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A 3

MR. SCHOLAR

BRAZIL

It is no surprise to see the Bank recommending that we agree to a Brazilian request for a further postponement of the BIS bridging loan. Essentially they want to put that decision in the hands of de Larosiere.

But for how long are we to roll over the BIS credit? The Bank is silent on this point. It is such an important issue that it cannot be a mere oversight. There must be a reason for the omission. Will this also be recommended by de Larosiere and agreed by us? As a very minimum requirement we ought to specify only another two weeks.

IMF Ineptitude

The Brazilian financing operation over the past nine months can inspire little confidence. The Bank says that the Brazilians have been ill-advised by the US banks with respect to the Interbank lines. But the IMF should have picked up the fragility of such promises; they are really no more than a confidence-booster in order to get everyone to join in. The IMF and central banks cannot slough off their responsibility onto the US banks. Everyone knows the US banks are critically interested in preserving their balance sheets, even at the expense of the rest of the world's taxpayers.

The IMF also now admit that (p.5) they did not take into account the seasonal pattern of exports. Why ever not? Every schoolboy knows that agriculture is a seasonal business.

The ineptitude of the financing plan is even more marked when it is recalled that American interest rates fell in mid-1982 and have stayed on that plateau in the first half of 1983. I suspect that the financial calculations assume that interest rates will either fall further or remain at the present low level. This is, I believe, a rash assumption. I expect US interest rates to rise.

The Next Act

I suspect that the IMF is bound to ask for the BIS roll over. The IMF is dominated by US banks. The banks in particular want to preserve the fictions in their balance sheets and the possibility of a bail-out by the US government. The US Administration, in turn, want to avoid the odium of such a bail-out as long as possible.

/The Brazilians know this

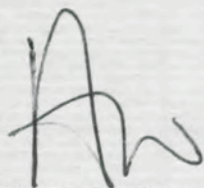
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The Brazilians know this. The widespread belief in Brazilia is that they will get the IMF's approval. I suspect the IMF will climb down, at least part of the way, on its definition of public sector deficit (the difference in definition is an astonishing 6-8% of GDP!) and on their part the Brazilians will make suitably impressive promises about de-indexation of wages. Some of these are already on offer. [But this is all my conjecture; I have no inside knowledge.]

The Bank omitted to say anything about the views of the member countries on the Board of the BIS. Leutwiler told me that Germany, Switzerland and Holland were firmly against a postponement^{of repayment} of the bridging loan. If we joined that group then there would be four against the postponement. If all the other four countries (France, Italy, Belgium and Sweden) voted for postponement, the Board would be hung. It is normal procedure for the Chairman (Leutwiler) to have the casting vote. Thus our vote could be a critical one.

Conclusion

The Brazilian Government has successfully strung out its credit lines with cynical promises and little performance. The credibility of the creditors is at an all-time low. The integrity of interbank markets has already been jeopardised and now the bridging loan is being converted into merely another line of credit. We have paid too much already in financial blackmail. It is time to stop the charade. We should vote against postponement.



ALAN WALTERS
8 July 1983



10 DOWNING STREET

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Prime Minister

Brazil: paper by the Bank

① ^{/ Play A}
Alan argues that we should not
roll forward the BIS facility on
Monday; or that, if we do, we
should do so for 2 weeks only.

② The Chancellor ^{/ Play B} thinks we should
roll forward, but for 2 weeks only
and never again.

③ Agree a 2 week final postponement

MUS 8/7

When creditors are weak,
debtors will get into weak
trouble