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CCBQ

Treasury Chambers, Parliament Street, SW1P 3AG
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David Norgrove Esq
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London
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22 July 1986

Prime Minister

Yes

Content with X?

Dear David

N.L.W.

22.7

MEXICAN DEBT

As part of the arrangements which are being put together to support a Mexican IMF programme, the Managing Director of the Fund has asked Central Banks in certain member states to take part in a three-month bridging loan, to carry Mexico through the period until it can make a drawing from the IMF. It will be announced in Washington on Wednesday that Mexico has signed a Letter of Intent, which can be expected to lead to a Stand-By Agreement with the Fund in September, and an early drawing thereafter, from which the bridging loan would be repaid.

The bridging loan would amount to \$1.5 billion, and would be in three parts: one-third from the US Authorities (Fed and Treasury); one-third from the commercial banks who are exposed to Mexico; and one-third from central banks who are members of the BIS. The UK share of the Central Bank tranche could be up to \$85 million.

There is a precedent for this operation: a very similar loan was made in 1982 for Mexico (and somewhat similar operations were also carried out for Brazil and Yugoslavia).

X | The Chancellor proposes to authorise the Bank of England to take part in the operation, and to give them an indemnity on lines similar to that given in 1982.

Unlike 1982, there are now statutory powers for such an indemnity (International Monetary Arrangements Act 1983) and the Act requires us 'immediately after giving any undertaking under this section, to lay a statement of the undertaking before each House of Parliament'.

... | The Chancellor proposes to do this on Thursday. I attach a draft. I should be grateful for confirmation that the Prime Minister sees no objection.

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The Chancellor does not think it will be necessary to make a separate announcement, by way of arranged Question or otherwise. But the announcement will have been made in Washington on Wednesday so we shall let you have suitable briefing for the Prime Minister's use at Question Time on Thursday, and will provide speaking notes for the Adjournment Debates in both Houses in case the points are raised then. However, our expectation is that the operation is on balance unlikely to provoke any comment in Parliament.

The FCO has arranged to send an appropriate briefing to Mexico City and other foreign posts. Our Press Office and the FCO Press Office have question and answer briefing.

As a matter of courtesy, we will be notifying the Public Accounts Committee and the Treasury and Civil Service Select Committee.

I am copying this letter to Joan MacNaughton (Lord President's Office), Tony Galsworthy (FCO), Alison Smith (Lord Privy Seal's Office), Murdo Maclean (Chief Whip's Office), David Beamish (Lord Denham's Office), John Footman (Bank of England) and Bernard Ingham (No 10).

Yours ever,

Tony

A W KUCZYS

DRAFT 21.7.86

INDEMNITY TO THE BANK OF ENGLAND COVERING THEIR COMMITMENT
TO THE BANK FOR INTERNATIONAL SETTLEMENTS IN RESPECT OF A
LOAN TO MEXICO

Section 2(i) of the International Monetary Arrangements Act 1983 empowers the Treasury to undertake to indemnify the Bank of England in respect of financial assistance given by the Bank to the monetary authorities of a foreign country, in co-operation with the Bank for International Settlements or any other central banks or monetary authorities. The Act requires the Treasury to lay a statement of the undertaking before both Houses of Parliament immediately after giving the undertaking. This paper fulfils that requirement.

International assistance to Mexico

2. Financial support for Mexico is being provided or sought through an application by the Mexican Government to the International Monetary Fund for a Standby Agreement; an application to the International Bank for Reconstruction and Development for a series of loans; by assistance in various forms by the United States authorities; through discussions with the commercial banks of many countries which have provided loans to Mexico; and by a loan from the Bank for International Settlements supported by the central banks of a number of countries. The BIS loan to the Bank of Mexico is part of total central bank facilities of \$1.5 billion being made available to Mexico and is for a period of three months. The BIS will finance the loan from its own resources, but with a right of recourse to participating member central banks. The Bank of England's contingent liability under this arrangement is [\$85] million and the Treasury has agreed to

give the Bank an indemnity in respect of this commitment.

3. The Government's decision to support the BIS operation and to give the indemnity took into account that the Mexican Government had applied for assistance to the International Monetary Fund and the International Bank for Reconstruction and Development, and that the BIS loan was essentially of a bridging character. A more general consideration was the Government's view of the importance of facilitating Mexico's economic adjustment and the contribution that a bridging facility would make towards safeguarding the health of the international financial system.

4. A similar undertaking was given to the Bank of England in August 1982 in respect of a similar bridging operation. In the event the loan was repaid on time and the indemnity was not required. The present undertaking is given under statutory powers which were not available in 1982.