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PART A

Part A.

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Chancellors (Lawson) Papers:  
Fund Areas: The Guyana Support Group.

DD's: 25 Years

*Phil Lawson*

17/4/96

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FROM: H G WALSH  
DATE: 27 July 1988

CHANCELLOR

cc: Economic Secretary  
Sir Peter Middleton  
Sir Geoffrey Littler  
Mr Lankester o/r  
Mr Evans  
Mr Mountfield  
Mr Bottrill  
Mr Batt  
Ms Life  
Mr Kilpatrick  
Mr Tyrie

*Handwritten notes in red and black ink:*  
Not with push (ix) x(xv).  
OTU...  
Am v. doubtful  
Are you content with the...  
(para 55, Haggard)?

**ARREARS AT THE FUND AND BANK**

You may recall that the Interim Committee at its Spring Meeting asked the Executive Board of the IMF "to review the question of the overdue financial obligations and to submit a report at the next meeting of the Committee on measures to reduce and eventually eliminate arrears at the Fund". It is also coming up in the G10 discussions on the role of the Fund and Bank in the debt strategy, where the UK has been commissioned to prepare a paper. The attached internal paper considers arrears at both institutions. One of the most important issues to the possibility of introducing limited cross-default between them (paragraphs 34-39). The conclusions are contained in paragraphs 48-54.

2. The main general conclusion is that we should take action to deal with existing arrears and to discourage future arrears. Actions would be of two types:-

- i. Measures to help deal with major low-income IMF arrears cases including retroactive access to the ESAF where they are willing to undertake shadow adjustment programmes (the "carrot").
- ii. Measures to isolate existing countries not making an effort to adjust or repay and to discourage others from joining the arrears list (the "stick").

*Handwritten date:* 27/7

3. The most this combined approach could achieve by itself would be to contain the arrears problem to the present group of countries, and to deal with some of the minor cases. The intractable cases such as Sudan, Liberia and possibly also Zambia would require further measures to 2i above such as an extraordinary aid package. A contribution key would probably have to be agreed for each package, because historical aid contributions are not directly relevant precedents to packages aimed at the clearance of arrears at the IMF.

4. The recommendations are in paragraph 55. Recommendation ix (in favour of a presumptive form of cross default at the Fund and Bank including new project lending but not disbursements of existing loans) is not agreed by the ODA/FCO. They believe that a country which received nothing from the Bank because it is in arrears to the Fund would have little incentive to stay current with the Bank. This prospect they believe would seriously affect the Bank's market rating on its borrowing, although the Bank of England regard this as a small risk acceptable in relation to the benefit. Mr Cassell also has serious reservations about pushing for modified cross-default, mainly because of the difficulty of negotiating this in relation to the benefit that might be achieved.

5. The ODA/FCO also does not agree with recommendation xv, the withholding of new UK project aid where countries go into arrears at the IMF. Their view owes something to the wish to maintain discretion when there is a political reason for giving aid. Our proposals allow for this - although ODA would have to clear their lines with us on each such occasion. But they also feel that other donors may not co-operate: in particular, they feel, efforts now being made with some success to persuade other donors to cut off programme aid to a country in arrears would be jeopardised by trying to extend the cut off to new project aid. This is essentially a matter of tactics: of when such an initiative would stand the best chance of being adopted widely. But the UK should still adopt this policy as its own.

6. At the Fund, because of its special monetary character, we feel that more emphasis is necessary on external conditionality in programmes and in particular on repayment record and technical capacity to repay. This is given some attention in present IMF documentation and discussion, but we think much more needs to be done in future. We are also recommending that the present discretionary procedure for declaration of ineligibility at the Fund should have an automatic cut-off at six months after arrears arise. This would bring an end to the present situation where arrears' countries string the Board along with protestations of good intentions combined with token repayments, which is a waste of time for everyone.

7. The conclusion on provisioning (paragraphs 53 and 54) are that the Fund does not need to and should not provision, but should continue with its present two-tier reserve system. The World Bank is now reinforcing its provisioning, and this combined with its reserving policy should enable it to cope with the countries at present in non-accrual status and non-repayments by one of the three largest debtors (Brazil, Mexico and Argentina) but probably not two. There would be no point in provisioning against a mass declaration of non-repayment by the major debtors to the Bank.

X | 8. More attention would have to be given to packaging the proposals (if they are acceptable), to make sure there is a right balance between incentives and discipline. Mr Cassell's view is that, in order to get full benefit from our own initiative on retroactive access to the ESAF as a carrot to take some countries off the arrears list, it may be necessary to go along with the idea of "support groups" of developed countries which is favoured by the Managing Director - a watered-down version of the mentor approach. We have been very cautious on this so far.

9. The recommendations in paragraph 55 follow discussions with Mr Lankester and Sir Geoffrey Litter. Are you content with them? If we wished to pursue recommendations ix and xv, it would be necessary to persuade the Foreign Secretary - who has responsibility for the World Bank and aid - before the Berlin Meetings.

H.W.

H G WALSH

**ARREARS AT THE FUND AND BANK**

On 15 April the Interim Committee requested the Executive Board of the IMF "to review the question of the overdue financial obligations and to submit a report at the next meeting of the Committee on measures to reduce and eventually eliminate arrears". The IMF Board has now had a first discussion of arrears. Mr Cassell issued a "buff" statement which is attached. The present paper is intended to provide an overview of the arrears position at the Fund and Bank, and to reach some tentative conclusions and recommendations about an appropriate line for the UK to take.

Introduction

2. Arrears arise when debt is not serviced on time. This has consequences both for the country concerned - eventually it will become ineligible for disbursements at both Fund and Bank - and for the IFIs in terms of making good the shortfall. Arrears were fairly small in the early 1980s but have grown rapidly thereafter as earlier borrowing has come due for repayment. The growth of total arrears over the last several years has been:-

Table 1

|            | (\$m)        |             |              |             |              |             |              |
|------------|--------------|-------------|--------------|-------------|--------------|-------------|--------------|
|            | <u>12/84</u> | <u>6/85</u> | <u>12/85</u> | <u>6/86</u> | <u>12/86</u> | <u>6/87</u> | <u>12/87</u> |
| IMF        | 243          |             | 848          |             | 1414         |             | 2395         |
| World Bank |              | 86          |              | 322         |              | 630         | 845          |

1 SDR = \$1.366

3. Arrears are three times as large at the IMF as at the IBRD. They are concentrated in four countries (Zambia, Sudan, Liberia and Peru account for about 80 per cent). At the World Bank the top four (Peru, Syria, Nicaragua and Zambia) account for about 60 per cent of arrears. Eleven countries at the Fund have "complaint" status (two months or more in arrears) and thirteen at

the Bank are one month or more in arrears. The current total arrears position 1988 is summarised in the table below.

Table 2

ARREARS JUNE 1988 (IMF, IBRD, IDA)

|              | Total       | \$m | of which overdue<br>6 months or more |
|--------------|-------------|-----|--------------------------------------|
| IMF          | 2862        |     | 2258                                 |
| IBRD         | 1029        |     | 487                                  |
| IDA          | 19          |     | 9                                    |
| <hr/>        | <hr/>       |     | <hr/>                                |
| <b>TOTAL</b> | <b>3910</b> |     | <b>2754</b>                          |
|              | <hr/>       |     | <hr/>                                |

4. Unless the countries currently in arrears at the Fund get back on track, their arrears could total over \$5 billion by end-1990. At the Bank, projected arrears of countries in non-accrual status will amount to about \$1.9 billion by then. So combined arrears could amount to 5 per cent of total credit at both institutions together by 1990.

5. The Fund figure for arrears could be significantly higher if any further countries fell behind with payments. For instance, Zaire owes almost \$800m over 1988-90, Ivory Coast over \$550m, and Egypt over \$150m. Moreover, nearly 40 per cent of Fund credit is concentrated in Argentina, Brazil, Mexico, and Yugoslavia. These four could add as much as \$11 billion to arrears by the end of 1990 if they refused to repay. At the Bank, lending is less concentrated in the major debtors with Argentina, Brazil, Egypt, Mexico, Nigeria and Yugoslavia only accounting for about 27 per cent of loans outstanding. The difference is partly accounted for by the fact that India is a more important borrower at the Bank than at the Fund and China - an important Bank borrower - has no credit outstanding at the Fund. The Bank lends to a broader range of countries than the Fund, because in the main the Fund lends only to countries in need of an adjustment programme.

### Arrears at the Regional Development Banks

6. At the RDBs the pattern of arrears is broadly similar to that at the IBRD/IMF. At the AfDB arrears at the end of May amounted to \$101 million, 42 per cent of which is owed by Liberia. A policy of non-accrual after arrears of 12 months was introduced in May, as was a provisioning policy although no provisions have been made yet. At the IDB, arrears are essentially a short-term problem with all of the \$81.9 million outstanding at end-May being for less than 6 months. The countries mainly involved are Argentina, Colombia and Panama. Only one country, Nicaragua, has ever been in non-accrual status (for the period May-November 1987) but has since repaid its debts. At the AsDB arrears are minimal with the largest amounts outstanding owed by Vietnam at \$3.1 million and Afghanistan at \$2.3 million. At the Caribbean Development Bank (the smallest) arrears are a relatively large problem. Guyana owes \$18 million and has repaid nothing since 1982; disbursements were suspended in 1983 and provisions have been made. Antigua and Barbuda does not repay its obligations despite indications that it could do so.

### Characteristics of Arrears Countries

7. The main characteristics of debtors in arrears are shown in table A at the annex. Half of the 22 are in Africa (mainly low-income, debt-distressed), and the rest are in Latin America except for Kampuchea, Vietnam, Syria and Nicaragua. Peru is the only important arrears country outside Africa, and the only important arrears country with a GNP per head of over \$1,000. Sudan, as measured by its IMF arrears/export ratio of 109.7, would have the hardest task in earning enough to pay off its own arrears. Liberia comes next with 65.2. Peru stands out as a "won't pay" debtor.

### CONSEQUENCES OF ARREARS FOR DEBTORS

8. As things stand, the consequences for countries in arrears at the IFIs are:-



- i. At the Fund, obligations attract a "special charge" after they are 10 business days overdue. It is not penal, but levied so as to recover the direct financial costs to the Fund from late payment. At the World Bank Group and RDBs, there is normal interest charged on overdue principal repayments, but not interest on interest due.
- ii. Because arrears to the Fund mean automatic suspension of an SBA after a certain time, any Paris Club agreement would lapse and any new rescheduling would be refused, although this may mean simply that countries will finance themselves by building up arrears.
- iii. Major export credit agencies normally refuse to provide new cover except short-term trade lines/guarantees. This follows from arrears under Paris Club agreements rather than directly from arrears to the Fund.
- iv. Commercial banks refuse to provide credits to countries in arrears at the IMF other than highly restricted short-term trade lines. Although the London Club is more flexible than the Paris Club, they would normally refuse rescheduling.
- v. International Financial Institutions are legally independent. Countries ineligible at Fund are not necessarily ineligible for any disbursements at IDA and IBRD, although those ineligible at IBRD are ineligible at IDA and vice versa. Countries ineligible at the IMF and not in arrears at IBRD/IDA may however in practice be refused new IBRD/IDA policy-based lending, but this rests on judgements about the macro and sectoral policy environment rather than ineligibility at the Fund itself. Arrears to IBRD/IDA do not prevent lending by the IFC. There are

no necessary implications of ineligibility at the IMF/World Bank for access to credit at the RDBs. There are no direct consequences for ineligibility at the World Bank or IDA for the IMF, but IBRD/IDA arrears will form part of the financing gap that needs to be filled when a programme is set up.

- vi. The value of their commercial bank debt in the secondary markets will be reduced (but this can actually facilitate buy-backs).
- vii. Where the macroeconomic framework has broken down, new commitments of programme aid will normally be withheld by many countries, including the UK. A second stage can be reached under which at least some new capital aid is withheld as well, although in practice this may only happen if there are associated repayment credits (eg those under ECGD guarantee). Essential humanitarian aid and technical co-operation normally continues. These decisions are however only indirectly related to arrears at the IFIs.

#### FINANCIAL CONSEQUENCES OF ARREARS AT THE FUND AND BANK

9. The Fund and Bank have slightly different approaches to arrears. The Fund Board at its discretion may declare a country formally ineligible to make purchases (usually after 7-9 months of arrears build-up), but drawings are suspended immediately arrears occur. Disbursements (with minor exceptions) are automatically suspended at the Bank once a country has been in arrears for 75 days but there is no Board declaration of ineligibility.

#### Income

10. At both the Fund and Bank after six months of arrears the related shortfalls of income are absorbed into the Fund and Bank balance sheets because they no longer accrue. Only the Bank, however, has the formal category of "non-accrual status" which is both an accounting category and carries some of the same

opprobrium as "ineligibility" at the Fund. The cost of making interest arrears good ("deferred charges") at the Fund are shared equally between debtors and creditors. The former have to pay a higher rate of charge to make good one-half of the arrears of interest whereas adjustments are made to reduce the latter's rate of remuneration to produce the same effect. At the Bank, loss of income ultimately can only be made good under present arrangements by charging borrowers more by way of interest or fees.

### Capital Deficiencies

#### **IMF Practice**

11. The IMF (like the Bank) does not usually reschedule and never writes off capital. There is both a general reserve and a Special Contingent Account (SCA) which each increase by 5 per cent of the initial level of reserves at the beginning of the year. Reserves are financed by retained income (allowed for in the basic rate of charge) and the SCA is financed by the 50/50 burden sharing arrangements. The Fund's gold, worth over \$40 billion, means that it is financially secure and the Board has decided on past occasions that it does not also need to provision against specific risks.

#### World Bank Practice

12. The Bank's financial security ultimately rests with the callable capital of its members, the most reliable of which is contributed by OECD countries. But when the first long term arrears case arose in 1986 the Bank was concerned at the possible damaging impact on net income available to build up general reserves, and introduced a provisioning policy. This involved making 100 per cent provisions over a 5 year period against all loans outstanding to countries in arrears for 2 years or more. The basic purpose of the policy was:

- a) to present financial statements which were accepted by the financial markets as credible in the light of risks facing the bank.

b) to enable the Bank to avoid excessive volatility in future net income.

13. In 1986 only Nicaragua had long-term arrears but since then 7 additional countries have gone into non-accrual status, an indication of an increasing problem. But applying current provisioning policy would lead to a sudden major reduction in net income once these countries reached the 2-year trigger. As a result, the Bank reviewed its provisioning policy earlier this year and provisions will now be made against loans outstanding to all countries in non-accrual status, ie after arrears of 6-months. In August the Board will be asked to approve an initial amount of provisioning upon reaching non-accrual status of about 17 per cent of all loans outstanding to these countries and augmentation by 1 per cent of principal outstanding for each month that arrears continue - the augmentation rate to be reviewed periodically.

#### Recent Trends in Arrears Financing

14. Since the Fund does not attempt to make good delayed repurchases on a running basis, the only claims on the burden-sharing arrangements are:-

- i. To make good deferred charges (unpaid interest).
- ii. To build-up 5 per cent of reserves annually for the Special Contingent Account, as a quasi-provision (in addition to the 5 per cent build-up of the general reserve met from general income).

The sum of (i) and (ii) is the total claim on the burden-sharing arrangements:

Table 3

|                        | \$m           |               |               |
|------------------------|---------------|---------------|---------------|
|                        | <u>FY1987</u> | <u>FY1988</u> | <u>FY1989</u> |
| (i) Deferred Charges   | 248.3         | 210.5         | 265.7         |
| (ii) Additional Income | 38.2          | 82.8          | 102.0         |
| <b>Total</b>           | <u>286.5</u>  | <u>293.3</u>  | <u>367.7</u>  |

15. The rate of charge (for borrowers) has to be increased and the basic rate of remuneration (to debtors) decreased to raise amounts equal to the totals above. Some fairly large adjustments have had to be made to these: quarterly adjustments of about 0.5-0.75 per cent were made to charges and remuneration in FY87 and FY88. An adjustment of 0.7 per cent is expected in FY89. Because there is a remuneration floor of 85 per cent of the basic rate of remuneration agreed as part of the burden-sharing arrangements, there is a limit to which creditors can contribute to making good deferred charges and building up the Special Contingent Account. There is no formal limit on the contribution from debtors but, if it is assumed that reaching the floor would trigger the negotiation of new burden-sharing arrangements, it can be seen as a significant threshold for them too. Fund staff believe that the floor may be hit this quarter, so that burden-sharing may soon again arise as a subject for the Fund Board.

Implications for Reserves and Provisioning

16. The table below shows that there has been some improvement in the reserve ratios (as broadly defined to include the SCA at the Fund and provisions at the Bank) at both the Fund and Bank since 1986. But the reserves coverage of total arrears has declined by a half or more.

Table 4

|                   | <u>\$m (except ratios)</u> |             |             |
|-------------------|----------------------------|-------------|-------------|
|                   | IMF                        |             |             |
|                   | <u>1986</u>                | <u>1987</u> | <u>1988</u> |
| 1. Reserves + SCA | 1533                       | 1686        | 1852        |
| 2. Fund Credit    | 47318                      | 43228       | 38014       |
| 3. Ratio: 1/2 (%) | 3.2                        | 3.9         | 4.9         |
| 4. Arrears        | 910*                       | 1624*       | 2681        |
| 5. Ratio: 1/4     | 1.68                       | 1.03        | 0.69        |

Figures are for end-IMF financial year (end-April), except arrears (end-March).

|                           | IBRD        |             |             |
|---------------------------|-------------|-------------|-------------|
|                           | \$m         |             |             |
|                           | <u>1986</u> | <u>1987</u> | <u>1988</u> |
| 1. Reserves               | 5189        | 6576        | 8539        |
| 2. Cumulative provisions+ | 37          | 78          | 500         |
| 3. Loans outstanding      | 61064       | 75792       | 81807       |
| 4. Ratio: 1/3-2(%)*       | 8.5         | 8.7         | 9.3         |
| 5. Ratio: 1+2/3 (%)       | 8.6         | 8.8         | 11.0        |
| 6. Arrears                | 322         | 630         | 1029        |
| 7. Ratio: 1/6             | 16.11       | 10.43       | 8.29        |

June figures.

+ Provisions calculated on new basis.

\* Method of judging reserves used by Bank.

17. In the past, the Bank's policy on reserves was to have enough to cover all the loans outstanding to the largest borrower, which was held to about 10 per cent of total loans outstanding. As part of the agreement on the GCI, it has been decided that when the Board considers allocation of net income, the intention should be to retain all net income for building reserves unless reserves and surplus are at a level which, after deducting the loans

outstanding to countries in non-accrual status, would still represent 10% of the loan portfolio. Applying this policy will mean allocating all net income to reserve building for the time being.

#### PREVENTING ARREARS

18. An essential element is to try harder to prevent new arrears cases from arising. Sanctions which would tend to discourage "won't pay" countries from going into arrears are discussed below (paragraphs 19-38), but it would also be desirable to take measures to ensure that countries do not take on repayment responsibilities that they cannot meet. This is the responsibility of the management of the institutions and their Executive Boards as well as the countries involved. Because the objective is usually to improve repayment capacity by new programmes rather than to advance funds against high reserves or some other pre-existing capacity to repay, this means that programmes have to be sound before money is advanced. This has not been the case in a number of instances - eg Zaire and Argentina. Improving conventional programme conditionality should therefore contribute to avoiding arrears, as would a maximum of contingency leeway in programmes.

19. The problem of assessing capacity to repay arises at the IMF in particular since, once an IMF seal of approval has been obtained, a signal is sent to the World Bank, Paris Club, aid agencies etc, that credit can be extended. Examination of the IMF programme, and the country's track record on economic reform, is not sufficient by itself to ensure this. Increased attention than has been typical in the past should perhaps be given to:-

- i. The country's technical capacity to repay over the complete repayment period, including its other repayment commitments and the explicitly financial risks inherent in the programme.
- ii. The country's reserves, repayment record and the open market price/rating of its bank and securitised debt.

This means that the IMF, if it genuinely wishes to be repaid, might on some occasions not be able to implement programmes that are economically sound - in the sense of yielding an improvement in the country's financial position - unless other resources (eg aid) can be found which makes repayment more likely.

**POSSIBLE SANCTIONS: IMF**

20. In the past, the UK has been at pains not to press for sanctions which would not have much effect: this would only reduce the Fund's credibility. Such sanctions have also been thought likely (where ability rather than willingness to repay is involved) to make the balance of payments situation of the country worse, making ultimate repayment more unlikely. But the time has come to re-examine our position. None of the options considered below might have much effect on countries now in arrears, but could nonetheless have a suitable deterrent effect on others.

21. The IMF has a greater problem in exercising leverage because, unlike the World Bank, it is not now a net supplier of credit. It would be desirable to have a test of "co-operation with the Fund" to separate "can't pay" from "won't pay" cases of ineligibility. In practice there is no clear dividing line. But, at the extremities, clearly a country undertaking a shadow programme and making some attempt to clear arrears is in a different position from one that has lost contact with the Fund or has made a unilateral statement of unwillingness to repay its obligations. A framework for judging arrears cases is provided on page 3 of Mr Cassell's buff attached. Sudan and Zambia have perhaps the most legitimate claims that a good part of their problems are exogenous and Peru the least. Table 5 below examines exogenous/ endogenous factors for four important arrears cases.



Table 5

Causes of Arrears

Exogenous

Policy/Last Fund  
Programme

Zambia

70 per cent real fall in copper price (90 per cent of exports are copper) between 1973-1986. Should never have borrowed - or been lent - large amounts when copper prices were high.

20-month 1986 SBA at IMF broke down: public expenditure and monetary overruns. Shortfalls in copper exports and donor support. 10 per cent debt service limit.

Liberia

Deterioration in price of main exports (iron ore and rubber). Terms of trade declined by 13 per cent in six years to 1986/87.

1984 SBA (last one) broke down. Fiscal policy was especially weak.

Sudan

Drought 1982-85. One million inward refugees then.

Had series of programmes including EFF. Latest 1-year SBA in 1984 broke down. Excessive government spending and government and parastatal borrowed. Overvalued exchange rate. Elaborate government price and exchange controls. Civil conflict which is still continuing.

Peru

Terms of trade declined sharply in early 1980s after some recovery from long-term decline in late 1970s.

Long had erratic changes in policy. Had an SBA in 1984 which broke down on all fronts: fiscal, inflation and external. Broke off relations with Fund for political reasons. No Article IV consultations 1984-87. Over-borrowed country: originated 10 per cent debt service limitation. Elaborate exchange and price controls.

IMF: Possible Legal Sanctions

22. One of the measures that could be taken in cases of non-cooperation would be to attempt to sell the currencies that form the quotas of countries in arrears and help pay for arrears with the proceeds. The legal position would have to be ascertained, including whether SDR contributions could similarly be called up. But, since most of the arrangements for quotas are made through national central banks, it is likely that there would be refusal to meet a call from the IMF for their currency for this purpose even if it could somehow be converted into a currency usable by the Fund - which is most unlikely. The amounts involved would make only a small contribution to the clearance of arrears. A refusal to pay up would mean following the claim up in the courts with very limited chances of success because of the special nature of IMF obligations.

23. Approaches to the courts would also be very unlikely to be successful in terms of getting a repurchase from the member concerned, but the fact that legal proceedings were outstanding could damage the member's credit standing or at least cause embarrassment, which is the desired effect.

24. Another option would be to suspend or expel the member from the IMF. Suspension (or expulsion) would be a merely formal action. It is hard to see that it would be more effective than a simple declaration of ineligibility and might cause a permanent break in relations. A more limited action would simply be to recall the IMF representative in the country concerned if there is one.

25. The arguments for a completely automatic system of ineligibility at the IMF might have some merits, although it can be argued that the present partly discretionary system allows more leverage to be put on the country concerned in trying to piece a programme together. But it also wastes the time of the Fund Board, because countries in arrears try to string along the Board with promises, often accompanied by token repayments just before Board meetings. A more automatic ineligibility (eg an absolute time limit for arrears) might however have a role in the present tougher climate, although it probably would add little to the existing automatic sanction of immediately stopping disbursements. The best course would seem to be to have a cut-off under which ineligibility automatically become effective after six months arrears, the same period at which non-accrual status becomes effective at the Bank.

#### IMF: Financial Sanctions

26. Quota increases for countries in arrears should be frozen. It would not make their economic situation any worse, and would form a clear mark of disapproval without a permanent break in relations.

27. Increasing the special charge on overdue obligations (now between  $\frac{1}{2}$ -1 per cent) to penal levels would make it harder for countries who wish to do so to repay their obligations. Neither would it have much of a role in cases where the arrears had arisen because of unwillingness to repay, although it might deter future cases. Withdrawal of technical co-operation could however play a role in "won't pay" cases. This option is worth serious consideration.

28. In the past, the idea of formal notification of arrears by the IMF to other institutions has been rejected because it might give rise to inappropriate requests for reciprocity from the other institutions. For instance, the US could ask the IMF to help enforce economic sanctions against South Africa or labour laws in Chile. But the Fund should have another look at this. One option would be to notify arrears to the OECD, with a view to getting the country off cover or at least ineligible for any privileges under the OECD Export Credit Consensus (inclusion in Category III). Other organisations that might be notified include the EIB, and the RDBs. There should also be monthly notification of arrears at the Fund and Bank to the President of the Paris Club by the Treasurers of the two institutions for the avoidance of doubt. Lists of countries in arrears (with amounts) should be published in the Annual Reports or separately.

#### **WORLD BANK**

29. At the World Bank, there seems every reason to begin to charge interest on interest when repayments are overdue except where the Bank waives this - eg because the particular currency specified for repayment was unobtainable. This would penalise countries that are merely administratively sloppy in making their payments, or have other legal or Parliamentary difficulties in making the repayments on time, as well as the more serious case of countries who do not want to repay at all. It has the advantage of boosting net income at a time when it is under threat from arrears (and the related need to provision) and would stop countries delaying repayments intentionally up to the 75-day limit when they are refused new disbursements.

30. There is little possibility of asset seizure by the World Bank unless an asset has been made the security for a specific loan, because major issues of principle involving the right to distrain assets would have to be settled by an international tribunal or court as provided for in the General Loan Conditions. (This possibility has not been pursued even by the commercial banks vis-a-vis sovereign borrowers). But when new World Bank

Group loans are made to countries who have recently been in arrears or are otherwise poor credit risks and assets are available against which a charge could be made - eg Zambian copper or Sierra Leonian diamonds - security could be requested by the World Bank. We could ask the World Bank staff to look at this idea. An obvious practical difficulty is multiple pledges of the same asset and enforceability.

31. The equivalent of calling up a quota contribution at the IMF would be calling up its capital (including cashing promissory notes and its non-paid in capital) to help pay off a country's arrears at the World Bank. This measure would require a change in the Bank's Articles and they (in all probability) would not pay up anyway whatever the Articles said.

32. In 1987 LDCs accounted for almost \$2 billion of goods and services supplied for World Bank projects/programmes. It would be possible to declare arrears countries ineligible as suppliers (at the slight risk of cutting off the most efficient source of supply).

33. Another effective sanction might be for the Bank not even to consider a loan application during a period of suspension unless there was some chance of coaxing a recalcitrant country back on track; the period before suspension took effect could also be accelerated to fewer than 75 days. The latter proposal would involve better financial discipline, but the Bank might in return have to accept repayment in currencies it did not want in cases where the currency it called could not be obtained within the deadline.

#### General Cross-Default

34. Another reform that might be introduced is to have a form of cross-default between the two major Bretton Woods institutions so that, if a country was cut off from disbursements at one, there would be no question of receiving any disbursements or any new credit from the other. This seems to be worth serious

consideration, especially since only the IBRD and IDA, not the Fund, is a net supplier of credit.

35. We would not wish to stop all World Bank disbursements in response to a country becoming ineligible at the Fund. This would pose considerable risks to the Bank's own arrears position because the incentive to repay which comes from continuing to receive positive net lending would disappear. It also does not make economic sense (say) to leave an African road project financed by IDA half built (although this is what happens if a country goes into arrears at IBRD or IDA). So cross default could most easily be applied to new policy-based lending (including new loan tranches) and new projects.

36. We should also not want to apply cross default if a country, despite being in arrears to the Fund, had a shadow programme and was making efforts to get back to normal relations. In such cases, new policy-based funding from the IBRD or IDA should be available to help finance the shadow programme, and help the country concerned keep as up to date as possible with its current IMF commitments to avoid a further build-up of arrears.

37. Cross default might however be useful in cases of selective debt service by 'won't pay' cases. There is therefore a case for introducing cross default between the IMF and IBRD to discourage countries such as Argentina from possibly going into arrears at the Fund while remaining current at the Bank. The main danger of cross default at the World Bank is that countries in arrears at the IMF would have less incentive to keep current with the Bank if they were blocked from receiving new loans. Argentina for instance might be discouraged from staying current at the Bank if it did not wish to repay the Fund, which would have important adverse implications for the Bank's finances. This risk has to be balanced against the greater disincentive to go into arrears with the Fund.

38. Cross default (in however modified and discretionary a form) would be seen by the LDCs as a particularly objectionable form of cross-conditionality (though they should recognise that unless the

arrears problems of the two IFIs are contained, the LDCs would be the main losers). It also carries an increased financial risk to the World Bank. But we still have to ask ourselves whether we should go on supporting IDA/IBRD loans to countries already in arrears with the Fund (or, less likely, the other way round). There must come a point when we do not - though defining that point, still more getting agreement in the Fund and Bank Boards, would be very difficult.

39. The right balance would seem to be a form of "presumptive" cross-default, with the Bank Board exempting cases of arrears at the Fund from being barred from receiving IBRD/IDA funds if the grounds were strong enough - eg an IMF shadow programme was in place - and vice versa. The form it should take would be for discussion in the Fund and Bank Boards. Since the World Bank already withholds new policy-based lending (and also tranches of existing policy-based loans) where the macroeconomic framework is inadequate, this could be extended to a presumption that new project loans would be refused as well. And the "trigger" would be proposed to be not an inadequate macroeconomic framework but specifically ineligibility at the Fund. The trigger at the Fund would be non-accrual status at the IBRD or IDA. Countries in non-accrual status at IBRD/IDA would be ineligible for new Fund programmes.

#### ESAF and Arrears

40. At the Spring Meetings the Chancellor suggested that in those cases where a country wanted to get back into a Fund programme, it might be given backdated credit under the ESAF so that where it ran a successful shadow programme for a year or so, and after it cleared its arrears with a bridging loan, the entitlement to the first drawing on the ESAF could be made larger by being effectively backdated to the start of the shadow programme. This could then help pay back the bridging loan. (This proposal received a wide measure of support in the IMF Board discussion of 19 July, including from the Americans, although the Germans are opposed and the Canadians, Dutch, Belgium, Saudis and French have yet to express a view). In the case of the Sudan, we have also

discussed bilateral aid to assist a shadow programme and have hinted that we might be prepared to do this for Sierra Leone.

41. The above is very much a "carrot" approach, and could lead to the clearance of some arrears. But none of the eligible countries have expressed a willingness to undertake the necessary reform (Sudan's shadow programme has not been successful) so that it is by no means clear when this approach will get off the ground. In the case of the most intractable cases such as Sudan it is clear that a major aid effort will be required as well as retroactive access to the ESAF unless the Fund were to breach its normal rule and allow rescheduling. This is undesirable because of the bad precedent it would set. For this reason it is unlikely to be acceptable to other major creditors, although rescheduling is permitted under the IMF's Articles. Nevertheless, we should not rule it out: rescheduling might have to be the Fund's exceptional response to an exceptional situation.

42. A major rescue package, if offered to (say) Sudan, would effectively turn it into a "won't pay" case if it refused to adopt an adequate programme. In those circumstances, the "stick" of limited cross default would be a legitimate response, especially since the Bank's development and structural adjustment objectives would also be met by a shadow programme.

#### "Mentor" Approach

43. The Fund is well aware that, to bring back into the fold any of its serious arrears cases, widespread co-operation from other IFIs, and from governments (including aid agencies) will be required. Camdessus' first idea was to establish a "mentor" among the G7 to co-ordinate each arrears case.

44. This idea has developed into that of a "support group" for a country in arrears, again to co-ordinate efforts to clear arrears. The support group could be chaired by the mentor. The support group, and in particular the mentor, would assist the country and the Fund in drawing up and implementing a shadow programme, closely monitoring developments and, where appropriate, take the



lead in devising and drumming up support for debt buy-back schemes.

45. Thus far, the US and Saudi Arabia have taken on at least some of the role of mentors for Sudan, and though meetings in Washington have in fact been chaired by the Fund, they have also involved people from capitals as well as from Executive Directors' offices. In the case of Guyana, Canada seems to have taken on the role of mentor and is likely to try to do the same at some stage for Zambia.

46. There are difficulties with these approaches, and we have so far taken an extremely cautious attitude. The task of drawing up a shadow programme for the countries concerned belongs primarily to the IFIs and the specific task of convening consultative groups belongs to the World Bank. So, we need to be clear about how exactly a "support group" would fit into these arrangements. We know that other G7 countries also have reservations. But this approach might at least heighten awareness of the arrears problem across IFIs amongst the major countries, and help avoid the problem of a different attitude being taken in the Fund and Bank Boards by developed countries with different representation (Ministry of Finance/Aid Ministry) on the Fund and Bank Boards.

47. We will continue to take a cautious line and consult you about any suggestions for a more direct UK role. But the later, more informal, approaches are a distinct improvement on what went before and we would not want to be left out of discussions in these informal groups.

## CONCLUSIONS

48. Arrears are a growing problem at the Fund and Bank, but are concentrated in only a few countries. Sudan, Zambia, Liberia and Peru account for two-thirds of combined arrears at the Fund and Bank.

49. Aside from Argentina, Nigeria and Yugoslavia, who have only small arrears and are not ineligible at either of the IFIs, none of the major debtors are in arrears except for Peru, which stands out as the major "won't pay" debtor.

50. Default by more than one of the major debtors would cause difficulties at the IFIs which could not easily be coped with by existing mechanisms. Special measures would be required - possibly including the calling up of World Bank capital. The leverage provided by the World Bank Group as the preponderate net supplier of capital to these countries is important in providing a disincentive for them to go into default.

51. Action to deal with and discourage arrears should include both:-

- i. Measures to help deal with major IMF arrears cases (except Peru) using retroactive access to the ESAF where they are willing to undertake adjustment programmes (the "carrot").
- ii. Measures to isolate existing countries not making an effort to adjust or repay and to discourage others from joining the arrears list (the "stick").

52. The most this combined approach could achieve would be to contain the arrears problem to the present group of countries, and to take out some of the minor cases. The most difficult cases (Sudan, Liberia and possibly also Zambia) could probably not be resolved without special measures by the Fund itself, to which there would be resistance in the Board because of the risk of contagion.

53. The IMF deals with the consequences of arrears by a number of mechanisms which fall short of case-by-case provisioning. These have evolved largely in line with the status of the IMF as a monetary institution with revolving resources. To continue with the burden-sharing arrangements, the Special Contingent Account and a general reserve is probably the best practicable approach. Given its gold holdings, there is probably no need for provisioning at the Fund.

54. The World Bank is well on the way to adopting a new policy on provisioning, which would provide for a staged build-up of provisions against arrears cases as soon as they get into non-accrual status. It is also building up its general reserve. Combined, these should deal with the existing arrears cases at the World Bank, and with any future cases aside from two or more of the major middle income debtors going into default simultaneously.

Recommendations:-

55. The main recommendations are:-

IMF

- i. The UK should continue to follow up the proposal made by the Chancellor at the Spring IMF/IBRD Meetings to help deal with major Sub-Saharan arrears cases through retroactive access to the ESAF when these countries adopt shadow programmes as a lead-in to an ESAF.
- ii. The most intractable IMF arrears cases cannot be dealt with by (i) above even combined with strong adjustment. At the least, exceptional efforts would be required through the existing Consultative Group process, and a contribution basis would have to be decided in each case. There might also be pressure for reschedulings at the Fund and Bank, eg for Sudan. This would set a bad precedent, and would be acceptable only as a last resort at the Fund. At the

IBRD, because of the effect on its market standing, it would be completely unacceptable while at IDA the terms are already very concessional and so rescheduling would be difficult to justify and lead to demands for accelerated and/or increased contributions by donors.

- iii. There needs to be a renewed emphasis on external conditionality in all IMF programmes and in particular on repayment record and technical capacity to repay. The programmes should include provision for adequate technical assistance to help with implementation.
  
- iv. We should support the freezing of quota increases for countries ineligible at the IMF.
  
- v. Management should seriously consider on a case-by-case basis the withholding of IMF/IBRD technical assistance and the recall of local IMF and IBRD representatives from unco-operative countries.
  
- vi. The arguments for a more automatic system of ineligibility at the Fund run both ways and the staff would recommend against it. It may not have much additional effect, given Fund policy of cutting off disbursements immediately arrears appear. But a prolonged and discretionary procedure may delay repayments since countries seem often to believe that they can string the Board along with protestations of good intentions combined with token repayments. This can waste Board time. The recommended option would be to retain the present discretionary procedure but to have an automatic cut-off at (say) six months after arrears arise when members would automatically become ineligible.

World Bank

- vii. At the World Bank, interest should normally be charged on interest overdue, to discourage intentional arrears in the period up to the 75-day disbursement cut-off.
  
- viii. The World Bank Board should not consider loan proposals while a country is suspended from receiving disbursements. The ban on considering loan proposals should however be discretionary and should not for instance apply to countries that are negotiating arrangements to repay arrears or need to know the World Bank's role in a possible shadow programme being negotiated with the IMF.
  
- ix. The World Bank already applies informally a policy of not making new policy-based loans to countries with an inadequate macroeconomic framework; this requires co-operation with the IMF. It may also withhold tranche release for loans in these circumstances. This approach should be extended to new project lending on a presumptive basis using a new "trigger" of ineligibility at the Fund rather than a separate judgement about an inadequate macroeconomic framework. This policy should not apply to countries with IMF shadow programmes so as to encourage the adoption of such programmes. IBRD/IDA finance in these circumstances could help countries keep current with IMF obligations to avoid a further build-up of arrears. Nor would it necessarily apply where technical support and project lending are essential in sustaining minimally sensible policies during difficult times. As a quid pro quo, the IMF rules would be changed so that countries would be ineligible for new full programmes when they were in non-accrual status at IBRD/IDA.
  
- x. There should be a procurement ban from countries in non-accrual status.

- xii. Other measures which might be taken to discourage arrears - asset seizure, calling up of quotas or callable capital of debtors, raising charges on overdue obligations to penal levels, use of suspension or expulsion - be ineffective in practice in the typical arrears case.
- xiii. The idea of collateralising or securing new World Bank lending to countries with bad repayments records should be explored with Bank management. (It probably cannot be applied to the Fund but this should be verified with the IMF Legal Department).
- xiv. Formal notification of arrears at the IMF and the World Bank should be made to the Regional Development Banks, the EIB, OECD, and the Paris Club. Lists of countries in arrears (with amounts) should be published more prominently in the Annual Reports or separately.
- xv. The Treasurers of the Fund and Bank should send a monthly statement of arrears to the President of the Paris Club.

Aid

- xvi. ODA should stop programme aid and should seriously consider on a case-by-case basis the withholding of new capital aid to countries ineligible at the Fund or in non-accrual status at the Bank in the absence of a shadow programme approved by the Fund. This would be on the same basis as the policy recommended for the World Bank at ix above. (Exceptions would have to be agreed with the Treasury). We should persuade other countries to adopt the same policy.

## COUNTRIES IN ARREARS TO THE IMF, IBRD, AND IDA: EARLY 1988

| COUNTRY          | TOTAL ARREARS<br>\$M | ARREARS/<br>EXPORTS<br>% | ARREARS TO:<br>IMF<br>\$M | IBRD<br>\$M | IDA<br>\$M | EXPORTS OF<br>GOODS & SERVICES<br>\$M | INTEREST<br>SERVICE<br>RATIO % | DEBT/<br>EXPORTS | LIDD<br>SIBIUS | GNP PER<br>CAPITA<br>\$ 1986 |
|------------------|----------------------|--------------------------|---------------------------|-------------|------------|---------------------------------------|--------------------------------|------------------|----------------|------------------------------|
| Tanzania         | 7                    | 1.6                      |                           | 5           | 2          | 458                                   | 22.5                           | 8.0              | q              | 240                          |
| Somalia          | 30                   | 18.3                     | 30 **                     |             |            | 162                                   | 33.0                           | 8.7              | e              | 280                          |
| Kenya            | 16                   | 0.8                      |                           | 16          |            | 1910                                  | 10.0                           | 1.9              | e              | 300                          |
| Zambia           | 621                  | 38.2                     | 536 **                    | 82 *        | 3 *        | 1625                                  | 11.1                           | 2.2              | e              | 300                          |
| Sierra Leone     | 48                   | 27.5                     | 43 **                     | 3 *         | 2 *        | 174                                   | 7.3                            | 2.6              | e              | 310                          |
| Sudan            | 792                  | 109.7                    | 792 **                    |             | 0          | 722                                   | 44.7                           | 9.8              | e              | 320                          |
| Kampuchea        | 43                   | ..                       | 43 ***                    |             |            | ..                                    | ..                             | ..               |                | ..                           |
| Vietnam          | 113                  | ..                       | 113 **                    |             |            | ..                                    | ..                             | ..               |                | ..                           |
| Liberia          | 303                  | 65.2                     | 268 **                    | 34 *        | 1 *        | 464                                   | 9.4                            | 2.2              |                | 450                          |
| Guyana           | 126                  | ..                       | 101 **                    | 26 *        |            | ..                                    | ..                             | 2.8              |                | 500                          |
| Bolivia          | 8                    | 1.2                      |                           | 8           | 0          | 683                                   | 29.0                           | 5.2              |                | 540                          |
| Nigeria          | 105                  | 1.5                      |                           | 105         |            | 7076                                  | 15.4                           | 3.0              |                | 640                          |
| Cote d'Ivoire    | 54                   | 1.5                      |                           | 54          |            | 3703                                  | 16.6                           | 1.8              |                | 740                          |
| Honduras         | 37                   | 3.6                      | 13                        | 23          | 0          | 1029                                  | 12.9                           | 2.3              |                | 740                          |
| Nicaragua        | 121                  | 49.0                     |                           | 118 *       | 3 *        | 247                                   | 120.4                          | 21.6             |                | 790                          |
| Peru             | 817                  | 24.0                     | 534 **                    | 283 *       |            | 3398                                  | 28.4                           | 1.8              |                | 1130                         |
| Ecuador          | 20                   | 0.8                      |                           | 20          | 0          | 2617                                  | 27.3                           | 3.0              |                | 1160                         |
| Colombia         | 13                   | 0.2                      |                           | 13          |            | 6497                                  | 16.4                           | 1.8              |                | 1230                         |
| Syrian Arab Rep. | 126                  | 6.6                      |                           | 124         | 2 *        | 1901                                  | 6.3                            | 1.6              |                | 1560                         |
| Yugoslavia       | 13                   | 0.1                      |                           | 13          |            | 17441                                 | 8.7                            | 0.8              |                | 2300                         |
| Panama           | 59                   | 1.0                      | 22                        | 37 *        |            | 6161                                  | 4.9                            | 0.6              |                | 2330                         |
| Argentina        | 60                   | 0.7                      |                           | 60          |            | 9161                                  | 41.9                           | 4.2              |                | 2350                         |
| Others+          | 294                  | ..                       | 246                       | 44          | 4          | ..                                    | ..                             | ..               |                | ..                           |
| Total            | 3824                 | 5.0 a                    | 2740                      | 1067        | 17         | 65429                                 | 18.0 a                         | 2.1 a            |                | ..                           |

NOTE: IMF overdue payments as at 31 Jan 1988: converted to \$ at \$1.366 per SDR

IBRD, IDA overdue service payments as at 17 May 1988

\* Countries with non-accrual status; disbursements suspended

\*\* Ineligible; \*\*\* out-of-contact

q = qualifier a excluding 'others'  
e = eligible + see notes to table

**NOTES TO TABLE**

Some countries which have overdue obligations to the IMF/IBRD/IDA have been excluded from the analysis. Countries included cover those where either the amount of arrears is greater than \$10m or where the arrears/exports ratio is higher than 1%. Countries excluded but in arrears are: Burkina-Faso, Guinea-Bissau, Mali, Uganda, Burundi, Benin, Senegal, Afghanistan, Mauritania, Yemen PDR, Morocco, Dominican Republic, Egypt, El Salvador, Jamaica, Paraguay, Cameroon, Guatemala, Congo, Tunisia, Costa Rica, and Lebanon.

Col. 1 Low-Income Debt-Distressed countries are identified as q = qualifiers; e = eligible.

Col. 2 Data drawn from the 1988 update of the World Bank Atlas

Col. 3 Data drawn from EBS/87/252/Supp. 01. SDR figures converted to \$ at end-January rate. Overdue financial obligations include repurchases, charges, and assessments in the General Resources Account, net SDR charges, repayments and interest on Trust Funds and SAF loans, and special charges loans, and special charges

Cols. 4,5 Data drawn from Sec M88-553 and IDA/SecM88-153 respectively. Figures are overdue service payments (excluding those overdue for less than 30 days) due for less than 90 days

Col. 6 The sum of cols. 3,4, and 5

Col. 7 Exports of goods and services (on a balance of payments basis). From World Debt Tables, 1987/8 edition

Col. 8 Col. 6/Col. 7      Col. 9 Col. 6/Col. 7

Col. 9 Interest due on total long-term debt for 1986 as projected in the World Debt Tables, 1986/7 edition



Col. 10 Col. 9/Col. 7

1. 11 Total public and publicly guaranteed long-term debt outstanding and disbursed/exports of goods and services. From World Debt Tables, 1987/8 edition.

July 18, 1988 - 88/134

Statement by Mr. Cassell on  
Overdue Financial Obligations to the Fund  
Executive Board Meeting 88/107  
July 19, 1988

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Arrears to the Fund are rightly being treated as a matter of the greatest concern. They strike at the roots of the Fund as a co-operative institution. I therefore welcome the opportunity of this review to examine ways in which we might deal more decisively with the problem.

It needs to be said at the outset that there are no miracle cures and no neat technical fixes that will resolve the arrears problem at a stroke. Any initiative to break the stranglehold that arrears have on some members will involve exceptional efforts from the member, the Fund and other members of the international financial community. Since arrears are generally the symptom of severe economic and financial difficulties, the thrust of any realistic solution must be directed at resolving these underlying problems. The prerequisite for any attempt to resolve the arrears problem must be a committed and sustained effort by members in arrears to correct their underlying imbalances.

Where there is full commitment, the Fund must offer a life-line. Like the staff, I recognise the risks of a new approach but see even greater danger - both to the members concerned and to the Fund - in inaction. The Fund needs to act boldly and urgently if it is to avoid having disruptive solutions forced upon it. My authorities have proposed retroactive access to the ESAF - on which I circulated a statement on 28 June - as a way of helping low-income members with protracted arrears to extricate themselves from their predicament without undermining the policies which safeguard the Fund. This proposal would seem to fit in well with the "stick and carrot" approach which is set out by the staff in EBS/88/123 and which provides a most helpful basis for our review.

#### Intensified Collaboration

My authorities strongly endorse the need to "offer new opportunities for members to resolve their problems through collaboration with the Fund". The proposal for retroactive access to the ESAF is one way. It is fully consistent with the staff's approach. Indeed, it can be seen as a mechanism for the "acceleration of disbursements under a new Fund arrangement" mentioned on page 6 of EBS/88/123. It simply brings into sharper relief the strategy proposed by the staff and fills out their proposal for a "more precise framework for organising the efforts of the main parties". By providing a concrete arrangement on which creditors and donors can more clearly focus their efforts, it should help catalyse a broad range of external assistance.

Retroactive access to the ESAF should also be able to play a broader catalytic role. At the moment, it is difficult to present a convincing case to other creditors and donors for participation in an exercise that has, as an important aim, the clearance of arrears to the Fund. It will be no easy task to recruit other institutions. Aid agencies are as a rule reluctant to release development funds for debt service, and a number of them display little sympathy with the Fund. As recent discussions about one member in arrears have revealed, the rest of the international financial community is loath to commit exceptional resources to clear arrears to the Fund while the Fund itself offers nothing more than a vague possibility of future financial assistance. Retroactive access to the ESAF could provide other creditors and donors with greater confidence about the Fund's full participation by making explicit the way in which the Fund could once again become involved in the financing of a member in arrears (once the obstacle of arrears has been removed).

The exceptional efforts required from the wider international financial community clearly require close consultation and co-ordination between the Fund, and other creditor and donor organisations. Collaborative machinery will have to be developed. The staff have put forward some interesting suggestions for ad hoc groups of senior officials drawn from creditor and donor agencies to meet in "support groups" and for corresponding Executive Directors to form a "task force". If these ideas are to be pursued, they will obviously have to be developed further. We must be clear about the role and responsibilities of such ad hoc groups, in particular, their relationship to the Executive Board. At the same time, we must recognise that the idea of ad hoc groups will have to be adapted to reflect the wide differences that exist between arrears cases, both in terms of their particular economic circumstances and the identity of the main creditors and donors.

#### Remedial Action

Turning now to the remedial actions proposed by the staff, we must avoid placing any reliance on "paper tigers", which are only likely to end up by mauling the credibility of the Fund.

But, having chosen remedial measures carefully, we should apply them resolutely. This will require a broad consensus in the Board, which will in turn depend on some assurance that remedial actions will not be applied prematurely but will be applied uniformly. The need for uniformity of treatment entails a consistent framework within which we can objectively determine the relative willingness of members to co-operate with the Fund in efforts to clear their arrears.

I am disappointed that the staff have not been able to develop broad indicators to help distinguish "unwillingness" from "inability" to pay. I am surprised that they have felt unable to provide the Board with any details of their work on the subject following the requests made at our meeting of 10 February. The Board is not looking for mechanistic systems of assessment. What is sought is largely a formalisation of the

systems of assessment. What is sought is largely a formalisation of the criteria currently used by the Board ad hoc in assessing a member's record of co-operation. I would therefore ask the staff to return to this question.

An appropriate framework should include an assessment of a member's capacity to make payments to the Fund and its record of co-operation. Assessment of capacity to repay might include:

- i. official reserve holdings;
- ii. evidence of debt service payments other than to the Fund;
- ii. estimated foreign exchange inflows and implied capacity to earn foreign exchange, taking into account the estimated benefit from possible corrective policy actions, the impact of exogenous external developments, and support from creditors and donors.

Evidence of co-operation should be measured largely in terms of whether there have been any attempts to make payments in proportion to the estimated capacity to pay, as measured above, and whether a member's pattern of debt service has discriminated against the Fund. The degree to which a member is attempting to regularise its position with the Fund could be measured in terms of whether payments were being made to:

- i. maintain some regular pattern of payment; and
- ii. meet future obligations - either totally or just charges; and
- iii. clear arrears according to an announced, fixed schedule - either totally or just accumulated charges.

In addition, the test of co-operation for a member in arrears should include more general criteria covering:

- i. willingness to co-operate with the Fund in Article IV and ad hoc consultations;
- ii. prompt provision of adequate statistics;
- iii. prompt settlement of maintenance of value obligations.

Once we are reasonably confident that we can distinguish between different degrees of co-operation, remedial actions can be applied in a resolute manner. Of the measures suggested by the staff, I can endorse fully the proposals on (c) technical assistance (although more information might be included in the briefing offered to the Board when reviewing arrears cases) and (d) quota increases for members in arrears. These measures are justified fully by the principle that the Fund should not offer the benefits of normal co-operation to members judged not be co-operating fully.

As regards the other proposals made by the staff - (a) collaboration with other institutions and publicity, (b) penalty charges and (c) compulsory withdrawal from the Fund - I have some reservations. Greater publicity might polarize our relations with a member and unhelpfully circumscribe the scope for discreet negotiation. However, the Fund has a duty not to cover up the inappropriate policies and actions of members where these may undermine the operation of the open trade and payments system. I would therefore support direct communication with other official financial organisations, and the publication of data identifying the arrears of particular members in the Annual Report and in press communiques issued at the time of a declaration of ineligibility and after Board reviews. I am uneasy about the idea of the Fund initiating direct communication with private institutions, though I think it should be ready to answer specific queries about protracted arrears from private entities.

I am attracted in principle by the idea of penalty charges but see little point in practice if we merely end up increasing the cost of an eventual solution. This is unlikely to help us mobilise the support of the rest of the international financial community in clearing members' arrears to the Fund. The basic problem is that the Fund will only ever be able to collect penalty charges from members who begin to co-operate. In this sense, penalty charges large enough to be significant could act as a disincentive to normalise relations. It seems pointless to suggest that such charges should be waived if co-operation is resumed: this would hardly make for a credible deterrent. In addition, while there would seem to be little difficulty with a system of penalty charges applied to members unwilling/able to pay the Fund, which can be waived for those who are willing/unable, a problem arises with those judged unwilling/unable.

A compromise may be to have a system of penalty charges that can be waived if partial payments are being made to the Fund that are sufficient, for example, to prevent the further accumulation of arrears or at least to cover normal charges.

At this stage, I would not rule out compulsory withdrawal from the Fund as a last resort, but further thought needs to be given to the implications of such a policy.

#### Balancing Remedial Actions and Intensified Collaboration

The staff paper outlines a balance between "the promise of a co-operative and positive approach...if [members in arrears]...are prepared to demonstrate concretely their own active collaboration" and a demonstration of "the Fund membership's determination to deal resolutely with members that are not prepared to collaborate in maintaining or normalizing their relations with the institution" (p3). And the staff also note the need to pay particular attention to the "timing" of remedial actions (p7). It would seem logical to make such actions dependent on failure to co-operate or to improve co-operation. Perhaps we could in this way devise a more active arrears strategy. Members in arrears would

be presented with a series of choices, each one leading either to the next step in the process of intensified collaboration or to further remedial action - in effect, a "decision tree", the structure of which would be designed to encourage movement along an appropriate path leading towards the full clearance of the arrears.

### Preventive Action

The third arm of the staff's proposals is clearly a crucial one. If we are to prevent more members falling into arrears in future, we must draw the right lessons from the experiences that have led to the present problem. The legacy of arrears has many causes, some quite beyond the control of the country itself. But, on occasion, the principal reason has been that the Fund, sometimes under pressure from governments, has acquiesced in weak or inadequately financed programmes. Restoring prudent lending policies will be essential to ensuring the arrears problem can be resolved permanently.

The staff paper demonstrates the need for the Fund to reaffirm its commitment to the policies that safeguard its resources, inter alia, on access, phasing and financing assurances. It also reinforces the importance of procedures such as medium-term scenarios and assessments of capacity to repay that have been developed to improve the process of analysing credit risks to the Fund. Unfortunately, the rigor of such analyses has been variable in the past; greater consistency is needed.

The specific actions developed by the staff, particularly the imaginative use of the SDR, would seem to play a valuable, if usually hidden, role in heading off further arrears. This chair has previously called for wider application of these techniques, particularly in cases where arrears arise regularly if only temporarily. Specifically, I would repeat suggestions that future requests for use of Fund resources should include, in the standard section assessing a member's ability to repurchase, an assessment of that member's "technical" repayment capability and a summary of its past payments record, covering the incidence of recurrent arrears and including delays in maintenance of value payments. Where a potential problem was identified, preventive action should be a standard condition for access to Fund resources.

The proposal made by the staff, for an escrow or trust account to withhold a share of new Fund disbursements for use in repayments of maturing purchases, makes more automatic the process of netting-out that should occur anyway. The device will however be of little use where no repurchases are due for some time and there is therefore nothing to net out against. It would seem unreasonable to hold back financing for this purpose: taken to its logical conclusion, no money would ever be disbursed. One possible alternative might be to divert the share of disbursements intended to enhance a member's reserves into a restricted SDR account which would be designed to operate as a short-term revolving fund. In effect, this fund would perform the classic functions of reserves.

Conclusion

Arrears raise many difficult questions. The Board will need to examine all of them. However, I hope that, in our discussion on 19 July, we will be able to agree on some concrete measures that will demonstrate our firm resolve to deal effectively with arrears. The staff's proposals provide a helpful outline of such a strategy; retroactive access to the ESAF could usefully give it additional substance.

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FROM: J M G TAYLOR

DATE: 4 August 1988

MR WALSH

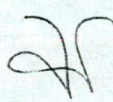
cc PS/Economic Secretary  
Sir P Middleton  
Sir G Littler  
Mr Lankester  
Mr Evans  
Mr Mountfield  
Mr Bottrill  
Mr Batt  
Ms Life  
Mr Kilpatrick  
Mr Tyrie

**ARREARS AT THE FUND AND BANK**

The Chancellor was grateful for your note of 27 July, and the enclosed paper.

2. As far as the recommendations listed in paragraph 55 of the paper are concerned, he thinks it is not worth pushing (ix) and (xv). He is otherwise content with the recommendations.

3. He is very doubtful about going along with the idea of "support groups" of developed countries favoured by the Managing Director (your paragraph 8).

  
J M G TAYLOR



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FROM: J M G TAYLOR

DATE: 4 August 1988

MR WALSH

108/3

cc PS/Economic Secretary  
Sir P Middleton  
Sir G Littler  
Mr Lankester  
Mr Evans  
Mr Mountfield  
Mr Bottrill  
Mr Batt  
Ms Life  
Mr Kilpatrick  
Mr Tyrie

**ARREARS AT THE FUND AND BANK**

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X 1 3. He is very doubtful about going along with the idea of "support groups" of developed countries favoured by the Managing Director (your paragraph 8).

A handwritten signature in dark ink, appearing to be 'JMG'.

J M G TAYLOR

30/8

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FM UKDEL IMF/IBRD WASHINGTON  
TO DESKBY 040900Z FCO  
TELNO 234  
OF 032300Z NOVEMBER 88  
INFO PRIORITY GEORGETOWN, BDDC BRIDGETOWN

IMF/IBRD: GUYANA - SUPPORT GROUP

1. ERB (FUND DMD) CHAIRED A MEETING WITH BROADLY THE SAME PARTICIPANTS AS HIS MEETING OF OCTOBER 28 (SEE OUR TELNO 231) TO DISCUSS THE FUND'S ATTITUDE TO THE 7 NOVEMBER CG MEETING, AND TO TAKE THE SUPPORT GROUP (SG) PROCESS FURTHER.

2. ERB INDICATED THAT THE FUND WAS SUPPORTIVE OF THE CG MEETING. HE HAD DISCUSSED IT WITH QURESHI AND AGREED THAT IT WOULD BE A KEY ELEMENT IN ATTEMPTING TO CLEAR ALL GUYANA'S ARREARS UP FRONT. FUND AND BANK WOULD WORK TOWARDS THIS OBJECTIVE. HOWEVER, IF UP-FRONT CLEARANCE PROVED NOT FEASIBLE, ERB CONSIDERED RESOLUTION OF THE ARREARS MUST OCCUR ALONG THE LINES ENDORSED BY THE INTERIM COMMITTEE, INVOLVING A SHADOW PROGRAMME, FINANCING THROUGH THE SHADOW PROGRAMME, AND THE ESTABLISHMENT OF ARRANGEMENTS WITH ALL PARTIES FOR THE CLEARANCE OF THEIR ARREARS, GENERALLY AT THE END OF THE SHADOW PROGRAMME. CRUCIALLY, ALL ISSUES RELATED TO THE PROCESS OF CLEARING ARREARS SHOULD BE HANDLED BY THE SUPPORT GROUP.

3. ERB WAS CONCERNED AT THE PROPOSAL IN THE BANK DOCUMENTATION THAT IN EFFECT BANK AND CDB ARREARS BE CLEARED AT THE START, AND THEY RESUME LENDING, WHILST OTHERS SHOULD FOLLOW LATER. INSTEAD, THERE SHOULD BE AN OVERALL APPROACH THAT SHOULD GIVE CONFIDENCE TO ALL PARTIES THAT THEIR ARREARS BE CLEARED AND ORDERLY ARRANGEMENTS DEVELOPED FOR GUYANA'S FINANCING. THE BANK MIGHT GO AHEAD AT SOME STAGE, BUT THIS HAD TO BE AS PART OF A CO-ORDINATED APPROACH, AND SHOULD NOT GIVE THE FEELING THAT SOME CREDITORS MIGHT BE LEFT BEHIND.

4. GOLD (CANADA) REPORTED THAT THE CANADIANS WERE KEEN THAT THE 7 NOVEMBER MEETING GO AHEAD. CANADA WOULD BE REPRESENTED BY LOEWENSON (MINISTRY OF FINANCE) AND LIVINGSTON (CEDA), WHO HOPED TO COME INTO THE FUND AFTER THE MEETING TO TAKE FORWARD THE PROCESS OF ESTABLISHING THE SG.

5. WARNER (US) NOTED THAT THE US REMAINED VERY SCEPTICAL OF THE CG MEETING. THEY WOULD ATTEND FOR DISCUSSIONS

PAGE 1  
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REGARDING IMMEDIATE CLEARANCE OF ARREARS, BUT WOULD NOT PARTICIPATE FURTHER IF THE BANK THEREAFTER SOUGHT TO EXAMINE ALTERNATIVE FINANCING SCENARIOS. HE CONSIDERED IT ESSENTIAL THAT THE SG ESTABLISH LEADERSHIP AT THIS STAGE.

6. POSTHUMUS (NETHERLANDS) AND GOOS (GERMANY) REMAINED MORE SCEPTICAL ON THE ROLE OF THE SG, AND PROBED AS TO HOW IT WOULD DIFFER FROM THE CG. ERB STRESSED THE WIDER ISSUES THE SG WOULD LOOK AT, INCLUDING FOR INSTANCE LIAISON WITH THE PARIS CLUB. THE CG HAD TRADITIONALLY SPECIALISED IN GAP-FILLING EXERCISES. THE ROLE OF THE SG WOULD BE TO DEFINE THE GAP.

7. ERB THEN OUTLINED HIS THINKING FOR THE SG. A RELATIVELY SMALL GROUP FOR GUYANA WOULD BE MORE COHESIVE AND WOULD FACILITATE CONTACT WITH ALL OTHER PARTIES. THE FUND WOULD PROPOSE THE MEMBERSHIP OF CANADA, TRINIDAD AND TOBAGO, UK, US, GERMANY AND JAPAN. THERE WOULD BE A BACK-UP GROUP IN THE FUND WHICH MIGHT INVOLVE DIRECTORS FROM THOSE COUNTRIES OR COULD INVOLVE A LARGER GROUP. HE EXPLICITLY DID NOT SEEK AGREEMENT ON PARTICIPATION AT THIS STAGE FROM THE COUNTRIES IDENTIFIED. DETAILS WOULD HAVE TO BE WORKED OUT WITH THE CANADIANS. THERE WOULD THEN HAVE TO BE PREPARATORY WORK FOR A HIGH-LEVEL MEETING. REPRESENTATIVES SHOULD REFLECT A WIDE RANGE OF INTERESTS WITHIN CAPITALS, BUT IT WOULD BE DESIRABLE TO IDENTIFY A SINGLE SPOKESMAN FOR EACH PARTICIPATING COUNTRY.

8. GOOS AND ADACHI (JAPAN) ASKED WHY THEY WERE TO BE ON THE SG, GIVEN THEIR VERY LIMITED BILATERAL CONTACTS WITH GUYANA. ERB RESPONDED THAT THEY WERE LARGE ESAF CONTRIBUTORS. GOOS REPEATED THAT HE COULD NOT GIVE ANY COMMITMENT TO PARTICIPATION, AT LEAST UNTIL THE END OF NEXT WEEK. MARCEL (FRANCE) AND OVI (NORDICS), ON THE OTHER HAND, SEEMED SOMEWHAT PUT OUT THAT THEY HAD NOT BEEN INCLUDED. MARCEL NOTED THAT FRANCE WOULD IN PRINCIPLE BE PREPARED, IF ASKED, TO PARTICIPATE IN AN SG FOR GUYANA. OVI SOUGHT, AND OBTAINED, ASSURANCES THAT SG MEETINGS WOULD BE FULLY OPEN TO NON-MEMBERS.

9. COMMENT: THE EXPLICIT LINKAGE BETWEEN GERMAN AND JAPANESE MEMBERSHIP OF THE SG AND THEIR ESAF CONTRIBUTIONS REFLECTS THE IMPORTANCE THE FUND CLEARLY ATTACH TO FINDING WAYS TO USE THE ESAF TO MEET GUYANA'S FINANCING NEEDS. THIS REINFORCES OUR EARLIER VIEW THAT THE FUND WOULD BE LOOKING TO THE UK LARGELY TO PRESS A ROLE FOR ESAF ALONG THE LINES OF THE CHANCELLOR'S INITIATIVE, THEREBY STRIVING FOR A MIDDLE GROUND BETWEEN THE US, WHO WOULD WANT VERY LARGE UP-FRONT

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DISBURSEMENTS, AND THE GERMANS AND JAPANESE, WHO WOULD BE VERY CAUTIOUS ABOUT ANY LARGE ESAF USE. WHILST WE HAVE NOT YET BEEN ASKED TO RESPOND TO THE INVITATION THAT WE PARTICIPATE IN THE SG, THIS MAY HAPPEN SOON. GIVEN THAT THE FUND IS PUSHING AHEAD WITH ITS ESTABLISHMENT, UNDER STRONG US PRESSURE, AND GIVEN THE GENERAL ENDORSEMENT OF THE SG STRATEGY AT THE INTERIM COMMITTEE MEETING IN BERLIN, IT WOULD BE AWKWARD THEN TO REFUSE.

10. DETAILS OF CANADIAN INTENTIONS ARE SCARCE HERE. THE ACTION SEEMS TO BE TAKING PLACE IN OTTAWA. WE HAVE HEARD FROM THE AMERICANS THAT THE CANADIANS ARE WORKING ON A COMPROMISE BETWEEN THE FUND AND BANK SCENARIOS INVOLVING A SIX-MONTH SHADOW PROGRAMME WITH ALL ARREARS CLEARED AT THE END. WHILST THIS ATTEMPT TO FIND A COMPROMISE IS COMMENDABLE, IT MAY WELL BE PREMATURE.

11. IT IS NOT CLEAR HOW THE 7 NOVEMBER MEETING WILL DEVELOP. ASSUMING THAT UP-FRONT CLEARANCE OF ARREARS IS SEEN NOT TO BE FEASIBLE, THE US AND (LESS PROBABLY) THE FUND MAY BE OVERTLY HOSTILE IF THE WORLD BANK CHAIRMANSHIP SEEKS TO PROCEED TO CONSIDER THE ALTERNATIVE SCENARIOS. ERB IS LUNCHING WITH CONABLE TOMORROW (FRIDAY), AND WILL TRY TO REACH SOME CONSENSUS.

12. THE ''ERB GROUP'' IS LIKELY TO MEET AGAIN NOVEMBER 8, PROBABLY WITH THE CANADIAN DELEGATION TO THE CG, TO DISCUSS THE OUTCOME OF THE CG MEETING AND TO CONSIDER HOW TO TAKE MATTERS FORWARD.

13. FCO PLEASE PASS TO EVANS (HMT), WARE (BOE), T RICHARDSON (ERD), MANNING (ODA) AND BREACH (ECGD).

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FM UKDEL IMF/IBRD WASHINGTON  
TO DESKBY 080800Z FCO  
TELNO 235  
OF 072300Z NOVEMBER 88  
INFO PRIORITY GEORGETOWN, BDDC BRIDGETOWN

ADVANCE COPY

GUYANA: DONORS MEETING

SUMMARY

1. NO FURTHER PROGRESS ON FILLING FINANCING GAP AT DONORS MEETING TODAY. SETTING UP OF SUPPORT GROUP NOW SEEMS INEVITABLE, THOUGH CANADIANS NOT YET AUTHORISED BY MINISTERS TO TAKE PART.

DETAIL

2. DONORS MEETING TODAY CHAIRED BY LOH (WORLD BANK) ATTENDED BY THE US (USAID, STATE DEPARTMENT AND TREASURY), CANADA (CIDA), THE UK, GERMANY AND THE IMF. JAPAN, THOUGH INVITED, DID NOT ATTEND. IN AN INITIAL TOUR DE TABLE THOSE PRESENT REITERATED EXISTING POSITIONS ON FINANCING ASPECTS, AND NO SIGNIFICANT PROGRESS WAS MADE ON FILLING THE RESIDUAL GAP, ESTIMATED BY WORLD BANK AT DOLLARS 140 - 160 MILLION.

3. THE US AND IMF THEN PRESSED HARD FOR EARLY SETTING UP OF SUPPORT GROUP (SG). BANK CHAIRMANSHIP ACQUIESCED, WHILE SEEKING CLARIFICATION OF RELATIONSHIP WITH CGCED. CANADA AND GERMANY, AS WELL AS THE UK, TOOK A CAUTIOUS AND NON-COMMITTAL APPROACH TO THE SG, AND DOUBTS WERE EXPRESSED WHETHER A SIMILAR SET OF GOVERNMENT REPRESENTATIVES MEETING IN A DIFFERENT FORUM WOULD BE ABLE TO MAKE FURTHER PROGRESS ON THE FINANCING PROBLEM. THE FUND STRESSED THE NEED FOR FLEXIBILITY AND EXAMINING SOME OF THE UNDERLYING ASSUMPTIONS IN EXISTING POSITIONS. FUND AND BANK MADE IT CLEAR BOTH WOULD PARTICIPATE FULLY IN BACKUP FOR THE SG. THE FUND ANNOUNCED THEY WOULD CONVENE A MEETING AT 4.30PM ON 8 NOVEMBER TO FURTHER CONSIDER PROCEDURES AND PRINCIPLES SURROUNDING SETTING UP OF THE SG.

4. A FUND MISSION LEAVES FOR GUYANA TOMORROW TO WORK ON DETAILS OF A PROGRAM WITHIN THE FRAMEWORK OF THE PFP. THERE WERE SUGGESTIONS BANK MIGHT PARTICIPATE. BANK HAD PLANNED AN

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APPRAISAL MISSION FOR THE SAC LEAVING ON 14 NOVEMBER. THE STAFF EXPRESSED DOUBT WHETHER THIS COULD LEAVE IN CURRENT UNCERTAINTY ABOUT FINANCING POSITION, BUT SEVERAL OF THOSE PRESENT URGED FLEXIBILITY AND AVOIDANCE OF SIGNALS WHICH WOULD CAUSE A LOSS OF MOMENTUM ON THE REFORM PROGRAM IN GUYANA.

5. FULL REPORT FOLLOWS BY BAG.

6. COMMENT: IT NOW SEEMS CERTAIN THAT THE UK WILL BE ASKED TO PARTICIPATE IN THE SG EITHER TOMORROW OR SHORTLY THEREAFTER. IN SPITE OF RESERVATIONS EXPRESSED AT THE MEETING, NO ALTERNATIVE WAY OF PURSUING THE GUYANA CASE WAS SUGGESTED, NOR WAS THERE ANY DISPOSITION TO ABANDON THE CASE AT THIS STAGE, AND SETTING UP OF THE SG NOW SEEMS INEVITABLE.

7. FCO PLEASE ADVANCE TO EVANS (HMT), WARE (BOE), T RICHARDSON (ERD), MANNING (ODA) AND BREACH (ECGD).

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.MONETARY  
EVANS TRSY  
WARE B/ENG  
T RICHARDSON ERD  
MANNING ODA  
BREACH ECGD  
MR BAYNE

MR CARRICK  
HD/ERD  
HD/ECD(E)  
RESIDENT CLERK  
MR LAVELLE CABINET OFFICE  
MR MOUNTFIELD HM TREASURY

NNNN

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FROM: H G WALSH  
 DATE: 8 November 1988

CHANCELLOR

cc Economic Secretary  
 Sir G Littler  
 Mr Lankester  
 Mr Evans  
 Mr Mountfield  
 Mr Davis  
 Mr Batt  
 Ms Life  
 Mr Kilpatrick  
 Mr Tyrrie

*Chipp's Psc.*  
*Content with Mr Walsh's*  
*proposed approach?*  
*OK -*  
*8/11*

**FUND ARREARS : GUYANA SUPPORT GROUP**

Mr Taylor's minute of 4 August recorded your doubts about the concept of support groups (originally known as "mentor" groups), as proposed by Camdessus. There is now a real opportunity to bring a specific arrears case at the Fund (Guyana) back on track perhaps with the help of your proposal for a backdated ESAF. This minute seeks your agreement to UK membership of the Guyana Support Group in the light of recent developments in this arrears case. The group would be chaired by Canada.

**Background**

2. Guyana is making adjustment efforts under the Hoyte government and wants to undertake a Fund programme. There have been several efforts to help bring it back to normal relations with the Fund and other IFIs to facilitate this. The Americans have favoured a bridging loan approach (to deal with its \$110 million of arrears) coupled with an immediate ESAF programme. The Germans and Japanese have strongly objected to the American approach on the grounds that Guyana has no track record and it puts ESAF funds at risk to which the Americans have not contributed. There has also (understandably) been unwillingness - including on the part of the UK - to subscribe to a large bridging loan (up to \$160 million).

3. The World Bank has recently entered the field by espousing the broad approach which you put forward at the Spring 1988

Meetings of the Bank and Fund - for a shadow programme plus an eventual ESAF. It is an approach which, provided the shadow programme is adequate and approved by the Fund Board, we should find broadly acceptable. It involves clearance of World Bank (and Caribbean Development Bank) arrears during the shadow programme period while Fund arrears remain outstanding. This would enable the World Bank and CDB to make disbursements during the shadow programme period to help fill the large residual (\$160 million) financing gap.

4. We are somewhat unhappy that the World Bank has attempted to claim leadership on this issue from the Fund. A consultative group chaired by the Bank met yesterday with inconclusive results, partly because of widespread unease that the World Bank should be in the chair on what is basically a Fund matter.

#### Proposal

5. The Fund equivalent of the existing type of consultative group chaired by the Bank would be the kind of support group envisaged by Camdessus. In UKDEL's view, it is inevitable that one will be set up for Guyana and also inevitable that we shall be asked to join. The Fund is pushing ahead with its establishment, under strong US pressure, and both we and UKDEL feel that it would be awkward for the UK to refuse to join if asked. It would mean refusing to take part in discussions which could well lead to the first case of a country ineligible at the Fund being brought back on track, perhaps using your backdated ESAF approach. If we join, we would envisage that Mr Cassell would be our member of the support group chaired by Canada. It would not in itself entail any extra commitment of resources by the UK, nor would it mean that we would have to join future groups set up for, say, Peru. All concerned are seized of the need to avoid any slippery slopes which would mean the use of massive extra resources.

6. It would be of enormous help in solving the Fund's arrears problems if we could clear Guyana's arrears - better still with an approach you proposed. Would you be content for us to give



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instructions permitting Mr Cassell to join the Guyana Support Group if he is asked? It would be helpful - given fast-moving events in Washington - to know your response within the next day or two.

7. I attach for reference UKDEL telnos. 234 and 235.

H.W.

H G WALSH



FROM: J M G TAYLOR

DATE: 9 November 1988

A handwritten signature in blue ink, appearing to be 'PMP'.

MR WALSH

cc PS/Economic Secretary  
Sir G Littler  
Mr Lankester  
Mr H P Evans  
Mr Mountfield  
Mr Davis  
Mr Batt  
Ms Life  
Mr Kilpatrick  
Mr Tyrie

FUND ARREARS: GUYANA SUPPORT GROUP

The Chancellor has seen your note of 8 November, and is content for you to give instructions permitting Mr Cassell to join the Guyana support group if he is asked.

Handwritten initials in blue ink, possibly 'JMG'.

J M G TAYLOR