loans to their home country. There is a need for a more sophisticated interbank risk analysis system: capital adequacy requirements for the lending and borrowing banks; incentives for lending banks to "look through the balance sheet" to the final destination of funds; better integration of interbank limits within country limits; and immediate information on the effective use of interbank lines of credit.

b. The interference of supervisors with individual bank practices runs contrary to the basic philosophy of many central banks. But a scheme like the CTLD scheme in Turkey, which offered foreign currency-denominated claims at domestic interest rates, was basically unsound and supervisors should have acted earlier to put an end to it.

c. Finally, there is a need for sanctions for inappropriate bank lending. All debt crises have been amplified by excessive lending in preceding years and especially by a rapid growth of short-term debt compared to total debt or foreign exchange reserves of which banks should have been aware through BIS reports. Clearly, the avoidance of default is vital to the overall functioning of the system, and this explains why country lending does not have the same built-in disciplines as corporate lending. Clearly also, the system as a whole should stress the need for borrowing countries, under all circumstances, to keep current on their interest payments. Hence, the only instrument by which some discipline, through prospective losses, can be imposed on banks is the prescription of provisions on claims on countries running into major debt crises. It is most probable that Poland will not be able to repay the principal of its debt under the terms of the rescheduling agreements that have been signed and in many creditor countries, subject to the position of the tax authorities, banks have made corresponding provisions, but a more orderly process coordinated by central banks within the Cooke Committee would be justified. 1/ Of course, at a time when there is a risk of a contraction of the overall bank lending system, steps should be cautious and balanced by a positive approach by supervisors to countries accepting an adjustment program under the auspices of the Fund, but a move in this direction would strengthen discipline in the marketplace and contribute to a better handling of external debt development.

C. The role of the Fund

The Fund, through its annual consultations and its policies on the use of its resources, should contribute to this overall process aiming at a better external debt management.

1. Consultation reports should stress more the external liquidity situation, the structure of the external debt, and the vulnerability to external shocks. In many instances, the staff had early knowledge of potential threats and called the attention of the authorities to the risks attached to debt developments, but these views were not fully reflected in the consultation reports. Many Executive Directors with whom discussions were held in the course of this study, stressed the same point for other countries, such as Mexico. To be sure, it is not that easy for the Fund to appear to impair by its comments the creditworthiness of a member country, but such comments form part of its surveillance functions in a liabilities settlement system. To avoid any appearance of discrimination between member countries, comments could be made under a standardized format used in all consultation reports. A special section, "External debt and external liquidity situation," could include the following subsections:

- debt structure: the various types of borrowers and the various channels of borrowing; the external situation of banks, with a specific reference to their capital adequacy, their debt situation, their use of the interbank market and their supervision by the central bank; the external situation of enterprises with a specific reference to trade-related credits and their maturities; the debt maturity profile and its likely development in the future; and the availability of information on the debt structure;

1/ An alternative course of action would be, at least for central banks relying on a capital adequacy ratio between capital and weighted assets, to give greater weight (and thus a larger capital requirement) to problem sovereign loans.

- access to capital markets: recent developments in syndicated loans raised by the country with a comparison between their spreads and maturities and average spreads and maturities on the market, as an indicator of the market's perception of the creditowrthiness of the country; an indication of the lead managers in such syndicated loans, as a reference for future contacts if needed; a description of any collateral or negative pledges offered to lenders; and a reference to relations with the World Bank and the IFC, especially for countries for which graduation is contemplated; and

- liquidity situation: adequacy of freely usable reserves; 1/ existence of unused lines of credits; and evolution of the principal ratios of the "country balance sheet": external short-term debt/reserves or reserves plus unused credit lines; short-term liabilities/total liabilities; debt service ratio; gross borrowing requirements, including the rollover of short-term debt in each of the five coming years; and vulnerability to external shocks.

2. Stand-by arrangements normally include a reference to external debt, frequently with ceilings on medium- and long-term borrowing. As mentioned by many central bankers and commercial bankers, the accumulation of short-term debt might thus have been encouraged under the assumption, no longer valid, that short-term debt is trade related. A gradual change in Fund policies is already under way and in some instances ceilings covering all maturities or specific ceilings on short-term debt have been set as performance criteria. This should become a more standard element of Fund programs probably under the form of adequate "balance sheet" ratios, to some extent derived from covenants in corporate lending.

3. Technical assistance by the Fund and/or the World Bank is a fundamental element in an overall process aiming at a better external debt management. It is an area where, in the view of many people encountered in the course of the mission, improvements are possible and desirable. Such was the purpose of the staff working group set up in July 1982 to "survey technical assistance to countries in the external debt area and to make recommendations concerning an expansion of the Central Banking Department (CBD) activities in this area." Its conclusions were presented in its October 1982 report. Leaving aside the role of the Fund in debt rescheduling negotiations, a subject dealt with below, these recommendations are commendable and should be implemented. This will require adequate staffing of the CBD or adequate hiring of external consultants, expansion of CBD technical assistance in the field of external debt statistics, in consultation with the IBRD External Debt

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1/ In discussions with some banks and in some countries, it appeared that the concept of foreign exchange reserves was blurred because there may be commitments to maintain a certain level of reserves as deposits in specific banks, formal pledging agreements of reserves against short-term credits, or gold swap agreements involving some double counting of reserves. This is an area in which the Fund, after a more detailed study, could try to elaborate more precise standard definitions.

Division, 1/ and the establishment of a permanent external debt management machinery, including statistical reporting, control and approval procedures, and a medium-term debt policy. There is, in addition, a need to strengthen the ability of the CBD to provide technical assistance in the field of bank supervision, where certain initiatives have already been taken. The seminar on central banking held by the Fund in July 1982 was a most welcome initiative, paving the way for added involvement of the Fund, in cooperation with the BIS, in bank supervision in non-BIS member countries and the budget proposals for 1983 included a specific reference to the role of the Fund in helping central banks to strengthen the role, functions, and capacities of their commercial banks. But a new impulse must be given to these endeavors, because of the growing role of interbank transactions and thus of the need for a sound, effective, and well-monitored banking system. In consultation with the World Bank and the IFC, there is scope for an extension of CBD technical assistance activities in bank supervision and in the setting up of foreign exchange markets, financial markets, financial instruments, and banking institutions designed to develop an adequate base for external borrowings by commercial banks, a logical step for countries entering or re-entering the international capital markets. This would imply some reinforcement of the permanent CBD structure and would involve the hiring of external consultants.

There is thus a variety of actions that could be taken by governments, central banks of both creditor and debtor countries, and the Fund to improve external debt management in borrowing countries. But these efforts will not reach their ultimate goal, which is to ensure a better working of the overall bank lending process, unless at the same time a coordinated effort is launched to develop constructive relations between the Fund, member countries, and commercial banks.

1/ The World Bank External Debt Division maintains standardized data on external debt operations, new commitments, and future debt service as regards public and publicly guaranteed debt and, in a limited number of cases, nonguaranteed private debt, of one year or more. These activities suffer from budgetary constraints and from delays in the production of data by reporting countries.

Part III. How to develop constructive relations between the Fund, member countries, and commercial banks in regular Fund activities

A. Exchange of information

1. An effective working of the marketplace relies on adequate information. In an ideal world, banks would have detailed and timely information on the external debt and the economic situation and policies in borrowing countries and thus be able constantly to revise their assessment of those countries and to send "signals" to them through a widening of spreads, or a shortening of maturities, or in other ways. For the advocates of "private conditionality," these market signals are likely to induce the required adjustments in borrowing countries and to pave the way for a new phase of expansion of lending when economic indicators point to the success of the adjustment program. In reality, the world is more complex: there are "noises" in the statistical system, making it difficult to discriminate between overall trends and specific country trends; competition between bankers leads to alternating phases of over-lending and of abrupt cuts; and regional contagion is playing an increasing role. Nevertheless, information is vital for an orderly lending process.

Since the Fund has a unique capacity to collect information from member countries, there has been constant pressure from commercial banks to obtain the release of information provided to the Fund. Pressure applied on the country itself to publish information (see above) is the most obvious answer to this concern, but banks are also eager to develop direct access to Fund information and judgments. Such an approach runs counter to the confidential nature of the information supplied to the Fund by member countries, on which its quality relies. It was rejected, therefore, by the Fund's Executive Board in 1975, and the validity of this decision, and of its motives, remains.

Times have changed, however, and in view of the current difficulties encountered by borrowing countries in raising funds on the capital markets, there is a growing tendency for them to accept or encourage direct contacts between the Fund and commercial banks to help their own borrowing. In addition, the Fund has more and more frequently felt the need to obtain through direct contacts with bankers a considered view on economic performance, relations with suppliers and creditors, and likely capital flows for individual countries. Thus direct contacts have been made with lead bankers for certain countries; there have been meetings in creditor countries' central banks with a group of banks to discuss regional situations; and Fund staff members have participated in seminars or ad hoc meetings of commercial banks. These initiatives have been welcomed by commercial banks which would like to see them become a regular feature. For example, presentations on the situation in some regions could be given to commercial bankers in various European and Asian financial centers; and there could also be periodic meetings with small banks, for instance, in U.S. reserve money centers outside New York, to disseminate better information on Fund policies and practices. Another positive suggestion was for the Fund staff to meet with leading commercial banks at the time of a consultation mission. The idea of a semiannual or annual meeting of a group of 30 to 40 potential lead managers with IMF staff members, which was submitted by some bankers, could well take place under the aegis of the Intitute of International Finance described below. Finally, general publications such as the report on international capital markets or the report on external indebtedness of developing countries were welcomed, but the suggestion was made that they could be supplemented by more detailed publications dealing with developments in different regions of the world.

Informal contacts between the Fund and commercial banks are evidently of a diverse nature: some of them involve country specialists, others capital market specialists, and others are to be made at the level of heads of departments or even the Managing Director himself. But thought may be given to various possibilities for coordinating more systematically this ongoing process.

2. On the side of commercial banks, there is a corresponding desire to streamline procedures so as to improve the handling of information and the management of crises by the banking community. This began with the initiative of the G-30 International Banking Advisory Group which suggested the creation of a liaison body to include commercial banks, supervisors, central banks, and officials of international organizations. Its main functions would be to gather information, notably on individual banks' exposure to individual countries. The information would be kept secret but would be at hand if needed in a crisis. The liaison body would be able to act quickly to set up steering committees of banks and to know from the beginning the magnitude of the claims of the various banks involved. This initiative was, to some extent, distrusted by commercial banks who were afraid to see their responsibilities diluted within a body they would not fully control and has been watered down to periodic meetings of the Advisory Group to exchange information between various participants with diverse backgrounds and prospectives, in itself a useful development. But as far as policy-oriented banking coordination is concerned, the initiative has shifted to another group, the "Ditchley Park Group," which consists of leading international banks in the United States, the United Kingdom, Japan, Canada, Germany, France, Switzerland, and the Netherlands. After two meetings, the first near London in May, and the second in New York in October, they have created on January 11, 1983 an Institute of International Finance located in Washington. Membership of the Institute is open to all banks, all over the world, having an international exposure, but votes will be weighted according to relative transborder exposure. It will collect information on borrowing countries and develop contacts with the Fund and the World Bank. It might also conduct periodic country reviews which would not substitute for but would complement the own country risk assessments of the individual banks. This initiative could help avoid abrupt shifts in the attitudes of bankers to individual countries, structure the dialogue between borrowing countries and international banks, and reassure small banks that are now a vital part of the international bank lending process. It is therefore important for the Fund to develop with the Institute

confident relations leading to a better mutual understanding through accessibility and openness, in the mutual respect of confidentiality rules.

B. Complementarity in lending

As pointed out in the Fund report on "External Indebtedness of Developing Countries," there have been large swings in bank lending. The ratio of net bank flows to current account receipts for five countries having experienced debt service difficulties was in the range of 10 percent to 26 percent for the three-year period of peak inflow and in a range of -9 percent to +1 percent for the succeeding three years. 1/ As explained above, there has been a succession of debt cycles characterized by a phase of excessive borrowing, fueled by competition among banks, followed by a phase of severe adjustment, and, finally, a period of restoration of creditworthiness as the country rebuilds its access to the market.

These contrasting developments are clearly unwelcome since rapid increases in bank financing tend to be associated with unduly expansionary domestic policies, declining domestic savings rates, too ambitious investment strategy, and delays in necessary adjustment. Moreover, the severity of adjustment after such delays and the lengthy process by which creditworthiness is restored harm the normal development pattern of the borrowing country.

The Fund, in coordination with central banks and commercial banks, should therefore aim at smoothing this process by greater complementarity between bank lending and the use of Fund resources.

During a period of overlending, adequate information remains the best answer to the needed self-discipline in the marketplace, even if competition among banks reduces its impact. It has been suggested that the Fund, in its consultation reports, could issue guidelines on what would constitute adequate domestic policies or could even agree with the country on conditions under which the Fund would stand ready to step in (a "reverse stand-by arrangement"). But such a suggestion would appear difficult to implement since a deviation from guidelines or an absence of agreement could be looked at as impairing the borrowing capacity of a member country at a time when it is not using Fund resources. An

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1/ More recently, from 1976 to 1980, the average annual increase of external debt reached about 30 percent of current account receipts for countries such as Mexico (39 percent), Argentina (38 percent), and Brazil (27 percent).

adequate exchange of information between member countries, commercial banks, and the Fund on prospective balance of payments requirements and capital flows is probably a more realistic proposal. 1/

During a period of adjustment, banks normally apply pressure on the country to use Fund resources. The view was expressed that in such circumstances the Fund steps in too late, waiting for the outcome of lengthy discussions between the Fund staff and the country on the adjustment program, between the country and its creditors on debt service, and between the country, the World Bank, and donor countries on projected aid flows, thus aggravating the crisis. A possible answer might be a greater use of one-year stand-by arrangements at an earlier stage. Whatever the pattern of financing finally used by the Fund, there is also a need to integrate bank lending flows more fully in Fund programs. As mentioned by some officials "there was, in some stand-by arrangements, an assumption of banking finance which did not materialize." There is a clear need for a common assessment of required capital flows in the future, an approach for which the discussions between the Managing Director and bankers on Mexico might well appear as a forerunner. During adjustment periods, the complementarity of lending by the Fund and by commercial banks could take the form of an understanding on the exposure to be maintained by commercial banks provided the country remains current on its interest payments, and more formal assurances should be sought from commercial banks regarding their lending to members undertaking adjustment programs.

Finally, after an adjustment program has been successfully implemented, the Fund should help countries to regain access to the market and to embark on a normal pattern of financing by bank lending. This might be achieved by adequate incentives in Fund programs to restore the borrowing capacity of individual domestic entities, especially the commercial banks, but it also implies adequate contacts with export credit agencies, governments, central banks, and commercial banks to speed up the process of restoring creditworthiness.

C. Joint actions

1. The ultimate expression of a concerted approach to balance of payments financing would be joint action or cofinancing by commercial banks and the Fund. There have already been cases in which short-term bridging facilities were granted by commercial banks to prefinance drawings on the Fund (e.g., Turkey) or in which medium-term bank facilities were explicitly tied to the existence of Fund programs and even to the phasing of the use of Fund resources (e.g., Yugoslavia, Mexico, Brazil, and Argentina). Such an approach would be especially appropriate for a country like

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1/ Some bankers mentioned that, in addition to the direct release of information by countries, the Fund could maintain a data bank on these economic policy variables which, in its judgment, are the key variables in individual member countries. But this suggestion also runs counter to the need to protect relations between the Fund and member countries on the confidentiality of the consultation process.

Turkey when it is regaining access to the market. A joint meeting at the initiative of the borrowing country could include the Fund and the leading commercial banks to agree on their respective financing shares and to set up parallel loans with an explicit common phasing.

2. In present circumstances, many consider that the Fund should be ready to go further. Commercial banks have provided about US$50 billion for the financing of non-oil LDCs' current account deficits in 1981, and it is likely that the figure will be in the vicinity of US$25 billion in 1982 and US$20-25 billion in 1983. 1/ To close a potential annual financing gap of about US$20 billion, the Fund could step in by way of innovative techniques, such as cofinancing agreements, with some risk sharing, and borrowing on the markets. In particular, there could be a new conceptual framework under which banks would grant additional credits to a borrowing country and at the same time lend to the Fund the amounts it needs to finance its lending operations. It was pointed out, however, that, for many countries, the maximum amount provided by the Fund was not commensurate with external requirements (e.g., Mexico, where the annual amount provided by the Fund is in the vicinity of US$1.3 billion, whereas US$5 billion is required from banks in 1983). Hence the idea that the overall limit of 450 percent of quota could be temporarily waived (e.g., in a possible short-term facility as described below), or that the normal drawings on the Fund could be supplemented by resources provided by the Fund or by a Fund subsidiary borrowing in the markets at a time when there is, at least temporarily, a need for new channels of intermediation. On the other hand, it can be argued that, through collective agreements by bankers to supply the major debtors (Brazil and Mexico) with bank credits consistent with borrowing requirements under Fund programs, through additional restraint by other borrowers, and through continued bank lending to creditworthy countries, the present system is still fully able to meet the overall financing requirements, provided the Fund acts quickly and effectively when the need arises.

1/ As pointed out in the most recent World Economic Outlook, the impact on non-oil LDCs of this reduction in banking flows on current account deficits was partly compensated for by a massive swing in reserve movements (from an accumulation of US$2 billion in 1981 to a drawdown of about US$11 billion in 1982) and by a rise, from US$3.5 billion to US$10 billion, in the use of Fund credit. One significant source of financing for part of the 1982 deficit--the reduction of reserves--cannot be considered available again in 1983.

Part IV. How to handle better actual or potential crises

A. Debt rescheduling

The ultimate outcome of debt mismanagement is the inability of a country to fulfill its commitments and the need for its creditors to agree to a stretching out of existing commitments under a rescheduling agreement. Some participants in the market, notably some investment bankers, consider it as a normal development in a system under which long-term development financing is provided without an adequate equity base and with a too short maturity pattern. Others, notably commercial bankers in New York, who have in some cases created special units to deal with rescheduling negotiations, consider it as a fundamental breach of contractual commitments, which should be sanctioned by a lengthy and difficult negotiation and by a hardening of the terms of the loans subject to renegotiation. Whatever the outcome of this ongoing debate, events have imposed upon the market participants a growing number of rescheduling agreements with official creditors (Paris Club) and with bankers.

From 1956 to 1974, there were 30 such renegotiations involving 11 countries for a total amount of US$7 billion. From 1975 to 1980, the corresponding figures were 16 renegotiations involving 9 countries for a total amount of US$9 billion, and in 1981 and 1982 there were 27 renegotiations involving 16 countries for a total amount of US$15 billion. There was also a rapid increase in the number of countries falling into arrears, as noted in the Annual Report on Exchange Restrictions (10 in 1977, 19 in 1979, 28 in 1980, 25 in 1981, and 30 in 1982, for a total amount of US$11 billion).

1. General patterns

The analyses of these debt crises, and notably the Fund study on "Debt Restructuring--the Experience of Six Member Countries," reveal a number of common elements in the experience of countries which had to restructure their debt: excessive borrowing to finance consumption; economic and social rigidities; excessive credit creation; excessive debt accumulation and undue reliance on short-term credits; poor debt management and deterioration of the debt service ratio; weak export growth; and outflows of capital. They also show that fairly standard patterns for rescheduling have gradually developed.

a. Paris Club

The minutes of the Paris Club meetings (meetings of OECD creditor countries and of observers, chaired by the French Treasury) 1/ show a growing tendency to apply standard rescheduling terms, viz.: 80 percent of public and publicly guaranteed debt rescheduled and

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1/ The implementation of the agreement described in the minutes of the Paris Club is ensured through bilateral agreements in which the interest rate and other variables are determined.

repayment over a seven- to ten-year period after a grace period of two to three years. Differences appear, however, in the period of debt payments covered by the agreement (with a tendency in recent agreements to limit the period to one year), in the treatment of interest (with generally a rescheduling of overdue interest payments) and more fundamentally in the types of debt included. There tend to be particularly wide variations in regard to short-term debt: short-term debt was included in the agreement for Turkey, but excluded for Romania, which meant for Romania an additional US$240 million debt repayment in 1982 when other constraints were already severe.

According to a study by the Overseas Development Council, these terms when measured in quantitative terms (the difference in discounted value of the stream of debt service payments before and after rescheduling) normally imply only a limited amount of debt relief (from 1 percent to 10 percent of outstanding debt), but there have been significant exceptions where the relief exceeded 40 percent of outstanding debt (Ghana, Indonesia, Turkey). The grace period, in addition, gives the country a breathing space during which it can adjust its economy and restore its creditworthiness.

b. Banks

The negotiating process with banks is somewhat different since, instead of a general agreement implemented through bilateral negotiations, there is a need--after a lengthy phase of negotiation by a steering committee of seven to ten banks--for a detailed legal document acceptable to all bankers before the rescheduling agreement can be signed. In practice, however, last minute difficulties raised by individual bankers have always been overcome and the final outcome is effectively determined by the lead banks.

Here also standard patterns have developed. This is partly a reflection of the "equal treatment" policy of the Paris Club which requests the country involved to obtain from its private creditors (bankers and suppliers) new terms for their debt repayments at least as favorable as those granted by official creditors. More importantly, the use of precedents facilitates the negotiating process between lead banks, with different relative exposures in different countries, between the steering committee and the country and between the steering committee and the other banks.

These standard patterns may be summarized as follows:

- coverage: all arrears, a part of short-term debt, medium- and long-term debt falling due during a one-year period;

- exclusion of interest;

- percentage rescheduled: 80 percent to 85 percent (Poland) or even 90 percent (Turkey);

- repayment period: up to seven to ten years, with a grace period of two and a half to three years; and

- interest rate: LIBOR plus 1.75 percent on all rescheduled credits (plus a restructuring fee of 1 percent).

In particular, commercial banks consider that the exclusion of interest payments from rescheduling is a fundamental aspect of debt rescheduling which should be integrally preserved, since it avoids a classification of claims by supervisors as nonperforming assets and thus protects ongoing financing flows from banks to borrowing countries. For various reasons, bankers do not consider Nicaragua (where interest payments beyond 7 percent were rescheduled) as a precedent in this respect. In extreme circumstances, however, bankers may grant new credits that help the country meet its obligations, including interest payments (e.g., Poland in 1982, where new credits represented one half of the interest payments due in that year).

2. <u>Scope for improvement</u>

In itself, the concept of standardized patterns of rescheduling appears inadequate: the balance of payments and debt patterns of each individual country are unique and, in conformity with corporate debt rescheduling where future debt repayments are determined by cash flow projections compatible with the normal development of the restructured company, "tailored" solutions compatible with viable and sustainable balance of payments patterns would be far more appropriate. But such an approach would now be contrary to a series of precedents that have facilitated and continue to facilitate the negotiating process. In addition, commercial bankers stress that if a country restores its creditworthiness through adequate adjustment policies, through the avoidance of new arrears, and through the strict fulfillment of its obligations under the rescheduling agreements, it will find on the market the credits it will eventually need to smooth the repayment burden it is facing. The scope for improving the present rescheduling patterns is therefore limited but, nevertheless, there are means by which more predictability and more efficiency can be introduced in the system.

a. <u>Paris Club</u>

The weak element in the official debt rescheduling process is the absence of an injection of fresh money into the system by governments at a time when the country has no alternative source of funding. There has been constant pressure by developing countries to drop the distinction between debt relief and development assistance and to grant terms of debt relief suited to the medium-term balance of payments profile and the overall financing needs of the borrower. Indeed, for lower-income countries, there has been a recent tendency to convene a meeting of donor countries in parallel or shortly after the Paris Club meeting. The special mission currently under way for Sudan, on behalf of the Fund and the World Bank, is another attempt to adapt the debt rescheduling process to the special needs of low-income countries. But for most countries, and notably for middle-income countries, this solution is not applicable. The suggestion was made by some investment banks that official creditors should stand ready to refinance, when needed, interest payments that may impose such a burden on the borrowing country as to constitute a fundamental obstacle to a viable adjustment program. 1/ It is clear that, since governments do not have the same regulatory constraints as bankers, they should be prepared, as a matter of general policy, to reschedule interest payments on official debt, but it is difficult to conceive that they could, in addition, bail out the commercial banks by refinancing interest payments due to them.

A more trade-oriented approach was accordingly suggested in the course of the mission. There is normally a need for a rapid resumption of emergency imports at the time of the rescheduling agreement and either the World Bank, through a quick disbursing program loan, or governments, issuing guarantees for additional short-term trade credits, should stand ready to step in at that stage.

In order to help participating governments to contemplate such additional credits, one might conceive at the same time of some alleviation of the financial burden falling on governments under the present rescheduling patterns. Since commercial banks stand ready to reschedule their own unguaranteed claims, they should stand ready, through adequate financial incentives (fees and additional interest charges) to reschedule as well, under the same terms, their claims guaranteed by governments. The guarantees would remain intact and governments would repay their banks if the borrowing country were not fulfilling the terms of the rescheduling agreement, but for the creditor governments the financial burden would generally be deferred. There would be thus a good complementarity between (a) governments rescheduling direct loans and interest payments on official claims and extending (together with the World Bank?) some additional guarantees for trade financing and (b) banks rescheduling all their claims, guaranteed or nonguaranteed, with full payment of interest due to them. Furthermore, such an approach would lead to greater consistency in the coverage of the debts rescheduled under Paris Club agreements and agreements with banks.

b. Commercial banks

With the generalization of debt rescheduling agreements, there is scope for a more formalized process and some steps have already been taken in this direction. First, there is a need to speed up the negotiating process, which normally takes place during a period of rapid deterioration in the country's external situation. Borrowing countries themselves should initiate earlier discussions with their bankers and

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1/ A variant of this suggestion was also put forward which would involve the development of a secondary market for claims on borrowing countries with discounts for claims on problem countries and some kind of official support. In addition, several schemes aiming at a consolidation of existing debt into claims on an international organization have been presented (see bibliography).

maintain an accurate record of their various external debt commitments, with the help of an external advisor if needed. As far as banks are concerned, the setting up of the Institute of International Finance might contribute to a more rapid selection of participants in the steering committees and a more rapid dissemination of information to other bankers.

Second, there could be merit in defining "guidelines for rescheduling." In addition to a confirmation of the standard rescheduling patterns, they would introduce predictability and consistency with regard to the definition of credits to be rescheduled, which is the least satisfactory element to present policies, since in many cases (e.g., Turkey) the exclusion of some types of credit has harmed the country at the worst possible moment. Efforts to implement such a concept have, however, met with limited success for the time being because many bankers fear that the definition of guidelines could confer respectability and normality to a process which, in their view, should be regarded as atypical, cumbersome, and penalizing. Nevertheless, they have narrowed the issues to three: short-term trade-related credits, interbank deposits, and bonds and notes.

There are some good arguments for excluding short-term trade-related credits from rescheduling, in particular to maintain normal trade financing patterns, but the exclusion should be narrowly limited to documentary credits. For interbank deposits there is a fear that supervisors may treat them as credits if they are to be normally rescheduled, but clearly their exclusion is unjustified since they constitute the most volatile and destabilizing element in the whole picture. For bonds and notes, investment bankers (and the World Bank) stress that the rescheduling of bonds is a cumbersome process which would lastingly harm the ability of developing countries to issue bonds on the markets. Commercial bankers who prevailed in some recent discussions point out the limited difference between some syndicated loans and some floating-rate note issues and insist on including the latter with, on balance, probably more convincing arguments in many cases.

Finally, there is scope for improvement in the treatment of suppliers' credits. Banks insist on an equal treatment for suppliers which means that, with the exception of minor claims, their claims have to be rescheduled under the same terms as banks' claims. In practice, however, the negotiating position of suppliers is weak and in many cases suppliers have to accept conditions on maturities and interest which are unfair compared to the treatment applied to bank claims. In this area, more direct responsibility of bankers, acting on behalf of their industrial customers, could be of help; the Fund could also pay greater attention when assessing the outcome of debt rescheduling negotiations.

3. The role of the Fund

a. The Fund is invited, as an observer, to Paris Club meetings. Its role was highlighted by the UNCTAD resolution of 1979 (a compromise between developing countries seeking an independent and multilateral framework of negotiation, and OECD countries intending to protect the specific role of creditors), which indicated that the Fund, the World Bank, and UNCTAD should be invited as observers to Paris Club meetings and that the Fund and the Bank should jointly provide a contact point through which debt problems can be addressed and channeled toward the competent international bodies. In assessing balance of payments trends and prospects, and in describing the Fund-supported adjustment program, which is now a standard prerequisite to any rescheduling agreement, the representatives of the Fund play a most valuable role in the negotiating process.

The involvement of the Fund in discussions for the rescheduling of bank claims is more recent. There were some reschedulings of debts to banks in the 1950s and 1960s (Brazil, Argentina, Chile), but it was only in 1976-78, with Zaîre, Peru, Turkey, Jamaica, and the Sudan, that they became a standard feature in the treatment of severe debt problems. At the beginning of this process, commercial bankers tried to impose their own conditionality on countries (Zaîre, Peru),but the experience proved short-lived since commercial bankers were not in a position to monitor the borrowing government's implementation of economic policy measures and they gradually came to the view that the best approach was to ask the country to enter into an upper credit tranche stand-by arrangement with the Fund.

When such an arrangement is negotiated, there is a clear need for Fund involvement in discussions between the bankers and the country, to ensure a sufficient degree of compatibility. It took, however, some time for the Fund to move from a rather indirect involvement (Turkey) to a direct one (Romania) in which Fund representatives would supply participants with alternative balance of payments projections.

As an observer in both Paris Club meetings and meetings of banks, and as a supplier of funds under an adjustment program, the Fund is in a unique position to obtain a reasonable degree of consistency between interrelated decisions. In particular, it is entirely appropriate for the Fund to advise banks to maintain a minimum level of new lending. It implies mutually agreed views on prospective current accounts, including interest payments, and on associated capital flows, including additional bank lending.

In addition to this "complementary financing" approach, there might be a case for the elaboration by the Fund itself of an autonomous and coherent doctrine on rescheduling. While the situation of each individual country is unique, and while the Fund should not become involved in discussions between bankers themselves, which reflect their respective exposure in various types of credit, such a doctrine could be used as a benchmark against which to assess individual negotiations. It should be based on an in-depth study of all recent rescheduling negotiations but its basic components could be as follows:

- the scope of the rescheduling should be as large as possible, including all types of credit, with possibly the exceptions of short-term documentary credits;

- equal treatment should be applied to all creditors; there was a tendency in some recent agreements to treat suppliers less favorably than bankers, with the complicity of bankers; the Fund, through its policy on arrears, should ensure that suppliers are not unfairly treated; and

- the rescheduling should be tailored to the needs of the country, which might imply some advance discussions with Paris Club participants on less rigid patterns of reimbursement; the option of "partial rescheduing," limited to certain entities that are overindebted, should also be looked at more carefully.

b. While there is broad agreement that the Fund should be a more active "observer" or "mediator" in rescheduling negotiations, its possible role as an "advisor" for the country is more controversial. The functions of advisors have developed gradually with a leading role being played by investment banks in countries such as Indonesia, Gabon, Turkey, and Costa Rica. Views on the role of advisors differ widely. Some praise their ability to assemble data in a professional way, to give credibility to the figures supplied by the country, and to come up with imaginative schemes like the possible use of suppliers' claims on Turkey for new investments or for reprocessing activities. Others would prefer to see the data collection functions left to accounting firms, and underline that significant fees are asked for by investment bankers with frequently limited input. It has been suggested that the Fund, in order to present to member countries an alternative to their own assessment of the pros and cons of an investment bank, should offer its services under its technical assistance program, as an advisor in rescheduling negotiations. It does not seem advisable for the Fund to go too far in this direction: the Fund should appear neutral as between debtors and creditors and would lose its ability to influence the position of creditor countries and banks if it clearly sided with the debtors.

There is still great validity in the view that rescheduling should not be looked upon as a normal development and that a penalty should be attached to it. At the same time, a smooth handling of debt problems might help reassure the market in its assessment of sovereign risks and thus contribute to the maintenance of an adequate flow of international bank lending. The Fund, by a more active role in negotiations, which would not require it to act as an advisor, could contribute to this objective.

B. Individual liquidity crises

As indicated above, debt crises have normally been associated with international imbalances aggravated by unsound and procyclical lending by international banks. However, 1982 has seen the emergence of a new type of crisis induced by external developments, contagion effects, and a shift in the general attitude of bankers. This might be called a liquidity crisis and is typified by the cases of Hungary and Yugoslavia.

In such situations, there is normally a case for an adjustment program backed by the Fund, but there is at the same time a need to avoid an immediate crisis and a rapid withdrawal of deposits. Measures taken by the countries themselves (prudent use of the interbank market, an adequate debt profile, an appropriate level of reserves, maintenance of unused lines of credit) are essential. But collective action by commercial banks, the BIS, and the Fund has proved to be equally important.

1. The standstill concept

Many bankers deplore the absence of a mechanism by which a standstill on existing exposures could be imposed on individual international banks--rather in the manner of Chapter 11 of the bankruptcy law for U.S. corporations. They see in such a collective agreement the fundamental answer to cumulative withdrawals which may start with small banks (last in, first out) and spread to large banks, that may be willing to maintain their own exposure but do not wish to bail out other banks. The ways of implementing such a collective "freeze" of existing credit lines are diverse: covenants in syndicated loans under which central banks of borrowing countries would have to call a meeting of their lead banks if their short-term borrowing were falling below a certain limit; telexes sent by lead banks to all banks, inviting them to follow their example and to maintain their exposure; or national or regional meetings between individual lead banks and their national or regional partners. Such an approach implies that bankers feel that time is not running against them. Accordingly, some fresh money needs to be put into the system, in the form of immediately available funds from official sources.

2. The short-term facility

A possible solution to this problem would be a short-term six-month facility in the Fund amounting to 100/125 percent of quota and open to countries whose liabilities to banks or current account payments are higher than a given percentage of quota and who can meet some preconditions (see below). However, such an approach could be judged discriminatory among member countries, and could impair the ability of the Fund to negotiate a comprehensive adjustment program since, through the short-term facility, some of its funds would already be at stake.

The alternative, which was developed in 1982 for Hungary, Mexico, Brazil, Yugoslavia, and Argentina, is joint intervention by the BIS and the Fund. Whatever the merits of a flexible approach, there are some drawbacks attached to it as well. The case-by-case ad hoc approach could not be sufficient to reassure participants in the international banking market on the handling of future potential crises; the repayment of the BIS credits may be judged unwarranted, as was the case for Mexico, by bankers who are being asked to increase their exposure. A more standardized pattern for the use by the same country of BIS credits and Fund resources could help alleviate this difficulty.

Hence an intermediate approach might be proposed, involving some sort of joint financing by the BIS and the Fund, to be used--when requested--by a country for which there is both a need for fundamental adjustment and a need to cope with a potential liquidity crisis that could have adverse effects on the system as a whole. In such cases the Fund and the BIS would stand ready to act jointly as follows:

a. the IMF would start negotiating a comprehensive adjustment program under a stand-by agreement, ensuring a yearly amount of available resources in the range of 100 to 150 percent of quota; the BIS would grant a short-term credit (6 to 12 months), reimbursed by the first drawing on the Fund; and

b. the joint action of the BIS and the IMF would be dependent upon the fulfillment of three preconditions:

- the selection by the country of a small coordinating group of major banks which would ensure that all banks stand ready to maintain an adequate level of exposure during a certain period of time;

- immediate action by the country to take policy measures with the instruments that are readily available, particularly the exchange rate and interest rates; and

- a judgment by the Fund staff that there is a reasonable assurance that the country will implement a comprehensive program of adjustment embodied in a stand-by arrangement.

In view of the very proper preoccupation of the BIS Governors to avoid general commitments which may not be appropriate in all circumstances, it is natural that they should continue to wish to act on an ad hoc basis on this matter. But similar results can be achieved through this more pragmatic approach.

It is clear, in view of the sheer magnitude of short-term indebtedness of many borrowing countries, and in view of the number of banks involved in some countries, that such joint action will not be sufficient to deal with all possible situations, and it is likely that some liquidity problems will develop into debt crises, implying a partial or total rescheduling of existing debts. However, this action would help to limit the number of such cases, to defuse the tensions within the system, and to reassure market participants of the viability of the overall bank lending framework.

C. Overall liquidity crisis

Finally, there is a pessimistic view, to which some recent difficulties give impetus, according to which one cannot exclude a generalized crisis in the banking system. Due to adverse developments on the asset side of its balance sheet, a major bank could register on the liability side a large withdrawal of deposits and lines of credit. It would then be unable to meet its commitments, either directly or with the help of its central bank, if the central bank did not have available foreign exchange reserves commensurate with the size of the problem.

The decline in interest rates and the handling of the individual country crises of 1982 have made such developments more unlikely than could have been felt around the middle of 1982. Nevertheless, a strengthening of the system's ability to cope with such a potential crisis would be the best way to avoid its occurrence, since it would inject into the system badly needed confidence factors. This would imply a clearer definition of the responsibilities of individual central banks, mutual understanding between central banks to provide each other with the resources that might be needed, and a backing by the Fund standing ready to see its resources used in such circumstances.

1. Individual central banks as lenders of last resort

Internationally, as well as domestically, the best way to avoid a bank crisis is to show in advance that the central bank is prepared to act as lender of last resort if a liquidity squeeze were applied to an individual bank. However, central bankers do not want to commit themselves in advance to any precise action: uncertainty is a necessary element in prudential behavior by banks; provoking a crisis and avoiding its spreading remains the essence of central banking art, as described by Bagehot; the means available to cope with a particular situation are not known in advance, especially in countries where, besides central banks, other agencies (such as the Federal Deposit Insurance Corporation in the United States) or governmental funds (Germany) have to be involved. This explains why in 1974, when central bankers had to face the first postwar crisis of confidence in the international banking system, they issued the following rather cryptic statement: "...they recognized that it would not be practical to lay down in advance rules and procedures for the provision of temporary liquidity" but "...they were satisfied that means are available for that purpose and will be used if and when necessary."

This statement was accompanied by some specific measures dealing with the supervision of individual banks (the creation of the Blunden Committee) and did help to restore confidence, the more so since it had not to be tested. Both the Herstatt failure in Germany, where the bank defaulted on its foreign exchange commitments in the middle of a working day, and the Franklin crisis in the United States, where finally, through cooperative action between the Fed of New York, the Bank of England, and other central banks, a solution was found that did not entail any loss for creditors (a takeover by a consortium of European banks) damaged the markets in 1974, but their size was not such as to strike a fundamental blow to the system.

If ambiguity in the way in which central banks will deal with a crisis can, within certain limits, be explained, a clear understanding of the respective responsibilities of individual central banks would, however, seem essential. While dealing not specifically with the lender-of-last resort issue but with supervisory functions, the Concordat of 1975 aimed at such a result. Unfortunately, while it clearly attributed responsibility to the parent central bank as far as branches are concerned, it was ambiguous on subsidiaries by stating that "for foreign subsidiaries and joint ventures, primary responsibility rests with host authorities; but parent authorities must take account of the exposure of their domestic banks' commitments to those foreign establishments," leaving open differences of interpretation as to the responsibility for solvency.

The Ambrosiano crisis showed the drawbacks of ambiguity. It prompted the Luxembourg supervisory authorities to ask from parent banks "letters of comfort" along lines already followed by the Bank of England. But it cast an additional doubt on subsidiaries, consortium banks, and joint ventures operating on the market, led to some discrimination between locations, and fueled the crisis that developed in the summer of 1982.

There is thus a need to clarify the role of central banks by a new declaration that would allocate responsibilities between central banks without ambiguity, while leaving some vagueness, if this were felt indispensable, as to the means to be used. 1/

However, individual central banks would hesitate to take such responsibilities as lenders of last resort if they did not feel assured that they would themselves be provided adequate liquidity by other central banks, if needed.

2. The central banks' network as a liquidity guarantee

When a central bank is facing a domestic liquidity crisis, it has an unlimited ability to provide funds to the market or to the banks running into difficulties. However, its ability to cope, for instance, with a dollar liquidity crisis of one of its commercial banks is constrained by its own dollar reserves. In the end, the only lender of last resort in dollars is the U.S. Federal Reserve System and, while central banks with large dollar reserves, such as the Bundesbank, or with a large and diversified dollar market, such as the Bank of England, have adequate resources to cope with a dollar crisis, the same is not

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1/ The Concordat was revised in 1983 with greater emphasis put on consolidation and on control of nonbank subsidiaries performing bank functions. But it was stressed again that it was dealing with supervision issues and not addressing the question of the lender of last resort.

true for all central banks. In addition, while in 1976, when some banks had difficulties funding their operations, the market was able to take over the claims of these banks when they matured, thus avoiding a net contraction of the market, such an attitude would probably not prevail under present conditions, which means that an individual crisis would be bound to spread to the market as a whole.

It is necessary, therefore, to strengthen cooperation between BIS central banks to ensure collectively that adequate dollar resources will be available to face potential liquidity shortages. The instrument to that effect exists, namely, the swap network between central banks, but it has not been expanded in recent years and its present size, at US$32 billion, is not longer commensurate with the potential risks on a US$2,000 billion market. Renegotiation of the swap network, with a doubling or a tripling of its size and a clear understanding that it could be used by a central bank when it judges the time appropriate to enter into individual swap agreements with some of its commercial banks to help them meet a potential liquidity crisis, would appear justified.

While such swap facilities are normally of a temporary and self-reversing character, the extension of the network and the enlargement of its functions would be easier for potential creditor central banks to accept if it were possible for the debtor or the creditor to refinance swap drawings.

3. The Fund as a supplier of medium-term finance

The Fund has, therefore, an important role to play in the overall picture. Since monetary stability in the world is one of the major goals of the institution, it should be willing to contribute to the avoidance of an overall liquidity crisis that might result from a bank crisis by standing ready to refinance commitments resulting from the activation of the central banks' network under the circumstances just described.

Two broad avenues should be further explored:

a. An exchange of the claims of a creditor central bank on debtor central banks against fully liquid SDR-denominated claims on the Fund. It would have the merit of avoiding the risks of discrimination between countries. Such a system would, however, encounter many of the difficulties attached to the substitution account concept.

b. The possibility for a central bank, either as a debtor repaying its swap commitments or as a creditor granting swap facilities, to use Fund resources to refinance its debts or claims. Clearly the resources that the country could use would have to be sufficient to meet potential liquidity risks and thus not be limited by an overall ceiling related only to quotas. The discriminatory element could be alleviated if resources for such drawings beyond the standard limit of 450 percent of quota were available from a separate borrowing arrangement funded by major creditor countries.

But clearly whatever the technical solution selected, such a possibility would imply additional Fund resources beyond those already committed, which means that the time is probably not ripe to address this issue.

It is clear that the slowdown of international bank lending will, in addition, have depressive effects on the world economy if it is not matched, as far as possible, by an increase in lending by official institutions. An increase in the resources of the World Bank, thereby avoiding a graduation process with adverse effects in present circumstances, supplemented by imaginative cofinancing techniques between the commercial banks and the World Bank, a fresh look at multilateral guarantee mechanisms, and an increase in ordinary Fund resources, appear to be necessary complementary actions. As far as the Fund is concerned, the quota increase presently under way will bring a first positive contribution, *provided that it is associated with some enlarging of potential* drawings in absolute terms.

A clear signal given by the Governors during the Annual Meeting to move forward in the direction of securing additional resources for the Fund and to encourage the Fund to devise mechanisms better equipped to deal with potential liquidity crises would be a most positive development in efforts under way to restore confidence on the international banking scene.

Part V. Conclusions and recommendations

International bank credits have played a vital role in the expansion of the world economy during the last ten years. The simultaneous occurrence in 1982 of high interest rates, political tensions, and debt crises in several major borrowing countries has led to a major shift in the attitudes of bankers, which could well initiate a spiral of sharply reduced new lending, added difficulties for certain countries, and depressive influences on the much needed world economic recovery.

There is therefore a need for a set of collective actions by which governments, central banks, commercial banks, and international organizations show their common desire to restore confidence in the marketplace. The Fund has to be an essential partner in this overall process.

Suggestions to that effect have been made in the course of this report and belong to four broad categories:

- a better assessment of trends in the market and of the attitude of commercial banks: analysis of potential flows with special attention to interbank transactions, oil trade-related credits, and intra-Comecon financial relations; improvement of statistical data and pressure on member countries to release adequate information; and the setting up in the Fund of a country risk assessment model to help predict banks' attitudes toward individual countries;

- a contribution to better external debt management by individual countries: greater attention to liquidity and debt developments in consultation reports; technical assistance to help countries diversify and monitor their external debt; and close association with supervisors in both debtor and creditor countries, through the BIS Committee on Bank Supervision;

- a constructive collaboration with commercial banks: development of ad hoc contacts through different channels, notably the new Institute of International Finance; better integration of private financial flows in Fund programs with a view to avoiding undue recourse to short-term borrowing; and a cofinancing approach for countries re-entering the market after a phase of adjustment; and

- a better handling of potential crises: deeper Fund involvement in rescheduling negotiations through discussions with Paris Club members on future rescheduling patterns and through the definition of guidelines for rescheduling bank claims; the setting up of a short-term Fund facility or a more integrated BIS/IMF package to cope with liquidity crises; and the mobilization of additional resources by central banks agreeing on a more precise and more structured undertaking as lenders of last resort to meet the needs which might arise in the context of a bank liquidity crisis.

The coordinated stragegy for averting an international debt crisis which was initiated by the Fund in 1982, in full cooperation with borrowing countries, creditor countries, the BIS, and commercial banks, has displayed the aptitude of the institution to face major challenges. In the months to come, additional actions, based on the experience of 1982, might well appear appropriate to help the international bank lending market overcome its present crisis of confidence, and thus reduce the risks of a too short-lived and too narrowly based economic recovery in the world.

List of Persons Encountered in the Course of the Mission

International Monetary Fund

The Managing Director; the Deputy Managing Director.

Executive Directors: Messrs. Anson (Taylor), de Groote, de Maulde, Erb, Hirao, Kafka, Laske, Lovato, Nimatallah, and Polak.

Heads of Departments: Messrs. Whittome, Finch, Habermeier, Hood, Kaul, and Robichek.

Office in Europe: Mr. Guetta and Mr. Ley.

European Department: Messrs. Rose, de Fontenay, Mrs. Junz, Messrs. Schmitt, Tyler, Hole, Mrs. Ter-Minassian, Mr. Manison, Ms. Ripley, and Ms. Salop.

Exchange and Trade Relations Department: Messrs. R. Williams, R. Abrams, Ms. Dillon, Messrs. Donovan, and Johnson.

Treasurer's Department: Mr. D. Williams.

Research Department: Mr. Schwartz.

Central Banking Department: Messrs. Duvaux and Mehran.

Bureau of Statistics: Messrs. McLenaghan and O'Connor

Other international organizations

Bank for International Settlements: Messrs. Leutwiler, Schleiminger, Dealtry, Gros, Hall, Lamfalussy, Mayer, and Vallet.

World Bank: Messrs. Stern, Balassa, and Hope.

OECD: Messrs. Hackett and Keyzer.

Paris Club: Mr. Camdessus.

Governments and central banks

Washington/New York: Federal Reserve: Messrs. Wallich, Solomon, Cross, Kubarick, and Miss Dowson.

London: Bank of England: Messrs. McMahon, Loehnis, Holland, Gilchrist, Kent, Cooke, and Quinn. Treasury: Mr. Lavelle and associates.

Frankfurt: Bundesbank: Messrs. Rieke, Müller, and associates.

Paris: Ministry of Finance: Messrs. Camdessus and Trichet. Bank of France: Messrs. de La Genière, Waitzenegger, and Aubanel.

Zürich: Swiss National Bank: Messrs. Leutwiler and Mayer.

Vienna: National Bank of Austria: Messrs. Treichl, Lachs, and Hain.

Commercial banks

New York

Citibank: Messrs. Clark, Guenther, West, and associates.

Chase Manhattan: Messrs. Ogden, Mason, Sleighton (plus Mr. Greer in London).

Morgan Guaranty: Messrs. Weatherston, de Vries, Stange, and associates.

Manufacturers Hanover: Messrs. Taylor, McCouch, and associate.

Bankers Trust: Messrs. Brainard and Schwarz.

Chemical: Messrs. Carson and Tunney.

London

Lloyds: Sir Jeremy Morse, Messrs. Kingshott and Clark.

Barclays: Mr. Ardron and associates.

Midland: Mr. Harris and associates (and Mr. Wilcox).

National Westminster: Mr. Plastow and associates.

Frankfurt

Deutsche Bank: Messrs. Vons, Von der Bey, and Arens.

Dresdner Bank: Messrs. Spaeh, Krueger, and associates.

Commerzbank: Mr. Lucassen and associates.

Bank für Gemeinwirtschaft: Mr. Müller.

Paris

BNP: Messrs. Wahl, Decker, Pinot, and Lacombe.

Crédit Lyonnais: Mr. Smolarski and associates.

Société Générale: Messrs. Vienot, Auberger, and Laulan.

UBAF: Mr. Abushadi and associates.

Zürich:

Union Bank of Switzerland: Mr. Hanselmann.

SBC: Mr. Streichenberger.

Crédit Suisse: Mr. Guyter and associates.

Amsterdam

Algemene Bank Nederland: Mr. Oort and associates.

AMRO: Mr. Ruding and associates.

Brussels

Société Générale de Banque: Messrs. Derwa and Piloy .

Vienna

Creditanstalt Bankverein:

Toronto

Royal Bank of Canada: Mr. Taylor

First National of Chicago: Mr. MacDonough

Bank of America: Mr. Prussia (plus Messrs. Heller and Campbell in Washington and Mr. Felby in London).

Bank of Tokyo: Mr. Matsumoto.

Investment banks

New York

Lehmann-Kuhn-Loeb: Mr. Stein and Mrs. Bindert.

Paribas-Warburg: Mr. Heimann.

Schroeder: Mr. Bell

London

Morgan Grenfell: Mr. Whittington and associates.

Kleinworth, Benson:

Paris

Lazard Frères: Mr. de Pourtalès.

Research organizations and consultant firms

Wharton Econometrics (Washington): Mr. Vanous.

Council for Economic Relations (New York): Messrs. Diebolt and de Menil.

Carnegie Endowment Fund (New York): Miss Lissakers.

Institute for International Studies (Washington): Mr. Bergsten.

Participation in meetings

G-30 International Banking Group (Messrs. Witteveen, Emminger, Heimann, Bell, Finch, and Whittome, and representatives of the BIS, central banks, and commercial banks): London (May and December); Toronto (September).

Ditchley Park Group: Messrs. Ogden (Chase Manhattan), Leslie (Barclays), Co-Chairmen, with representatives of leading American, Japanese, U.K., Canadian, German, French, Swiss, and Dutch banks, and of the IMF, BIS, IBRD, Bank of England, and U.S. Comptroller of the Currency. Ditchley Park, England, May 1982--attended by Mr. de Larosière and Mr. Finch; New York, November 1982--attended by Mr. Finch.

Borrowing countries

Portugal: Ministry of Finance, Central Bank, commercial banks (Banco Atlantico, Banco Sotto Mayor, Banco Spirito Soto, and Banco Totta y Açores), and Development Bank.

Turkey: Ministry of Finance, Central Bank, commercial banks (Isbank, Akbank, Garanti Bankasi, and Pamuk Bank), Chamber of Commerce, and Development Bank.

Romania: Ministry of Finance, National Bank, and Bank for Foreign Trade.

Hungary: National Bank, Bank for Foreign Trade, and Intercontinental Bank.

Yugoslavia: Executive Council, Ministry of Finance, National Bank, and commercial banks (Jugobanka, Zagrebacka Banka, Privredna Banka Zagreb, and Ljubljanska Banka).

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External Indebtedness of Borrowing Countries, May 1981 (ETR, Mr. Nowzad) [1]

Debt Restructuring by Commercial Banks, August 1981 (ETR) [6]

The Stability of the International Banking System (Annex: International Coordination of Bank Supervision--Need and Availability of an International Lender of Last Resort) [5]

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Seminar on Central Banking 2/ (CBD) [3, 5, 6]

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Statistics on International Banking and External Indebtedness, December 1982 (STAT) [2]

The Impact of Country Risk Assessment, May 1980 (RES) [3]

External Public Debt Management, 1981 (WHD, Mr. Robichek) [1]

Internal Documents and Memoranda (EUR, ETR, STAT, CBD)

Debt Capacity and Developing Country Borrowing, August 1982 (ETR) [1]

Aspects of the International Banking Safety Net, 1983 (ETR, Messrs. Johnson and Abram) [4, 5]

World Bank

Development Committee. Task Force on Nonconcessional Flows, April 1982 [1]

1/ The numbers in square brackets indicate the subjects dealt with in the paper as follows: [1] general setting; [2] statistical data and issues; [3] country risk assessment; [4] the interbank market; [5] supervision; [6] rescheduling; and [7] external debt of Comecon countries. The main elements of the IMF papers are presented in the annotated bibliography under these seven headings.

2/ See last page of bibliography.

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International Debt Renegotiation: Lessons from the Past, 1979 (Mr. Cisauskas) [6]

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DAC: Geographical Distribution of Financial Flows to Developing Countries, 1982 [2]

External Debt of Developing Countries, 1982 [1]

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Seminar on Legal Aspects of International Financing Transactions, January 1983 [1, 6]

BIS

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Bank of England

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G-30

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