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THE DEPUTY GOVERNOR

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BANK OF ENGLAND
LONDON
EC2R 8AH

C. A.W.

Prime Minister

12 July 1983

The Governor
is now having second
thoughts about X. No decision
required tonight; the Governor
and Chancellor will put the
matter to you tomorrow.

M C Scholar Esq
Private Secretary to
the Prime Minister
Prime Minister's Office
No 10 Downing Street
London
SW1

Dear Michael,

MUS 12/7

BIS LOAN TO BRAZIL

I am writing to confirm what I heard from the Governor speaking from Basle this morning and passed on to you by telephone.

Leutwiler's uncompromising remarks, on the need for the current \$400 million tranche of the BIS loan to be paid on its due date, appear to have been very effective. Larosière was subsequently on the 'phone to Delfim Netto who was fully-seized of the need to show some real movement and was going straight to the President to urge it. We also heard that Langoni, the central bank governor, had been stiffened.

Leutwiler then convened a meeting of the BIS Governors (representing the UK, France, Germany, Italy, the Netherlands and Sweden) with Larosière. After some discussion, the outcome of this meeting was as follows. It was proposed by Leutwiler and agreed unanimously by the Governors, subject, in some cases such as our own, to reference back to capitals, that if Larosière was able to say on Friday that he had received assurances that were satisfactory to him from President Figueredo, the BIS would issue the following statement:

"In the light of the declaration by the President of Brazil, the Managing Director of the IMF has requested that the BIS and the central banks which participated in the credit to Brazil should postpone the maturity of the \$400 million tranche due on 15 July. This postponement should enable the IMF to complete its negotiations with the Brazilian authorities, against the background of the reforms announced by the President. The participating central banks have agreed to the Managing Director's request and, as a consequence, have taken over their respective shares. At the same time these central banks have asked the BIS to represent their interest in relation to their credits with Brazil."

You will note, of course, that this suggested statement contains no term on the postponement. It was agreed by all the central banks that this was now the right course because (a) they will only be making the postponement if the Brazilians have actually shown that they have responded to the leverage they have already exerted; and (b) they recognise that they cannot determine when the IMF negotiations will be complete though they must realistically be expected to take at least three weeks.

but they
could
backtrack
later

- 50, 90 for 5 weeks, or 7 weeks, or....

It is also relevant that de Larosière asked the US Treasury whether if Brazil made a satisfactory declaration to him, they (the US Treasury) would be prepared to extend a loan to enable the Brazilians to pay off part or all of the \$400 million tranche. He reported that the Treasury response was "not negative". The rationale behind this approach is that all concerned feel it would be in the general interest to preserve the credibility of the BIS as a provider of essentially short-term bridging finance which is unquestionably repaid when it becomes due. Our Governor was asked whether he could prevail on our Chancellor to telephone Regan to encourage him to provide (only, of course, if the satisfactory declaration was made) some finance. Larosière appeared to believe that Regan would be likely to be persuadable.

MCS

If no satisfactory declaration is forthcoming by 15 July it is agreed that there shall be no question of any further postponement of the BIS credit. It will be announced that the central banks have substituted themselves for the BIS, though asking the BIS to continue to represent their interest and on their behalf demand repayment. We shall then have a situation of technical default if the Brazilians are unable to make the payment.

X | The Governor has asked me to say that he hopes that in the various circumstances outlined above, the Prime Minister will be content that he should join his colleagues in making the proposed statement.

I am copying this letter to John Kerr and Brian Fall.

Yours ever
Kit

C W McMahon