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**IMMEDIATE
ATTENTION**

EBS/85/197

CONFIDENTIAL

August 20, 1985

To: Members of the Executive Board
From: The Acting Secretary
Subject: Yugoslavia - Review of External Financing Arrangements

It is not proposed to bring the attached memorandum to the agenda of the Executive Board for discussion unless an Executive Director so requests by the close of business on Friday, August 23, 1985. In the absence of such a request, the draft decision that appears on page 3 will be deemed approved by the Executive Board and it will be so recorded in the minutes of the next meeting thereafter.

Mrs. Junz (ext. 8849) is available to answer technical or factual questions relating to this paper.

Att: (1)

CONFIDENTIAL

INTERNATIONAL MONETARY FUND

YUGOSLAVIA

Review of External Financing Arrangements

Prepared by the European Department

(In consultation with other Departments)

Approved by P. de Fontenay and Eduard Brau

August 19, 1985

I. Introduction

On April 29, 1985 the Executive Board approved a one-year stand-by arrangement for Yugoslavia in an amount equivalent to SDR 300 million, or 49 percent of quota. The first purchase, SDR 30 million, was made on May 31, 1985.

In view of the continuing negotiations between Yugoslavia and its commercial bank creditors on the refinancing of maturities falling due in the period of the stand-by arrangement, the Executive Board decided that the second purchase, SDR 67.5 million, scheduled to become available on August 30, 1985, would be contingent upon a finding by the Fund "...that satisfactory arrangements have been made... for the refinancing of maturities falling due during the period from January 1, 1985 until the expiration of the stand-by arrangement..." This decision reflected a wish to be assured of the financial soundness of the economic program for Yugoslavia.

II. Status of multi-year refinancing agreement with banks

In the period since the Executive Board approved the stand-by arrangement for Yugoslavia, extensive discussions have taken place between the Yugoslav authorities and the creditor banks' International Coordinating Committee (ICC) on the refinancing of nonguaranteed maturities falling due over the period 1985-88. Because the Fund's provision of enhanced surveillance from May 1986 is an integral part of the agreement being negotiated, the Executive Board met on July 22 in informal session to review the modalities of enhanced surveillance that would be requested, on the basis of the agreement in principle that had been reached by the banks and the Yugoslav authorities, and to indicate

the Fund's willingness to participate in the activities envisaged. The agreement in principle is presented in EBS/85/171 (7/19/85). Formal approval of the Fund's carrying out enhanced surveillance will require a decision of the Executive Board in due course.

During the week of July 29, another round of discussions between the Yugoslav authorities and the ICC resulted in further progress toward agreement on the economic elements of the financing package. It is the staff's understanding that agreement was reached on the economic content of the refinancing package; although the banks have not yet reached consensus on how to translate this agreement into a formal offer, the shapes such an offer could take have been reduced to two, both of which have been declared to be acceptable, in principle, to the Yugoslav authorities.

With regard to enhanced surveillance, the one outstanding issue between the authorities and the banks was resolved when the authorities accepted an operative period from May 1986 until the end of 1991. The ICC is currently engaged in forging a consensus around one of two proposed pricing structures and it is hoped that by the end of August an offer will have been made and accepted, so that the final steps toward concluding the refinancing can be put in train.

III. Staff appraisal

Negotiations between Yugoslavia and its commercial bank creditors on the refinancing of maturities falling due in the period 1985-88 have reached an advanced stage, with agreement having been reached in principle on the modalities of enhanced surveillance to be requested of the Fund and on all economic terms and conditions of the refinancing agreement. The one outstanding issue concerns the structuring, but not the overall magnitude, of interest costs over the life of the loan. The staff believes on the basis of the discussions in London that a consensus among creditor banks can be reached within a reasonable time period, and that such a consensus offer would be acceptable to the Yugoslav authorities. Meanwhile, pending formal agreement on the refinancing package, the standstill on repayment of maturing debt in effect since January 1, 1985 has been prolonged until end-September 1985. In this light, it is proposed that the Executive Board find, for the purpose of allowing the purchase phased for the period after August 29 and before November 29 to proceed, that "satisfactory arrangements have been made" for the refinancing of maturities falling due to banks during the period of the stand-by arrangement. Subject to the determination that all other performance criteria applicable to the second purchase have been met, this finding would permit Yugoslavia to proceed with the purchase phased for end-August. Although it is not envisaged that delays in reaching final agreement on the refinancing would continue beyond early September, it is proposed that the end-November purchase be made contingent upon finding that agreement has been reached.

In view of the foregoing, the following draft decision is proposed for adoption by the Executive Board:

The Fund has been informed of the substantial progress of negotiations for the refinancing by Yugoslavia of maturities falling due during the period from January 1, 1985 until the expiration of the stand-by arrangement. In the light of this information, the Fund determines, for the purpose of purchases phased for the period before November 29, 1985 only, that the requirement in paragraph 4.e of the Stand-By Arrangement is met.