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Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon Paul Channon MP
Minister for Trade
Department of Trade and Industry
1 - 19 Victoria Street
London
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29 April 1985

Dear Minister

POLAND RESCHEDULING

Thank you for your letter of 16 April about the desirability of refinancing rather than rescheduling debt agreements under the auspices of the Paris Club.

On the general issue my view is that the method of restructuring such debts should continue to be considered case by case. If propriety and considerations of cost to ECGD permit - and the debtor can be persuaded - refinancing should be the preferred route. Where it is, care must be taken to minimise its monetary effects. This will generally mean funding by capital market issues rather than by bank lending. Even then the benefit to the PSBR, though welcome, will not be reflected in an equivalent reduction in pressure on interest rates.

We have also considered the two major cases you mention of Nigeria and Poland. On Nigeria, I think we are at one in rejecting for the moment any refinancing of Nigerian claims given its unwillingness to come to an agreement with the IMF and the risk of the Nigerians defaulting on their medium term liabilities.

The Chancellor and I have considered the question of refinancing v rescheduling very carefully in the case of Poland. I cannot agree that judgements about Poland's ability to repay a restructured debt are irrelevant to the choice of method. A refinancing would involve the issue of a fresh guarantee. In the case of Poland, its past record and our serious concern about its future performance means that there is very considerable uncertainty about whether Poland will be able or willing to repay. Even if this falls short of circumstances in which it would be improper in a legal sense for the Department to give its guarantee, I think it would be imprudent,

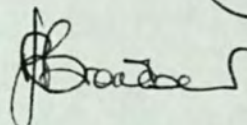
and difficult to justify to Parliament, giving or renewing a guarantee in respect of a risk which seems very likely to crystallise, when an alternative mechanism is available. It would also be open to criticism to choose a restructuring technique which obscured the underlying position and gave a misleading picture of ECGD's and the public finances.

Nor do I agree with your assertion that if the situation is so bad, we ought not to be going along with the Paris Club agreement in its present terms. Our support for that agreement rests on its importance as a means of securing some inflow of funds to the UK and ECGD, as opposed to the 100 per cent moratorium the Poles have benefitted from so far.

I hope therefore you can now accept that Poland's debt should be rescheduled rather than refinanced. Our view has been reached after careful reflection. Since our officials are to meet the Poles multilaterally in the Paris Club on 18 and 19 April and, subsequently bilaterally on 13 and 14 May, the draft form of agreement assuming rescheduling does need to be sent to the Poles without delay.

I am copying this letter to the Prime Minister, to members of EA and EX and to Sir Robert Armstrong.

Yours sincerely

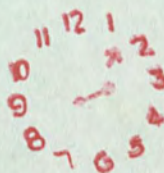


for PETER REES

[Approved by the Chief Secretary]

TRANS-ECGD Jan '80.

29 APR 1985





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From the Minister for Trade

The Rt Hon Peter Rees QC MP
Chief Secretary to the Treasury
Parliament Street
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16 April 1985

See TRADE: ECGD Jan. 85.

In your minute of 3 April to the Prime Minister you outlined the steps you and I are taking to improve ECGD's financial position. At our meeting before this, we discussed the relevant merits of refinancing and rescheduling ECGD's overseas debts which are subject to Paris Club treatment.

My starting point is that we should seek to refinance wherever possible on the grounds that this achieves a real improvement in ECGD's cashflow and to the PSBR.

The underlying debt is unchanged, whether we refinance or reschedule, but I attach considerable importance to the presentational advantages of reducing ECGD's cash deficit as far as we can. And I would imagine that you would welcome the relief to the PSBR.

I mentioned at our meeting that there were two big ticket items where in my view refinancing ought to be considered. They are Nigeria and Poland. Nigeria cannot be a serious candidate at this stage in view of their failure to come to terms with IMF: indeed the future prospects are looking somewhat bleak and we have already agreed to revise our projections for ECGD's overall cashflow in recognition that there is now some risk of the Nigerians defaulting on their medium term liabilities in the not too distant future. But Poland is a good candidate and I should like it to be seriously considered since we shall very shortly be talking to the Poles about restructuring their 1982-84 debts. We have already agreed two refinancing loans for Poland and the structure of their 1982-84 debt is such that a further refinancing would be relatively easy to arrange. Moreover, the amount (£486m) is substantial.

I understand, however, that Treasury officials have reservations about a refinancing deal for Poland, mainly on the grounds that their economy is so weak that there must be serious doubts as to whether they will be able to service a new loan over the term already agreed in the Paris Club. I cannot, however, see that this is relevant to the issue of whether the Polish debt should be refinanced or rescheduled. I regard both techniques as of equal merit and I cannot see that the risk of a further rephrasing of the terms of the loan should preclude the granting



of that loan. If the situation is so bad that we believe the Poles will be unable to pay on the agreed dates then we ought not to be going along with the Paris Club agreement in its present terms.

If on the other hand there are problems in relation to the monetary effects of a refinancing loan then of course we should have to take account of them. but in the absence of any compelling Treasury counter arguments I should like to authorise ECGD to identify the most appropriate refinancing technique and to invite tenders from the bankers.

I should welcome an early reaction since there is not all that much time to do this ahead of the bilateral discussions due to take place at the end of April or early in May.

I am copying this letter to the Prime Minister, to members of EA and EX and to Sir Robert Armstrong.

A handwritten signature in dark ink, appearing to read 'Paul Channon', with a large, sweeping initial 'P'.

PAUL CHANNON

A large, stylized handwritten signature in dark ink, appearing to read 'Paul', with a large, sweeping initial 'P'.