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10 DOWNING STREET

From the Private Secretary

16 February, 1984.

Argentina: Commercial Bank Lending

The Prime Minister has seen your letter to me of 14 February and the Bank of England note which was attached to it. She agrees that this matter can rest, now that the Bank and LBI are fully aware of the need to keep Government fully informed of developments relating to Argentine debt.

Andrew Turnbull

John Kerr, Esq.,
HM Treasury.

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cc No

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Prime Minister

Agree this can rest, now
that LBI and Bank are
fully aware of need to keep
Government fully informed?

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

14 February 1984

AT
15/2

Andrew Turnbull Esq
10 Downing Street
LONDON SW1

Dear Andrew,

ARGENTINA: COMMERCIAL BANK LENDING

In his minute of 17 January to the Prime Minister the Chancellor mentioned that he would be pursuing the question of why the Bank of England's contacts with Lloyds Bank International did not bring to light earlier the expiry date of the draw-down period for the medium-term loan to Argentina.

I now enclose an explanatory note prepared by the Bank at the Treasury's request. It appears that the Bank were not informed of this provision by LBI until shortly before the Argentine Working Committee meeting in New York on 9-10 January, and that they decided not to pass the information on to the Treasury until they knew whether the matter had been discussed at that meeting. In the event, the Working Party did not discuss the point, and the Bank informed the Treasury on 12 January.

The Chancellor is surprised that the Bank's note suggests that they have still not seen a copy of the loan agreement. His firm view that Ministers should have been told of the expiry date provision as soon as it came to light has been conveyed to the Bank. He very much agrees with the Prime Minister - your letter of 19 January - that Ministers could, through not knowing of the provision, have found themselves in an embarrassingly false position. On his instructions, officials have impressed on the Bank the importance of keeping the Treasury closely and promptly informed of all developments relating to the loan agreement and the Argentine debt situation.

Yours ever,
J O KERR

J O KERR
Principal Private Secretary

ARGENTINA'S \$1.5 BN LOAN

The Bank of England learned in the following way that the banks' commitment to make disbursements under the Loan Agreement with Argentina was due to terminate on 31 January 1984 and could only be extended thereafter on the unanimous vote of the 313 participating banks.

2 A meeting of the Argentine Working Committee on which Lloyds Bank International represents the British banks, was called for 9-10 January - the first meeting since 24 November. As usual, there was a preliminary meeting shortly beforehand of the main British banks, with the Bank of England represented, to consider what attitude should be taken in the Working Committee towards any Argentine requests that might be put forward by the Argentine Economic Minister, Grinspun, in relation to the \$1.5 bn loan. The discussion brought to light the important fact of the Termination Date.

3 Since the Bank understood that the Working Committee would be discussing this point in a preliminary way, as well as hearing at first-hand from Grinspun what kind of programme the new Argentine Government was proposing to adopt, it seemed right to wait to convey this new information to the Treasury until its significance could be assessed in the light of the outcome of these discussions in New York and of the attitude of the other banks in the Working Committee. This the Bank did as soon as the LBI representative had debriefed us immediately on his return from New York (though it emerged that the Working Committee had not in fact discussed this point at all).

4 Next comes the question why LBI had not thought it necessary to notify the Bank earlier of the Termination Date. This is explicable in the light of the conditions under which the banks, and especially the LBI, had been operating. The negotiation of the loan itself and of the single drawdown that in the event has been made under it,

had been dogged by delays and difficulties almost wholly of the Argentines' own making. Every stage has involved great complications, some technical, many sensitive. This is not surprising, since the Bank have been told that the Loan Agreement and its related documentation, which is exceedingly complex, runs to some 90 pages of the Agreement itself plus as many again of schedules and exhibits. For the first drawing to take place, 15 pre-conditions, it seems, should have been met and we understand that 20 potential Events of Default are listed in the Agreement. As a result, the first drawing in early December (and even then a last-minute technical hitch almost prevented it) took place after the third and last drawing should normally have occurred. This would have been over two months before the Termination Date for the drawings which was, therefore, in some sense a formality in the Agreement at the time it was drawn up.

5 Nevertheless, LBI have been fully aware of the political importance attaching to this loan and they have striven to keep the Bank properly informed about the slow progress of the original negotiations leading up to the signature of the loan and any material subsequent developments. What they knew, however, was that for wider international reasons HMG had acquiesced in the British banks' participation in the original bridging loan of December 1982 and the subsequent IMF-backed loan package. HMG's concerns in August 1983 and thereafter had been to ensure that this participation, on the one hand, could be used as a lever to remove Argentine discriminatory restrictions against the UK and, on the other hand, should be firmly linked to an IMF agreement, since that body's seal of approval was the best assurance available to HMG and the banks that the Argentine Government was pursuing responsible economic and fiscal policies and therefore making proper and justifiable use of any moneys it received from the banks' loan. LBI were not privy to HMG's examination of ways by which the British banks might positively be prevented from lending to Argentina and therefore they had no reason to suppose that HMG expected them to look for ways of actually withdrawing from the loan.

6 They would have been confirmed in this view by the fact that at the time of the December drawing a way was open to them to prevent disbursement, since their consent was needed for a waiver on certain conditions attaching to the earlier bridging loan. They gave their waiver with HMG's knowledge. From the banks' point of view, therefore, the Termination Date was not a material element in their consideration of their actions vis-a-vis Argentina until early 1984 because it did not become operative until 31 January; and in the earlier period there were numerous other issues relating to the loan which needed to be immediately dealt with in one way or another and these had been the focus of their attention.

7 It is also relevant that the leading figures in the Working Committee on Argentina are also key members of the Advisory Group on Brazil. These members were engaged almost continuously between the end of November and mid-January, either individually or as a group, in their ultimately successful efforts to put together the Brazilian new money loan of \$6.5 bn. During that period the new democratically-elected Argentine Government was finding its feet and in no position to discuss with the banks and the IMF how they would cope with the mess the Junta had bequeathed to them. It was therefore to be expected that the banks put the immediate problems of Argentina out of their minds during this time.

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