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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 86/163

6:15 p.m., September 30, 1986

Sheraton Washington Hotel

J. de Larosière, Chairman
R. D. Erb, Deputy Managing Director

Executive Directors	Alternate Executive Directors
	Mawakani Samba
C. H. Dallara	
J. de Groote	
	T. Alhaimus
	M. Sugita
	B. Goos
Huang F.	
J. E. Ismael	Jaafar A.
A. Kafka	H. A. Arias
T. P. Lankester	M. Foot
	H. Fugmann
M. Massé	
E. I. M. Mtei	A. Abdallah
F. L. Nebbia	
Y. A. Nimatallah	J. E. Suraisry
P. Pérez	G. Ortiz
H. Ploix	S. de Forges
J. J. Polak	J. de Beaufort Wijnholds
	A. V. Romuáldez
G. Salehkhou	O. Kabbaj
	A. S. Jayawardena
S. Zecchini	

L. Van Houtven, Secretary
B. J. Owen, Assistant

Also Present

Asian Department: H. Neiss, Deputy Director. European Department: L. A. Whittome, Counsellor and Director. Exchange and Trade Relations Department: M. Guitián, Deputy Director. External Relations Department: A. F. Mohammed, Director. Legal Department: F. P. Gianviti, Director; S. A. Silard. Research Department: R. R. Rhomberg, Deputy Director. Secretary's Department: J. W. Lang, Jr., Deputy Secretary; A. P. Bhagwat. Treasurer's Department: D. Williams, Deputy Treasurer. Western Hemisphere Department: E. Wiesner, Director; S. T. Beza, Associate Director; J. O. Bonvicini, E. R. J. Kalter, J. P. Pujol, L. M. Valdivieso. Personal Assistant to the Managing Director: R. M. G. Brown. Advisors to Executive Directors: W.-R. Bengs, L. P. Ebrill, J. Hospedales, K. Murakami, A. Ouanes, D. C. Templeman, A. Vasudevan. Assistants to Executive Directors: J. R. N. Almeida, O. S.-M. Bethel, J. de la Herrán, W. N. Engert, L. Hubloue, S. King, J. E. Rodríguez, G. Schurr, L. Tornetta, B. D. White.

1. MEXICO - REPORT BY MANAGING DIRECTOR AND DEPUTY MANAGING DIRECTOR

The Chairman said that he had come from a meeting with commercial bankers where he had been informed that an agreement in principle had just been reached between the Mexican authorities and the commercial banks. The amount of financing to be provided by the banks in support of Mexico's program--US$6 billion of new money--had been maintained, although a certain amount would be deducted on account of concessions granted by the banks to Mexico on the spread. The earlier assumptions had included a spread of one and one-eighth percent and anything less represented a saving that would reduce the amount correspondingly. The World Bank was to provide a limited guarantee.

Referring to the contingency mechanisms included in the program under the stand-by arrangement--approved in principle on September 8 (EBM/86/149)--the Chairman noted that the growth contingency had been maintained, as had the conditions for its activation. The World Bank would again take part by means of a guarantee of US$250 million.

The essence of the oil contingency had also been retained, with some modifications to the commercial banks' contribution that remained to be finalized in a specific understanding between the commercial banks and the Fund, the Chairman added. The maximum contribution by the banks would be US$1.2 billion--rather than US$1.7 billion--and the Fund had asked the Mexican authorities to accept a reduction in its own contribution from SDR 800 million to SDR 600 million, for a total of US$1.8 million, retaining the proportions of 1:2. With the passage of time, it was obvious that the oil contingency could not be activated in the third quarter of 1986, because the price of oil obviously would not fall in that quarter, and there was little probability also that the floor reference price of US$9 would be reached in the fourth quarter.

The share of the banks in the oil contingency would have the name of "Commercial Bank Contingency Investment Support Facility," the Chairman explained. The reason was to be found in the purpose of the contingency, in the context of the Baker initiative, and the desire of the bankers to emphasize the need to promote investment. It was clear that if the Mexican economy were to be hit by a dramatic new fall in the price of oil, budgetary receipts would be affected immediately, and unless support was provided, capital investment in the budget would have to be cut. From the bankers' point of view, it was more in conformity with the intentions of the exercise in which they were participating, as well as with the marketability of the package, to place less emphasis on the factors that could trigger the contingency mechanism and to highlight instead the dangers of leaving the program unprotected against a drastic cut in investment in the budget. The Fund, the Mexican authorities, and the commercial banks would be working together closely in the days ahead on the precise modalities of the joint contingency mechanism. As soon as agreement was reached, the Executive Board would be informed of the details in a staff paper; for the time being, it could be said that the basic thrust of the financial package had been agreed, in principle, without changing the basic parameters of the arrangement with Mexico.

One of the most difficult points in the negotiations on which agreement had just been reached concerned the rate of interest, the Chairman continued. The two parties had finally agreed on a spread of thirteen sixteenths over LIBOR for all categories of money, and on maturities of 12 years with 5 years' grace for the new money, 20 years with 7 years' grace for the old rescheduled money, and no change in maturities for the "old" new money. The term sheet had yet to be finalized, and thereafter, the agreement would have to be accepted by the banking community. The bankers considered that the critical mass could be attained by October 31. Since the period for final approval of the stand-by arrangement, which had been approved in principle, had expired on the previous day, it would be necessary to resubmit the request to the Executive Board for approval on or after October 31, 1986.

The Deputy Managing Director added that as he understood it, the World Bank guarantee would cover the outer end of the maturities, or about US$500 million of the US$7.7 billion package. About half of the growth contingency--US$250 million--would be guaranteed by the World Bank. The World Bank had in fact made a marginal contribution to the package by improving its marketability.

Mr. Kafka inquired whether the form of the World Bank's contribution meant that the World Bank support would not be available if Mexico's external receipts fell seriously enough to endanger current investment expenditures.

The Chairman responded that if the oil contingency mechanism was triggered, the impact on the budgetary outlook and the consequences for the investment program would have to be assessed by the Fund. The legal modalities for triggering a pro rata contribution by the commercial banks remained to be worked out.

The Deputy Managing Director added that the companion Commercial Bank Contingency Investment Support Facility had a close logical link to the oil contingency mechanism. The objective was to provide some cushion in the ongoing program of Mexico, and in particular the investment program, against a sudden decline in the Government's external revenues, which were dominated by the relationship with the price of oil. The process of assessment did not envisage a detailed analysis of the investment program to determine whether the additional resources were needed; rather, the objective would be to determine whether some other shift in external revenue might offset the impact of the decline in oil revenue which might be cause for an adjustment in disbursements under the companion Commercial Bank Contingency Investment Support Facility. Operationally, that facility would work as if it were part of the oil contingency, but for presentational reasons and to gain support for the basic concepts underlying the package, the banks preferred to highlight the purpose of the oil contingency rather than to emphasize the oil price link.

Mr. Ortiz pointed out that a small portion of the Investment Support Facility--US$100 million--could take the form of onlending.

In response to a question by Mr. Lankester, Mr. Ortiz said that the concession on the spread, in terms of the total package of US$6 billion, would be worth about US$250 million, on an average annual basis.

The Deputy Managing Director, in response to questions by Mr. Lankester, said that he could confirm that the World Bank's overall exposure would remain unchanged, at US$2.3 billion, discounted for the value of the guarantees. The World Bank was in a better position to explain the details of the maturities of the guarantees.

Mr. Zecchini said that he wondered whether the World Bank and the Fund were not being expected to provide additional support compared with what had been envisaged in the original program, for the purpose of enabling Mexico to benefit from better conditions from the commercial banks.

The Chairman responded that the Fund had made no concessions; its support was unchanged, the reduction in the oil contingency from SDR 800 million to SDR 600 million having been necessitated by the passage of time. The World Bank had provided guarantees but had discounted them in its exposure, confirmed by the Deputy Managing Director.

The Director of the Legal Department noted that a new decision would have to be adopted by the Executive Board, the period for approving the stand-by arrangement having lapsed, and certain adjustments might have to be made to the arrangement, including the amounts.

The Deputy Director of the Exchange and Trade Relations Department commented that the performance criteria and phasing would not have to be changed. However, a supplementary staff paper would have to be issued to incorporate the necessary changes in the stand-by arrangement in response to the reduction in the maximum potential amount to be made available and to the specific features of the final agreement with the banks, for consideration and approval of the request by the Executive Board on the date on which the critical mass was achieved.

The Chairman commented that it was important to be able to reactivate the program and for the stand-by arrangement to become effective no later than October 31.

The Deputy Managing Director said that it was also important to emphasize the date of the first disbursement. Frequently, it took months after the critical mass was reached for the legal documentation to be finalized and the first disbursement triggered. The Fund had emphasized the necessity for disbursements to begin during 1986, some time in December. It was also useful to indicate to the banks that the term sheet should be approved within the next few days. The statement of the Fund's continued support for the program could then be telexed to the banks by the Managing Director (see EBS/86/233, 10/17/86).

Mr. Ortiz confirmed that the Mexican authorities would be responsible for informing the press about the agreement in principle that had been reached with the banks and the Fund.

The Executive Directors took note of the report by the Managing Director and Deputy Managing Director.

DECISIONS TAKEN SINCE PREVIOUS BOARD MEETING

The following decisions were adopted by the Executive Board without meeting in the period between EBM/86/162 (9/24/86) and EBM/86/163 (9/30/86).

2. MOROCCO - TECHNICAL ASSISTANCE

In response to a request from the authorities of Morocco for technical assistance in the fiscal field, the Executive Board approves the proposal set forth in EBD/86/252 (9/19/86).

Adopted September 25, 1986

3. EUROPEAN MONETARY SYSTEM - RECENT DEVELOPMENTS - PUBLICATION

The Executive Board approves the proposal for publication, in the Occasional Paper series, of the staff paper entitled "The European Monetary System - Recent Developments" as set forth in SM/86/233 (9/8/86) and Supplement 1 (9/16/86).

Adopted September 24, 1986

4. EXECUTIVE DIRECTOR - EXTENSION OF PERIOD FOR REPATRIATION

The Executive Board approves the recommendation concerning the extension of the period for repatriation of Mr. Lieftinck as set forth in EBAP/86/227 (9/22/86).

Adopted September 26, 1986

5. ASSISTANT TO EXECUTIVE DIRECTOR

The Executive Board approves the appointment of an Assistant to Executive Director as set forth in EBAP/86/226 (9/22/86).

Adopted September 24, 1986

6. APPROVAL OF MINUTES

a. The minutes of Executive Board Meetings 86/17 and 86/18 are approved. (EBD/86/251, 9/19/86)

Adopted September 25, 1986

b. The minutes of Executive Board Meetings 86/19 and 86/20 are approved. (EBD/86/254, 9/22/86)

Adopted September 26, 1986

c. The minutes of Executive Board Meetings 86/21 through 86/25 are approved. (EBD/86/256, 9/23/86)

Adopted September 29, 1986

7. EXECUTIVE BOARD TRAVEL

Travel by an Executive Director as set forth in EBAP/86/209, Supplement 1 (9/25/86) and by an Advisor to Executive Director as set forth in EBAP/86/232 (9/26/86) is approved.

APPROVED: June 5, 1987

LEO VAN HOUTVEN
Secretary