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Barber B. Conable

President's Council files 04
August 1987

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August 26 MEETING

FORM NO. 89
(2-83)

# THE WORLD BANK

| ROUTING SLIP | Date 8/28/87 |
|---|---|

**OFFICE OF THE PRESIDENT**

| Name | Room No. |
|---|---|
| Messrs. S. Husain | I-8015 |
| P. Loh | I-5015 |
| V. Dubey | E-3069 |
| | |
| | |

| | | | |
|---|---|---|---|
| | To Handle | | Note and File |
| | Appropriate Disposition | | Prepare Reply |
| | Approval | | Per Our Conversation |
| | Information | | Recommendation |

Remarks

Would appreciate your comments before Mr. Conable signs.

From Marianne Haug

THE WORLD BANK
Washington, D.C. 20433
U.S.A.

Office of the President

September 1, 1987

To Mr. Qureshi

Re.: Jamaica-CSP

I appreciated the open and constructive discussion of the Jamaica-CSP during the Policy Committee discussion on August 26 and support the course of action proposed in the Strategy Paper as a basis for our position at the upcoming donor conference.

The Bank's commitment to the implementation of this program will be conditional on:

a) achieving an adequate level of capital flows and equitable burden sharing among donors, and

b) meeting the agreed policy reform.

I would appreciate keeping me informed about political and economic developments in Jamaica as well as the results of the aid coordination effort.

cc: Members of the Policy Committee

D R A F T

August 28, 1987

To Mr. Husain

Re.: Jamaica-CSP

I appreciated the open and constructive discussion of the Jamaica-CSP during the Policy Committee discussion on August 26 and support the course of action proposed in the Strategy Paper as a basis for our position at the upcoming donor conference.

The Bank's commitment to the implementation of this program will be conditional on:

a) achieving an adequate level of capital flows and equitable burden sharing among donors including a slower withdrawal by the IMF, and

b) meeting the agreed policy reform and exchange rate targets.

I would appreciate keeping me informed about political and economic developments in Jamaica as well as the results of the aid coordination effort.

M. Haug

cc: Members of the Policy Committee

**POLICY COMMITTEE MEETING**

WEDNESDAY, AUGUST 26, 1987

9:30 a.m.

**AGENDA**

1. Jamaica--Country Strategy Paper

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

# OFFICE MEMORANDUM

DATE: August 26, 1987

TO: Files

FROM: Marianne Haug

EXTENSION: 73585

SUBJECT: Minutes of the Policy Committee of August 26, 1987

Members Present

Messrs. Conable, Hopper, Ryrie, Shihata, Thahane

Acting Members

Messrs. Cosgrove, Karaosmanoglu, Vergin

Other Staff Members

Messrs. Edelman, Husain, Loh, Robinson, Tanaka, Voyadzis
Ms. Haug

## Jamaica Country Strategy Paper

Messrs. Husain and Loh provided an overview of the Jamaica economic situation. In spite of better than expected performance over the past year, the overall performance of the Jamaican economy has not been good. The proposed lending program should be considered in light of the country's creditworthiness, and is conditioned by an agreement over a medium term framework with the Bank, a burden sharing agreement with other donors, and the evolution of the political situation.

The financing of the proposed program drew questions from several participants. Mr. Loh communicated that the ExIm Bank of Japan could become a source of untied funds although Japan has not been a traditional lender to date. Mr. Husain mentioned that major donors for Jamaica included USAID and Canada, and recognized that the task of mobilizing concessional funds would be difficult. Mr. Husain informed that he has had meetings with the State Department and USAID which have given assurance to increase their level of financing. Mr. Voyadzis mentioned that IDB is planning a lending program of US$ 24-25 million, including policy lending, and would be willing to cofinance.

In response to a question on political risk considering the upcoming election, Mr. Husain emphasized the importance of focusing on the stability of reforms rather than individuals. He noticed in this respect that reversal on privatization initiatives and tax reform would be difficult. Mr. Loh described potential risks related to public expenditures and the wage bill. These issues will have to be dealt in the context of negotiations with the Government.

Mr. Loh pointed out that conditionality would focus on fiscal balance, financial payment and exchange rate. In response to a question by the Chairman concerning further exchange rates adjustments during the election year, Mr. Loh explained that an agreement on exchange rates would be sought before the current IMF agreement runs out in March 1988.

Mr. Hopper questioned the assumptions concerning increased domestic financing and the role of private creditors, and noticed that there was a need to have agreements not only with the IMF and USAID but with the commercial banks. Mr. Loh proposed in this respect that the CSP format be adjusted to cover issues of commercial bank debt. Mr. Loh added that Jamaica had been prudent with respect to commercial banks and that only a small proportion of its debt was owed to commercial banks.

Mr. Hopper inquired about the fallback strategies available in the event negotiations did not succeed or policy reversal occurred as a result of the election. Mr. Husain replied that the lending program consisted of a fifty/fifty split between adjustment lending and project lending.

Mr. Thahane raised a concern over the IMF position on repurchasing. Mr. Husain pointed out that the IMF cannot be expected to maintain its level of exposure, and that it is necessary to consider the overall range of financing sources available to reduce IMF exposure. Messrs. Hopper and Loh added that the tapering down of repurchasing at a level of, for example, 70% was appropriate.

Mr.Vergin considered that the Bank should be concerned about its preferred creditor status and focus on strengthening that status. He was in particular disturbed by the building up of arrears and by the level of exposure at a time where turbulency may increase. Mr. Loh mentioned that the Government of Jamaica had emphasized the preferred creditor role of IDB and the Bank. Mr. Shihata added that there was no penalty for delaying payments within the existing limit. Participants considered that delaying payments within the limit was a rational financial management decision, and Mr. Husain suggestedd that further pressure should be put on countries to pay on time through the introduction of a penalty.

Mr. Ryrie mentioned that IFC operations have been relatively small in Jamaica, but that possibilities for new power and hotel investments have arisen. Mr. Ryrie was, however, hesitant on increasing IFC's level of exposure in Jamaica.

Mr.Cosgrove questioned the pursuit of general tax reform measures during the coming election year. Mr. Loh responded that tax reform work by USAID and the Bank has been underway for the past 6 to 7 years to improve the efficiency of the tax collection system, and that first results from this work were encouraging. Mr. Cosgrove mentioned that the medium term program should include measures to support growth; Mr. Loh confirmed that investment in infrastructure was already being considered.

Mr.Shihata expressed concern over the possible increase in the Bank relative share in overall exposure. Mr. Husain responded that the Bank would be keeping its level of exposure constant through burden sharing with other donors.

Mr. Hopper welcomed the decision to bring the Jamaica case to the Policy Committee as it reflects one end of the spectrum of countries in similar difficult situations. In the case of Jamaica, the recent good performance has been a mitigating factor which does not exist in many other countries facing similar problems. Mr. Hopper foresees tough negotiations ahead and would like to be kept informed on the follow up of discussions with the IMF and bilateral institutions as an example of what is being done for countries in this high risk situation.

~~THE WORLD~~ BANK · INTERNATIONAL FINANCE CORPORATION

# OFFICE MEMORANDUM

DATE: July 27, 1987

TO: Operations Committee

FROM: Vinod Dubey, Director, EAS

EXT: 78051

SUBJECT: Jamaica: Country Strategy Paper - Agenda

Attached is an agenda and comments on issues that appear to merit consideration by the Operations Committee. The suggested agenda items are:

a) Creditworthiness and coordination with the Fund

b) The economic program and country commitment

c) The lending program and local cost financing

The Operations Committee will meet on Wednesday, July 29, 1987 at 3:00 p.m. in Conference Room E-1244.

Attachment

cc: Messrs. Loh
Voyadzis
Ryrie
El Serafy
Liebenthal
Ray
Steer

JAMAICA - COUNTRY STRATEGY PAPER

**Topics for Discussion**

1. The Bank resumed policy lending to Jamaica with the two recently approved sectoral adjustment loans for Trade/Finance and Public Enterprises. These two loans followed the new Stand-by arrangement approved by the IMF Board in March.

2. The recent resumption of policy lending is consistent with the strategy proposed in this CSP, which predates the Board presentations. The strategy would continue the strong support the Bank has provided since the economic reform program began in 1981. The policy agenda, to be defined in a forthcoming medium-term framework paper (MFP), would be a broad one. It would include trade and exchange rate policies, the tax system, banking and capital markets, public enterprises and social sectors. As before, the Bank and the Fund would coordinate a "global" financing package to assist the reform process. The main issues are: (a) creditworthiness and aid coordination, (b) program content and country commitment, and (c) lending program.

Creditworthiness and Aid Coordination

3. Jamaica's overall public debt has more than doubled since the beginning of the decade. It now exceeds 150% of GDP. After rescheduling, debt service is about 52% of exports (75% in 1986 before rescheduling). The share of preferred creditors in total debt is 43%.

4. Due to their heavy involvement in the past, the exposures of both the Bank and the Fund are high. The Bank's share of public MLT is 15%. Debt service to the Bank represents about 13% of total service payments and 6.5% of exports. The total Fund credit outstanding at the end of March 1987 was 365% of quota.

5. The proposed FY88-92 lending program of about $53 million a year would maintain the Bank's share of public MLT at about 15%. However, the USAID assistance level is being reduced, and the IMF is planning to reduce its exposure. As the CSP brings out, the projected financial gap of $355 million would become unsustainable if the IMF reduces its exposure at the intended pace. The paper also remarks that it would appear inappropriate for the Bank to be seen financing IMF repurchases. It thus proposes that the Bank and the IMF reach an agreement whereby the IMF will approve new programs after the present ones to offset 70% of its repurchases. In that case the projected base scenario would become viable.

6. It should be noted that the projected financing gap that new IMF credits might fill is highly uncertain. Despite some export diversification, the economy remains highly vulnerable to adverse changes in oil and bauxite prices. If, for example, the bauxite and alumina prices become consistently lower than those forecast by only 10%, the cumulative financing gap from FY88/89 to FY90/91 would increase by $130 million. In

addition, there are risks associated with delays and back-sliding in the domestic program.

OPERATIONS COMMITTEE

7. **In view of this, the Committee may wish to consider:**

- **whether the problems raised by the Bank's high exposure and** the country's creditworthiness warrant the continuation of lending at the proposed scale; and

- whether, as suggested by the Region, representations should be made by the Bank to the IMF at the highest level to ensure a more equitable sharing of assistance to Jamaica. What would be an equitable sharing of risks?

Program Content and Country Commitment

8. The overall performance of the Jamaican economy since 1981 has not been good. This has been partly due to external factors, such as the sharp drop in bauxite prices. But internal policies have also had a prominent role. Even in the case of bauxite, Jamaica has steadily lost its market share to other countries facing similar market conditions.

9. However, the performance during the last Jamaican fiscal year has been much better than expected earlier by both the Bank and the Fund staff. The last Bank mission reports that GDP growth has been higher (3.7% in real terms), exports--led by tourism--have done very well, the ratio of the current account deficit to GDP has fallen from 14.4% to 4.9% in one year, inflation is much less, and the level of unemployment has fallen by 3%. The extent to which this good performance reflects the delayed effects of earlier reforms is not yet clear but may well be very significant.

10. Optimism regarding the future program needs to be a bit guarded not only because of the past record, but also because of the impending elections and a possible change in government. The agreement with the Fund notwithstanding, the consistency of the reform program--especially as it relates to trade liberalization--with the fixed exchange rate regime can be questioned. While the government is committed to check appreciations of the real exchange rate, the expectations of a devaluation in a fixed-rate system might give rise to capital flight, or to much reduced private capital inflows than assumed in the financial projections. The Region might comment on:

- the ability of the government to stick to the schedule for trade reforms, especially if it is also unable to introduce the General Consumption Tax (which is not a condition of Bank/Fund operations),

- the feasibility of restoring flexibility in the nominal exchange rate at this time to avoid the possible need for a devaluation during the election year.

<u>Lending Program</u>

11. **With respect to policy loans, the forthcoming medium-term framework paper is expected to clarify the precise nature and sequencing of the reform process across a broad front.** Even without it one can see that neither of the reform programs being supported by the recent sector adjustment loans would be fully completed at the end of the design periods. In the case of the trade and finance loan, for example, considerable differentiation in the trade regime will remain. <u>Would the Region comment on the mix of instruments in the proposed lending program in view of the need to sustain the reform process and to maintain focus on the critical trade and finance issues</u>?

12. With respect to other loans, the Region proposes that the Bank finance all the foreign exchange costs of projects as well as local cost up to a limit of 75% of total project costs. This limit appears to be higher than the ones being used for countries at about the same per capita income level and in comparable circumstances. For Dominican Republic, for example, the Bank finances up to 60% total project costs; for Cameroon no local cost financing is permitted; and for Peru the Bank finances up to 50% of total project costs (up to 60% in social sector projects). The Committee may wish to discuss <u>the justification for the proposed generous limit for local cost financing, and decide on a level to ensure consistency among borrowers</u>.

August 24 MEETING

THE WORLD BANK / INTERNATIONAL FINANCE CORPORATION

# OFFICE MEMORANDUM

**DATE:** August 26, 1987

**TO:** Members, Policy Committee

**FROM:** Barber B. Conable

**EXT:** 72001

**SUBJECT:** Policy Committee Meeting of August 24, 1987: Staff Selection Round 2--Proposals for Accelerated Placement

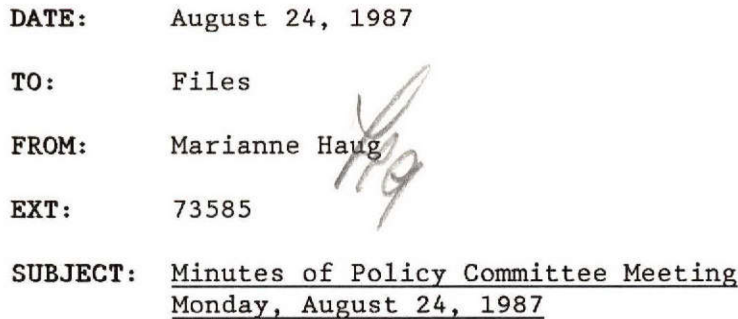
Further to the Policy Committee discussion of August 24, 1987, I wish to reiterate my support in principal to Mr. Wapenhans' memorandum dated August 21 on "Staff Selection Round 2--Proposals for Accelerated Placement".

I expect all managers to urgently and diligently review all placement and training options for available staff and vacancies following the timetable proposed. I plan to review with the Senior Vice Presidents the results of this effort upon my return from Europe, September 11. At that point I intend to decide whether further actions, such as transfer of vacancies and continued recruitment freeze are needed and appropriate to meet the objectives of the reorganization and the approved budget.

Barber Conable

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

# OFFICE MEMORANDUM



**DATE:** August 24, 1987

**TO:** Files

**FROM:** Marianne Haug

**EXT:** 73585

**SUBJECT:** Minutes of Policy Committee Meeting Monday, August 24, 1987

Attending:

Members

Messrs. Conable, Hopper, Thahane, Wapenhans

Acting

Messrs. Karaosmanoglu, Parmar, Scott, Vergin

Others

Mr. Cosgrove

Staff Selection Process--Round 2: Proposed Improvements

1. Mr. Conable stated that he has no intention of going back to the Board to obtain additional budget funds or authorization for additional personnel lay-offs. He expected the managers to manage the process and therefore endorse the measures proposed in Mr. Wapenhans' memorandum to the Policy Committee dated August 21, 1987. Mr. Karaosmanoglu brought to the Committee's attention the difficulty in placing the remaining five percent of staff, in particular, at Level 25. It was agreed that following the September 4 deadline, it might be necessary for the Senior Vice Presidents and Vice Presidents to sit down and review the Level 25 vacancy situation and agree to redistribution of vacancies. An additional redistribution of Level 25 vacancies among a panel of Technical Directors would take place during this week.

2. Mr. Scott reported on the situation of the Administrative Tribunal. He noted that, in the Legal Department's view, the cases of the Staff Association and ten officers of the Staff Association were unlikely to have any standing. The Legal Department had to finalize their response by September 4 and Mr. Shihata would be reviewing the documents on his return.

3. Mr. Hopper noted the relatively high vacancy rate in his area and planned to review the matter with his managers today. He felt there was a "bunching" phenomenon which should normalize as soon as the deadline approaches.

4. Mr. Conable closed the meeting noting that he wished to review the present situation with each Senior Vice President in individual discussions during the course of the day.

# POLICY COMMITTEE MEETING

MONDAY, AUGUST 24, 1987

9:30 a.m.

## AGENDA

1. Staff Selection Process--Round 2
   Proposal for Improvements

THE WORLD BANK / INTERNATIONAL FINANCE CORPORATION

# OFFICE MEMORANDUM

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DATE: August 21, 1987

TO: Members of the Policy Committee

FROM: Willi A. Wapenhans

EXT: 75656

SUBJECT: Staff Selection Round 2 -- Proposals for Accelerated Placement

1. We discussed on August 19 the lack of progress of Round 2 staff selections and concluded that much greater efforts were needed to achieve substantially more job-person matches. The purpose of this memo is to make specific proposals to reach those results. The proposals break down in two categories:

- action to encourage managers to increase selections and extend offers formally; and
- action to encourage unselected staff to seek positions and submit applications.

Action to Encourage Selections

2. This set of action proposals includes the following:

(a) Managers in each Vice Presidency should systematically review, with their Personnel Teams, unselected staff they have either interviewed or who belong to that Vice Presidency and explicitly address in each case the feasibility of training/retraining. These assessments should be shared with the VPPER by no later than September 4. Where suitability for a future job within the VPU is determined, the responsibility for a job offer conditional on training rests within the Vice Presidency and would represent a selection against a VPU position.

(b) Managers with vacancies should report to their SVPs for each vacancy still unfilled by September 4 (or such earlier date as the SVP may chose), the efforts they have made to fill them (considering candidates available on the roster or from skill searches, candidates interviewed, underfill options, offers made, files reviewed, etc.) and state in writing the reasons why they have not selected anyone. Non-selection will be questioned in particular for disciplines where the Round 2 roster indicates an ample supply of candidates with apparent requisite qualifications. (VPPER has just circulated to each of you lists of all your vacancies sorted by department, to facilitate your review.)

P-1867

(c) In the case of secretarial vacancies, we have analyzed the roster of available candidates and positions as of August 21, and have found the following:

| Position Type | No. of Positions Available | No. of Candidates |
|---|---|---|
| Secretarial (grade 13/14) | 71 | 37 |
| Staff Assistant (grade 15) | 62 | 65 |
| Sr. Staff Assistant/Adm.Sec./ Adm. Asst. (grade 15-17) | 13 | 42 |
| | 146 a/ | 144 |

Managers should be made aware that a systematic review of the 144 secretarial staff on the Round 2 roster shows that a large majority have satisfactory performance records. Notwithstanding some grade mis-match between available positions and candidates, the following actions are recommended:

- o the filling of secretarial slots in all cases where a suitable candidate exists (even if the higher level staff to be supported are not yet in place; in the interim, use of such placements can be made to reduce recourse to temporaries, overtime, and/or TAP);
- o the systematic review of any between-unit (but within VPU) reassignments to even out distribution of scarce but needed skills (e.g., bilingual) to enable greater absorption of other available secretaries, taking into account staff preferences to the extent possible;
- o the reclaiming (by September 11) by the SVP or VP concerned of any vacant secretarial positions below the budgeted fill ratio by department;
- o and immediate creation of VPU (or SVPU) pools of support staff to be recruited at their existing level and managed within the VPU (or SVPU) to provide support to sub-units as needed.

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a/ It should be remembered that the salary budget assumes that, on average, a percentage of positions will be vacant.

(d) Depending on the status of higher level staff selections, placement panels could be organized for various disciplines by September 8. One obvious one may be for the four Technical Directors to convene as a panel and review all candidates remaining against all vacancies in the respective technical disciplines, with a view to decide placements for a maximum number of reasonably qualified Round 2 staff. Similarly, panels for Country Departments could be organized to help place available and reasonably qualified economists and country officers; and a FIN/PPR panel could be set up to place budget/accountant staff and research assistants.

(e) SVP's should reclaim from their VPU's (or Departments, as appropriate) a share of the positions still vacant as of September 15 together with the salary funds associated with those positions. I would propose the following scheme:

Vacancy ratio greater than 5% less than 8% -- 25% of the vacancies to be reclaimed

Vacancy ratio greater than 8% less than 10% -- 35% of the vacancies to be reclaimed

Vacancy ratio greater than 10% -- 50% of the vacancies to be reclaimed

(If the principle of this scheme is acceptable it could be refined to link the "tax" level to budgeted fill ratios which vary by unit.)

The positions could be reallocated, based on work program needs, within the SVPU where they could be filled with Round 2 candidates. As of September 18, a similar "taxation" could take place institution-wide with the positions and salary funds reclaimed by PBD, among other things to help provide positions for staff undergoing training with an institutional replacement guarantee from the VPPER. The latter would occur in cases where absorption outside a VPU is recommended by managers and accepted by the VPPER.

(f) All rejections of offers exclusively because the candidate's grade is higher than the position grade, should be brought to the attention of the VPPER. The VPPER will consider the merits of proposed solutions for each case.

(g) Since it is unlikely that many of the 142 TAP positions will be filled, we recommend that 70 positions be made available by the VPPER to SVPU's for support level positions, including both secretarial and non-secretarial. The allocation would be made on the condition that the position would be filled by someone from the Round 2 roster. The position authorization would bring with it the 25% of the salary budget which had been allocated to TAP. The remainder would be funded from existing VPU budgets, which already included an allowance for TAP use.

(h) Until we are in a position to determine that adequate progress has been made in Round 2 selections, I propose to reserve the decision on when external recruitment will be reopened.

Actions to Encourage Staff

3. Although staff have been strongly encouraged to apply, some 350 staff on the Round 2 roster have not sent in any applications. While in some cases this may be because they are "holding out" for Package B, there is evidence that many staff would accept jobs but are not applying because of fear of rejection, cultural aversion to job seeking, or simply disaffection with the process. The following actions are taken or being considered:

(a) VPPER has written again to all those who have not applied to urge them to contact their staff advisers.

(b) The Personnel Teams are also contacting these staff to find out why they are not making more efforts and urging them to apply for jobs of interest to them, as otherwise they might be selected for jobs they would not have chosen.

(c) Also, staff in VPPER are in the process of preparing and sending out lists of candidates for each vacancy for which no applications were received, using the Bank skills inventory.

(d) As noted in para 2(e) above, I am considering guaranteeing placement in positions at the staff member's level to all staff with skills for which there will be ongoing demand in the Bank but who need, and are willing, to undergo training. This will place a difficult longer term responsibility on the Bank's management. However, it is just not acceptable, nor budgetarily feasible, to separate a large number of staff while the overall vacancy ratio is around 10%.

cc: Mr. Stanton
Ms. Haug
Mr. Liebenthal

August 19 MEETING

J-3077

POLICY COMMITTEE MEETING

Wednesday, August 19, 1987 at 9:30 a.m.

AGENDA

1. Staff Selection Process - Round 2

   - Status and Prospects

   - Separation Packages - Implications of Amounts and Numbers involved

2. Proposed Information Technology Policy Committee

   (Memo from Mr. Wapenhans dated August 17, 1987)

3. Miscellaneous

Attending:

Messrs. Rajagopalan (acting for Mr. Hopper), Stern, Thahane, Wapenhans, Scott (acting for Mr. Shihata), Camacho (acting for Mr. Ryrie)

THE WORLD BANK / INTERNATIONAL FINANCE CORPORATION

# OFFICE MEMORANDUM

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DATE: August 18, 1987

TO: Members of the Policy Committee

FROM: W.A. Wapenhans

EXTENSION: 75656

SUBJECT: Issues Paper - Staff Selection (Round 2) Progress and Probable Budget Constraints

1. I would like to bring to your attention the emerging Round 2 selection results, some indicative projections of shortfalls in the special budget for reorganization-related separations, and some options on action which we may need to take soon. My current estimate is that, even with a reinforced effort to place remaining staff, an additional budget allocation in the range of $25 to $87 million will be needed to handle separations. This may argue for placing a supplementary budget paper before the Board within the next two weeks. Both the emerging number of probable separations and the unit costs are higher than in the budget approved by the Board. We need to think through our staffing tactics (to minimize the incremental budget need) and our plans to tackle the budget implications. This note provides some background and options.

2. General. There are 744 of the staff members who were on board at end-June who have not been placed or confirmed in Bank jobs as of August 17. This number is derived as follows:

| | Number | % |
|---|---|---|
| Staff on Board June 30, 1987 (IBRD regular, fixed term and part-time regular) | 5,976 | 100.0 |
| (less) Staff not Affected (YPs in early assignment, support staff in ED offices, staff on special leave, etc.) | 132 | 2.2 |

| | | |
|---|---|---|
| (less) Confirmed Staff Selections from Managerial & Staff Round 1 (not all Round 1 staff selection forms were signed and/or returned) | 4,862 | 81.4 |
| (less) Confirmed Staff Selections from Round 2 | 82 | 1.4 |
| (less) Staff Negotiating or Having Completed Negotiations for Separation under Package B | 156 | 2.6 |
| Remainder | 744 1/ | 12.4 |

Our analysis of the composition of the 744 is that it includes some 69 cases of staff not participating in the Round 2 selection process for a number of special reasons (these "other cases" include such things as terminations since July 1 for reasons unrelated to the reorganization; pending transfers to IFC; staff on extended sick leave; etc.). Of the remaining 675 staff, 422 are HL and 253 SL. A more detailed analysis is provided in Annex 1.

3. The prospective situation for staff not yet placed can be further viewed taking into account the following:

(a) most, if not all, of the group of 69 special cases noted above will be handled in ways which will not create reorganization budget claims;

(b) 32 additional cases of eligibility for Package B have been tentatively identified by the Personnel Officers;

(c) there are 249 applicants for Package A, of which 78 have not received position offers; a minimum of at least these 78 will be informed this week that they will be granted Package A;

(d) there remain 606 vacant positions (421 HL and 185 SL) advertised and available in the Round 2 process (Annex 2 provides a summary of the location by SVP complex and composition of these);

(e) there are also up to 142 positions available to support staff wishing to join the expanded Temporary Assignment Program, but early soundings indicate a very low level of staff interest in pursuing this option; and

---

1/ Includes some staff believed to have already been selected, but for whom selection confirmation forms have not been received or processed.

(f) only 28 cases of training (either for staff selected for positions in the respective complexes or with institutionally guaranteed reentry) have been identified to date out of the some 100 cases assumed in the budget.

4. Scenarios. Several scenarios can be developed to consider the budget and placement implications which confront us. For ease of reference, I label these pessimistic, middle and optimistic and focus first on the placement/separation numbers. The "optimistic" scenario now appears rather unlikely and it (or an even better result) would depend on a combination of good luck and exceptional success in pursuing all of the actions suggested in para 9.

| | Pessimistic | Middle | Optimistic |
|---|---|---|---|
| Starting Number | 744 | 744 | 744 |
| less: Additional Round 2 Selections before Sept. 30 (some with Training contingency), including cases of Round 2 reconfirmations of Round 1 Selection Forms which had not been received | 100 1/ | 190 1/ | 280 1/ |
| Institutionally Guaranteed Reentry after Retraining | 10 2/ | 10 2/ | 10 2/ |
| TAP | 20 | 40 | 60 |
| Cases likely to be handled Outside Reorganization Exercise 3/ | 60 | 60 | 60 |
| Remaining for Separation | 554 | 444 | 334 |
| of which: Pkg. A | (110) 4/ | (130) 4/ | (150) 4/ |
| Pkg. B | (444) | (314) | (184) |

1/ Would leave a Bankwide vacancy rate of around 8-9%, 7% or 5-6% respectively.

2/ Very difficult to predict in the absence of concrete cases and reasons why respective complex could not as readily or appropriately offer re-entry guarantee.

3/ See paras 2 and 3 on nature of cases. Assumes some cases will revert to reorganization exercise.

4/ Would depend on increasing degree of feasibility for some Package A applicants with position offers to be separated in cases where other unselected staff (otherwise Package B candidates) were actually found to replace them in the respective positions.

| | | | |
|---|---|---|---|
| Package B Separations Already in Process or Agreed | 156 | 156 | 156 |
| TOTAL Separations | 710 | 600 | 490 |
| of which: Pkg. A | (110) | (130) | (150) |
| Pkg. B | (600) | (470) | (340) |

5. A number of actions to stimulate a selection pattern which would reduce separation requirements are noted in para 9 below.

Budget Implications

6. The selection scenarios above suggest the almost certain emergence of a separation number in excess of the 390 approved by the Board. Experience to date with separation expenditure per actual Package B is that unit costs are higher than expected (reflecting a higher than predicted average age, length of service and salary per recipient). Together these 2 phenomena present the need for additional budget, even if an optimistic (or slightly better) selection pattern is achieved. Annexes 3 and 4 provide summary data on experience with unit costs and Annex 5 summarizes the current disposition of the reorganization budget.

7. Within the existing budget, there are several variables which one can work with:

(a) the relative share of Package A separations compared to Package B might be adjusted marginally by identifying cases where otherwise non-selected staff members (and likely to get Package B) can be found to fill the slots already offered to Package A applicants (171 of the 249 Package A applicants), thereby reducing the average cost of separations; this does not affect the aggregate "number" problem, however;

(b) a number of the separation cases (so far 10, but this is likely to increase) are from the 27 separation cases in process before the reorganization; FY87 budget was committed for handling the separations of the 27; some of the 27 are, however, now finding positions; we need to confirm with PBD and Accounting whether these funds can in fact still be drawn upon, and then to consider whether the cost of those not finding jobs now should not be charged fully to the FY87 funding rather than partly to the FY87 funding and partly to the reorganization exercise (20 cases at the average Package B cost to date would run a total of about $7.15 million, of which the incremental cost relating to

Package B benefits would probably amount to about $2 million; the remaining sum of just over $5 million should in any case be charged to the FY87 commitment assuming those funds are still available);

(c) we should confirm now that the July 1 - September 30 salary costs of staff members to be separated will need to be covered by the regular budget (as originally planned) rather than the reorganization budget (as more recently discussed); and

(d) most importantly, an increasingly aggressive selection process needs to be pursued.

8. Nonetheless, it is my best judgement that, assuming we stand firm against resorting to forced placements, we are going to be faced with the need to seek additional funding for reorganization-related separations. My estimate is that the range of such funding will vary between a low of $24.8 million and a high of $86.7 million as follows:

| | Costs (Units $ Millions) Under | | |
|---|---|---|---|
| | Pessimistic Selection Scenario | Middle Selection Scenario | Optimistic Selection Scenario |
| Cost of Package Bs Committed (as per Annex 5) | 55.8 | 55.8 | 55.8 |
| Cost of Additional Package Bs 1/ | 108.8 | 76.9 | 45.1 |
| Cost of Package As 2/ | 16.0 | 18.8 | 21.8 |
| Other costs (as per items B-E in Annex 5 with some adjustment for added resettlement) | 14.6 | 12.6 | 10.6 |
| Sub-Total | 195.2 | 164.1 | 133.3 |
| less: Full Cost Adjustment for up to 20 Separations from "Group of 27" | 7.2 | 7.2 | 7.2 |
| Adjusted Sub-Total for Separations and Misc. Reorg. Costs 3/ | 188.0 | 156.9 | 126.1 |
| Available | 101.3 | 101.3 | 101.3 |
| Shortfall | 86.7 | 55.6 | 24.8 |

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1/ Using an average of unit costs for levels 18-25 and 11-17 from Annex 3 weighted by the HL/SL split indicated in para 2. This results in an average unit cost for new Package Bs of $245,000.

2/ Using a weighted average of unit costs of levels 18-25 and 11-17 by adjusting Annex 3 data to reflect differences between Package A and Package B benefits. The results are an average unit cost for Package A of $145,000.

3/ Assumes all July 1 - September 30 salary costs of separated staff will be covered by the regular budget.

Action Options

9. Selection Process. Among the key tools (not mutually exclusive) we have available to minimize the number of separations (and to move from what might well otherwise be a "pessimistic" outcome) are the following:

(a) persuasive encouragement from senior management to their respective managers and intensive, systematic review of selection efforts by each complex; in this regard, I would appreciate: (i) a quick reading from you on how many more vacancies your managers feel they will be able to commit in Round 2 (including with resort to the training/retraining options), particularly in areas where large numbers of vacancies now exist; (ii) your re-emphasizing to your managers how vital the training tool may be in increasing the extent to which unselected staff might be matched to vacancies; (iii) your assessments on whether the maximum is being done in your respective complexes to utilize effectively staff at Grades 18 - 21; and (iv) any concrete suggestions you have on increasing the match-making between candidates and vacancies;

(b) VPP provision of such services as further skills searches for positions still vacant; and assistance in identifying and preparing training programs (an updated booklet on the processes and options is about to be circulated);

(c) consideration of an extended freeze on recruitment or on long term consultancy contract renewal (we have planned to maintain the freeze on recruitment, with only few exceptions, through September 30; the Staff Association suggests we announce a freeze through December 31; feedback from Personnel Officers suggests that a lengthened freeze on recruitment or action on use of longer term consultants would be extremely detrimental to work programs);

(d) mounting, probably through the personnel teams, staff advisors and Staff Association, an effort to encourage further selections of support staff to available support vacancies and, where this is not possible, to encourage unselected support level staff to participate in TAP; any suggestions on how to make more support level selections in Round 2 or on how to make TAP a more attractive option would be most welcome; and

(e) indirect pressure on managers to find the best available fits by such means as reversion of a share of vacancies and related salary budget in each complex to PBD to help fund the additional separation costs.

10. Budget Process/Next Steps. The last of the above options to encourage selections may also be, in the worst case, one of the options which may need to be considered for budgeting reasons. Other budget related steps we should consider are, in summary:

(a) alerting the Board in the end-August progress report on the reorganization to the probable need for additional budget;

(b) without in any way diminishing the efforts to increase the number of selections, mobilizing preparation of a supplementary budget request with a view to presenting it to the Board as early as the first week of September; this will have to address the question of the reasons for the number of separations now foreseen and the issue of the cost benefit analysis for the reorganization (and the "payback" period); clearly, the timing of such a request is a highly sensitive issue and will need to take into account the timing of the Annual Meeting, the selection time constraints imposed on us by the Staff Rule and the high cost of delaying separations;

(c) confirming that the July 1 - September 30 salary costs for staff to be separated should be covered by the regular budget (rather than the reorganization budget);

(d) deciding on an approach to the handling of the number and cost of separations from the previously identified "Group of 27"; and

(e) determining whether there may be any other (albeit painful) ways to find resources from the FY88 regular budget to help offset the increase needed to cover the reorganization or to help improve the reorganization "payback."

Attachments

cc: Mr. Stanton
Ms. Haug
Messrs. Cosgrove/Hume/Senner
Picciotto/Murli/Challa

ANNEX 1

Annex 1: Disciplines of Staff Not Yet Placed 1/
data as of August 17, 1987

| LG | Discipline | Sub-Discipline | Number | Percent |
|---|---|---|---|---|
| HIGHER | ACCOUNTANT | n/a | 20 | 3.0 |
| | ADMINISTRATION/BUDGET | n/a | 37 | 5.5 |
| | BUILDINGS/FACILITIES | n/a | 1 | .1 |
| | COUNTRY OFFICER | n/a | 35 | 5.2 |
| | DOCUMENT/RECORDS MANAGEMENT | n/a | 5 | .7 |
| | ECONOMIST | n/a | 57 | 8.4 |
| | EDITOR/PUBLICATIONS | n/a | 1 | .1 |
| | FINANCIAL ANALYST | n/a | 20 | 3.0 |
| | INFORMATION/COMPUTER SYSTEMS | n/a | 23 | 3.4 |
| | LINE MANAGER | n/a | 17 | 2.5 |
| | OPERATIONS/RESEARCH ASST | n/a | 18 | 2.7 |
| | OTHER | n/a | 47 | 7.0 |
| | PERSONNEL/COMPENSATION | n/a | 6 | .9 |
| | PRINTING/GRAPHICS/CARTOGRAPHY | n/a | 1 | .1 |
| | PUBLIC AFFAIRS | n/a | 7 | 1.0 |
| | RESEARCH | n/a | 36 | 5.3 |
| | RESIDENT REPRESENTATIVE | n/a | 4 | .6 |
| | SR MGR | n/a | 2 | .3 |
| | TECHNICAL SPECIALIST | AGRICULTURE/AGRONOMY | 8 | 1.2 |
| | | ARCHITECT/CONSTRUCTION | 3 | .4 |
| | | EDUCATION/TRAINING | 7 | 1.0 |
| | | ENERGY | 3 | .4 |
| | | ENVIRONMENT | 1 | .1 |
| | | EVALUATION | 5 | .7 |
| | | FOREST/TREE CROPS | 1 | .1 |
| | | HIGHWAY | 4 | .6 |
| | | IRRIGATION | 4 | .6 |
| | | LIVESTOCK/FISHERY | 2 | .3 |
| | | MINING/GEOLOGY | 1 | .1 |
| | | OTHER | 19 | 2.8 |
| | | PETROLEUM/GAS | 5 | .7 |
| | | POPULATION/DEMOGRAPHER | 2 | .3 |
| | | PORT | 1 | .1 |
| | | POWER | 5 | .7 |
| | | PROCUREMENT | 1 | .1 |
| | | PUBLIC HEALTH/NUTRITION | 1 | .1 |
| | | RAILROAD | 1 | .1 |
| | | TRANSPORTATION | 2 | .3 |
| | | URBAN | 5 | .7 |
| | | WATER/SANITATION | 2 | .3 |
| | WORD PROCESSING | n/a | 2 | .3 |
| Level,Group HIGHER | | | 422 | 62.5 |
| SUPPORT | ACCOUNTANT | n/a | 8 | 1.2 |
| | ADMINISTRATION/BUDGET | n/a | 9 | 1.3 |
| | CLERK | n/a | 1 | .1 |
| | DOCUMENT/RECORDS MANAGEMENT | n/a | 16 | 2.4 |
| | EDITOR/PUBLICATIONS | n/a | 2 | .3 |
| | INFORMATION/COMPUTER SYSTEMS | n/a | 7 | 1.0 |
| | OPERATIONS/RESEARCH ASST | n/a | 3 | .4 |
| | OTHER | n/a | 22 | 3.3 |
| | PRINTING/GRAPHICS/CARTOGRAPHY | n/a | 1 | .1 |
| | RESEARCH | n/a | 2 | .3 |
| | SECRETARY/STAFF ASSISTANT | n/a | 135 | 20.0 |
| | SR STAFF ASST/ADMIN SEC/ADMIN ASST | n/a | 38 | 5.6 |
| | WORD PROCESSING | n/a | 9 | 1.3 |
| Level,Group SUPPORT | | | 253 | 37.5 |
| TOTAL | | | 675 | 100.0 |

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1/ Does not include data on the 69 "other cases" noted in paras. 2 and 3 of memo. However, does include some staff believed to have already been selected, but for whom selection confirmation forms have not been received or processed.

Annex 2-A: Remaining Round 2 Vacancies as of August 17, 1987

| LEVGRP | Discipline | Sub-Discipline | Number | Percent |
|---|---|---|---|---|
| HIGHER | ACCOUNTANT | n/a | 22 | 3.6 |
| | ADMINISTRATION/BUDGET | n/a | 9 | 1.5 |
| | BUILDINGS/FACILITIES | n/a | 8 | 1.3 |
| | COUNTRY OFFICER | n/a | 10 | 1.7 |
| | DOCUMENT/RECORDS MANAGEMENT | n/a | 1 | .2 |
| | ECONOMIST | n/a | 132 | 21.8 |
| | EDITOR/PUBLICATIONS | n/a | 1 | .2 |
| | FINANCIAL ANALYST | n/a | 28 | 4.6 |
| | INFORMATION/COMPUTER SYSTEMS | n/a | 31 | 5.1 |
| | INVESTMENT OFFICER | n/a | 9 | 1.5 |
| | LINE MANAGER | n/a | 1 | .2 |
| | OPERATIONS/RESEARCH ASST | n/a | 27 | 4.5 |
| | OTHER | n/a | 4 | .7 |
| | PERSONNEL/COMPENSATION | n/a | 9 | 1.5 |
| | PUBLIC AFFAIRS | n/a | 4 | .7 |
| | RESEARCH | n/a | 6 | 1.0 |
| | TECHNICAL SPECIALIST | AGRICULTURE CREDIT/INDUSTRY | 6 | 1.0 |
| | | AGRICULTURE/AGRONOMY | 8 | 1.3 |
| | | ARCHITECT/CONSTRUCTION | 2 | .3 |
| | | CHEMICAL | 1 | .2 |
| | | EDUCATION/TRAINING | 10 | 1.7 |
| | | ENERGY | 3 | .5 |
| | | ENVIRONMENT | 10 | 1.7 |
| | | EVALUATION | 4 | .7 |
| | | FOREST/TREE CROPS | 2 | .3 |
| | | HIGHWAY | 2 | .3 |
| | | INDUSTRY | 2 | .3 |
| | | INFRASTRUCTURE | 2 | .3 |
| | | IRRIGATION | 3 | .5 |
| | | OTHER | 4 | .7 |
| | | PETROLEUM/GAS | 2 | .3 |
| | | POPULATION/DEMOGRAPHER | 7 | 1.2 |
| | | PORT | 2 | .3 |
| | | POWER | 10 | 1.7 |
| | | PROCUREMENT | 1 | .2 |
| | | PUBLIC HEALTH/NUTRITION | 7 | 1.2 |
| | | PUBLIC SECTOR MANAGEMENT | 12 | 2.0 |
| | | RAILROAD | 4 | .7 |
| | | RURAL DEVELOPMENT/EXTENSION | 4 | .7 |
| | | SOCIOLOGY | 2 | .3 |
| | | TRANSPORTATION | 2 | .3 |
| | | URBAN | 6 | 1.0 |
| | | WATER/SANITATION | 1 | .2 |
| *TOTAL LEVGRP HIGHER | | | 421 | 69.5 |
| SUPPORT | ACCOUNTANT | n/a | 3 | .5 |
| | BUILDINGS/FACILITIES | n/a | 1 | .2 |
| | CLERK | n/a | 1 | .2 |
| | DOCUMENT/RECORDS MANAGEMENT | n/a | 9 | 1.5 |
| | FINANCIAL ANALYST | n/a | 1 | .2 |
| | INFORMATION/COMPUTER SYSTEMS | n/a | 9 | 1.5 |
| | OTHER | n/a | 2 | .3 |
| | SECRETARY/STAFF ASSISTANT | n/a | 140 | 23.1 |
| | SR STAFF ASST/ADMIN SEC/ADMIN ASST | n/a | 13 | 2.1 |
| | WORD PROCESSING | n/a | 6 | 1.0 |
| *TOTAL LEVGRP SUPPORT | | | 185 | 30.5 |
| TOTAL | | | 606 | 100.0 |

Annex 2-B: Number of Round 2 Vacancies by Senior Vice-Presidency
data as of August 17, 1987

| New SVPU | Level Group HIGHER | SUPPORT | TOTAL |
|---|---|---|---|
| Operations | 204 | 92 | 296 |
| Finance | 35 | 14 | 49 |
| PPR | 113 | 38 | 151 |
| Administration | 60 | 35 | 95 |
| Other | 6 | 6 | 12 |
| IFC | 3 | . | 3 |
| TOTAL | 421 | 185 | 606 |

## Summary of Committed and Projected Unit Costs

### Package B Unit Costs

| | BOARD ESTIMATES | | AUGUST 14 | |
|---|---|---|---|---|
| | No. | Unit Cost | No. | Unit Cost |
| Levels 26 + | 43 | $445,000 | 58 | $518,000 |
| Levels 18-25 | 214 | $250,000 | 69 | $310,000 |
| Levels 11-17 | 33 | $100,000 | 29 | $136,000 |
| TOTAL | 290 | $265,000 | 156 | $355,000 |

Notes:

1. The Board estimates were based on average age, length of service, and salary data estimated usage of various benefits.

2. The estimated projected and commuted unit costs are based on actual staff members, with calculated pension and severance payment costs, and maximum usage of various benefits.

MAIN/Unit Costs
08/17/87

**Comparison of Demographics Used for Board Estimated and Demographics of Projected and Committed Staff for Package B**

| | Board Estimates | Projected and Committed Staff TO AUGUST 14, 1987 |
|---|---|---|
| Levels 26+ | | |
| Number | 43 | 58 |
| Average Service | 15 | 20 |
| Average Age | 49 | 57 |
| Average Salary | $84,500 | $87,500 |
| Levels 18-25 | | |
| Number | 214 | 69 |
| Average Service | 10 | 16 |
| Average Age | 44 | 51 |
| Average Salary | $58,000 | $54,200 |
| Levels 11-17 | | |
| Number | 33 | 29 |
| Average Service | 8 | 16 |
| Average Age | 40 | 50 |
| Average Salary | $23,000 | $27,100 |

MAIN/Demographics Package B
08/17/87

# SUMMARY OF COMMITTED AND PROJECTED COSTS FOR STAFF SEPARATIONS

($000)

AS OF : AUGUST 14, 1987

| | BUDGET ALLOCATION ($) | 1/ COMMITTED ($) | PERCENTAGE COMMITTED (%) | 2/ PROJECTED ($) | PERCENTAGE PROJECTED (%) | TOTAL COMMITTED & PROJECTED ($) | TOTAL COMMITTED & PROJECTED (%) |
|---|---|---|---|---|---|---|---|
| A. COST OF STAFF SEPARATIONS | | | | | | | |
| Number of Staff: 3/ 156 | | | | | | | |
| Separation Payment 4/ | 81,500.0 | 11,721.4 | 14.4% | 37,782.8 | 46.4% | 49,504.2 | 60.7% |
| Benefits 5/ | 4,300.0 | 430.4 | 10.0% | 1,450.7 | 33.7% | 1,881.1 | 43.7% |
| Other Services 6/ | 6,900.0 | 1,245.3 | 18.0% | 3,201.5 | 46.4% | 4,446.8 | 64.4% |
| SUB-TOTAL | 92,700.0 | 13,397.1 | 14.5% | 42,435.0 | 45.8% | 55,832.1 | 60.2% |
| B. COSTS FOR RESETTLEMENT 7/ | 1,100.0 | 1,100.0 | 100.0% | 0.0 | 0.0% | 1,100.0 | 100.0% |
| C. TRAINING FOR SKILLS UPGRADING | 4,500.0 | 358.2 | 8.0% | 0.0 | 0.0% | 358.2 | 8.0% |
| Number of Staff: 29 | | | | | | | |
| D. OFFICE MOVES | 2,500.0 | 1,624.0 | 65.0% | 876.0 | 35.0% | 2,500.0 | 100.0% |
| E. COMPUTER CHARGES | 500.0 | 0.0 | 0.0% | 0.0 | 0.0% | 0.0 | 0.0% |
| TOTAL | $101,300.0 | $16,479.3 | 16.3% | $43,311.0 | 42.8% | $59,790.3 | 59.0% |

1/ Includes staff who have signed a Separation Agreement.
2/ Based on the number of staff who have been notified in writing by their Senior Personnel Officer that they are eligible for Package B, and who have responded in writing that they intend to elect Package B. They have not yet signed a Separation Agreement.
3/ Includes 10 of the 27 suspended redundancy cases. Cost of their packages will be removed from Supplemental budget figures and charged to the accrued FY87 Special Leave/Skills Mix accounts.
4/ Separation payments includes: severance pay, tax allowance for U.S. nationalities and cost to the Bank for supplemental pension.
5/ Benefits include: insurance (Medical & Life) and Education Benefits.
6/ Other Services include: costs for consultants (Price Waterhouse, Benefit Counsellors, Staff Advisors); travel for job or home search; external training; and seed capital; and other overhead expenses.
7/ Entire amount has been committed to Overhead resettlement account. Estimated cost per resettlement is $22,000.

THE WORLD BANK / INTERNATIONAL FINANCE CORPORATION

# OFFICE MEMORANDUM

**DATE:** August 19, 1987

**TO:** Files

**FROM:** Robert Liebenthal, Acting Secretary

**EXT:** 73586

**SUBJECT:** Minutes of Policy Committee Meeting
Wednesday, August 19, 1987

Attending:

Members
Messrs. Qureshi (Chairman), Stern, Thahane, Wapenhans

Acting
Messrs. Camacho, Scott, Liebenthal (Secretary)

Others
Mr. Senner

1. Staff Selection Process--Round 2

The meeting discussed Mr. Wapenhans' memorandum of August 18, 1987, on the progress of Round 2 staff selection and probable budget constraints. In summary, the memorandum stated that 744 staff who were on board at end June had not yet been placed or confirmed in Bank jobs as of August 17, including 156 who were negotiating for, or had completed negotiations for, Package B. This included about 170 who had applied for Package A, but had been offered a job. Taking into account the progress of Round 2 selection and the decisions already taken to avoid forced placement, the numbers likely to be eligible for termination packages and the unit costs of termination were likely to exceed the amounts approved by the Board.

After the meeting had discussed a number of options, Mr. Qureshi concluded as follows:

(a) Every conceivable effort should be made to avoid going back to the Board for additional funds.

(b) Each SVPU should reexamine the availability of staff for vacant positions, on the basis of a list of potential candidates for each position.

(c) ADM should reassess the situation and be sure that there is a specific justification for each person not selected. In addition, some other options which had been discussed at the meeting should be examined further, notably the establishment of a permanent pool for secretaries, the relaxation of limits on the number of Level 25 staff, the introduction of a placement guarantee for staff selected for retraining, and the use of overfills--in addition to the suggestions in Mr. Wapenhans' memorandum.

2. The Proposed Information Technology Policy Committee

This item was postponed for future consideration.

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

# OFFICE MEMORANDUM

DATE: August 17, 1987

TO: Members of the Policy Committee

FROM: W.A. Wapenhans, SVPAD

SUBJ: Proposed Information Technology Policy Committee (ITPC)

1. One of the major recommendations of the Reorganization Steering Committee was to restructure the information management and technology function in the Bank. In addition to restructuring of ITF, the Steering Committee recommended a Bank-wide network of Committees to ensure proper oversight of the function by Senior line managers and to ensure coordination among different parts of the Bank. In this context, it recommended creation of a high level Information Technology Policy Committee.

2. The attached draft terms of reference for the Information Technology Policy Committee (ITPC) follow closely the Steering Committee's recommendations, except with respect to membership; I propose to add IFC to it. As anticipated by the Task Force, views and concerns of other parts of the Bank not represented on the Committee will be sought by the Secretariate and conveyed to the Committee, as necessary. For ease of reference, the relevant extracts from the Task Force report are also attached.

3. A critical requirement for the successful operation of the Committee and, indeed, its ability to help overcome the past weaknesses in the information technology functions throughout the Bank, will be that the Committee functions as a senior executive decision-making forum bringing to bear on its discussions and decisions institutional viewpoints as determined by senior line managers. For this reason, the members should be at the level of Vice President or equivalent. I would greatly appreciate it if you could send me your nomination by August 31. I propose to call the first meeting of the Committee by late September.

4. Since the proposed terms of reference of the ITPC and the Committee structure follow very closely the Steering Committee's recommendations, I do not propose inclusion of this item in the agenda of the Policy Committee, unless otherwise advised by you.

Attachment

cc; Mrs. Haug
Messrs: Cosgrove, Kohli

-- DRAFT --

# TERMS OF REFERENCE
# for
# INFORMATION TECHNOLOGY POLICY COMMITTEE (ITPC)

## Membership

1. The membership of the ITPC will be as below:

Chair: SVP Administration
Members: Vice President Representatives from Finance, Operations, PPR and IFC.

The Vice President level representatives will be nominated by the SVP concerned and would be subject to periodic rotation. Normal term of appointment will be 2-3 years. The nominee will also chair a high level Information Technology Committee of his own Complex. Director, PBD will be invited to join in the deliberations likely to result in additional resource needs at the institutional level.

## Secretariate

2. Director, Information, Technology and Facilities Department will be the Secretary of ITPC. He will be responsible for the agenda, documentation and staff attendance, as necessary. He will ensure that the deliberations and decisions of the Committee take place on the basis of completed staff work. The Secretariate will also be responsible for the recording, safe keeping, communication and follow up, as necessary, of decisions made, and for such measures as are necessary to protect the confidentiality of the proceedings.

## Responsibilities

3. The ITPC will be the highest institution-wide body charged with the responsibility to oversee the information management and technology activities throughout the Bank. It will review, decide on, or as appropriate, make recommendations to the Chairman on institutional strategies, policies, investments and plans for the management of information and information technology in the Bank.

4. To perform the above role, the specific responsibilities of the Committee will include the following:

(a) maintain an institutional oversight of information management and information technology (IMT) activities, strategies, policies, plans, investments and programs on a Bank-wide basis;

(b) review, consider and approve the structure, role and responsibilities of different committees and bodies related to IMT functions, including creation of new bodies;

(c) review and approve strategies, policies, investments and plans that may have a significant impact on the institution's business processes and budgets;

(d) monitor the overall information management and information technology activities in the Bank, review actual performance against agreed strategies and plans, and approve remedial actions, including changes in policy and plans;

(e) review and approve an annual report on information management and technology strategy to the Policy Committee;

(f) review and approve investments in major systems and hardware throughout the Bank;

(g) review and recommend for consideration by the President, the institutional component of the information and technology related budget of ITF;

(h) approve the size and priorities of the proposed Information Technology Innovation Fund, and oversee, through the Secretary, the work of the Information Technology Innovation Fund Committee.

Decision Making

5. As the senior-most institutional body on information management and technology activities, the Committee is expected to operate on a consensus basis. In case of opposing views, the Chairman will give the final ruling as the Bank's Senior Executive responsible for the Information Management and Technology function in the Bank group. However, in the case of decisions concerning additional budgetary resources, the Chairman will seek approval from the President.

Bankwide Committee Structure and Relationships

6. ITPC will be at the top of a pyramid of a network of four types of committees (see attached extract from Task Force report). Within the policy and strategic framework established by ITPC, each of the four main complexes and IFC will be responsible for formulating, implementing and evaluating information management and technology strategies, plans and activities. To help ensure a coordinated approach and necessary oversight by line managers, each complex (Administration, Finance, Operations, PPR and IFC) will maintain an Information Technology Policy Committee to deal with policy level matters under the jurisdiction of the Complex. The complex-specific committee will be chaired by the complex's representative on ITPC. Other members will be senior line managers at the level of Director or above. Director, ITF will be a member of each committee. The Secretariate service may be provided by the management/system/statistical Advisor to the SVP, or others.

7. The remaining two tiers of the network of committees will consist of:

(a) Specific purpose committees, as needed, at the Bank-wide or complex-wide level (e.g., Bank Information Management Systems, Information Technology Innovation Fund); and

(b) Information Exchange Committees along the lines of the existing Users Groups (e.g., IBM Advisory Group). Each of these committees will also be chaired by a line manager at an appropriately senior level.

Attachment

August 17, 1987

## PRINCIPAL RECOMMENDATIONS

### A. POLICY FRAMEWORK FOR INFORMATION/TECHNOLOGY

- Information and information technology should be assigned high priority and should be systematically managed from an institutional perspective.

- Within the strategic planning framework established by PPR, overall responsibility for establishing institutional policy on information and technology should rest with the SVP Administration, and the responsibility should be executed by means of a network of committees.

<u>First tier: Information Technology Policy Committee</u>

- The SVP Administration should chair an Information Technology Policy Committee which should comprise representatives (line-managers) of each of the four complexes. Membership in the committee should rotate periodically. ITF should act as the secretariat to this committee.

  - the Information Technology Policy Committee should be the senior executive organ for establishing institutional policy in information and technology.

  - The Information Technology Policy Committee should be responsible for:

    o maintaining an overview of information/technology activities, policies, plans and programs.

    o reviewing and approving broad policies, standards and strategies in information and technology that may have a significant impact on the organization's way of doing business or investments.

    o reviewing and approving major systems and investments.

    o reviewing and approving the institutional component of the information- and technology-related budget of ITF.

    o approving the size of the proposed Information Technology Innovation Fund.

<u>Second tier: committees led by individual complexes</u>

- Within the policy framework established by the Information Technology Policy Committee, each complex should be responsible for formulating, implementing and evaluating information and related technology strategies.

- To assist in ensuring a coordinated approach to fulfilling these

responsibilities, each of the main complexes should maintain an information technology policy committee to deal with information and related technology policy matters in areas under its jurisdiction.

| | |
|---|---|
| PPR: | Social and Economic Statistics Committee |
| Operations: | Operations Information Technology Committee |
| Finance: | Finance Information Technology Committee |
| Administration: | Administration Information Technology Committee |

- ITF should have a representative on each of the complex committees.

Third tier: specific purpose committees

- The Information Technology Policy Committee should also be responsible for designating committees to manage specific tasks that require greater time and technical expertise than the policy committee or complex committees can muster, yet necessitate mechanisms to ensure a combination of institutional viewpoints and user inputs into project design. Examples should include:

  - a committee to oversee a major system developments projects, such as the enhancements to the OpsMIS.

  - a committee to oversee an Information Technology Innovative Projects Fund to encourage and fund innovative activities, initiated by line managers, to be implemented in partnership with ITF. Such a committee might be staffed by managers at the director level, and chaired by a senior manager in a complex other than Administration.

  - the Information Security Committee.

Fourth tier: information exchange committees

- The fourth tier is the user committee structure, which mainly serve the purpose of exchanging information. These groups -- the Burroughs Advisory Group, IBM Advisory Group, DEC Advisory Group, OSAG Group, Communications User Group -- should be left to continue under their current mandate to foster close working relationships between ITF service providers and the relevant user communities.

Abolition of IRAC

- IRAC -- currently a high-level information exchange committee -- should be abolished, as it currently serves no institutional decision making purpose, and other new committees would serve its information exchange purpose.

Role of Data Administrators

- The responsibilities of the Data Administrators should be clarified, so as to make more explicit that the Data Administrator is a essentially a staff function of assisting line managers exercise their responsibilities for managing information and technology.

  - The representatives of the complexes on the main information/technology committees should be line managers, not Data Administrators.

  - The Data Administrators should only exercise line functions where there is a specific task for which they are given responsibility e.g. administering a specific data base.

THE WORLD BANK INTERNATIONAL FINANCE CORPORATION

# OFFICE MEMORANDUM

DATE: August 3, 1987

TO: Messrs. Moeen A. Qureshi
Ernest Stern and
Willi A. Wapenhans

FROM: W. David Hopper

SUBJECT: Creation of a Steering Group to Harmonize the Development of Management Information Systems in the Bank

While the Operations complex already has a reasonably complete and effective MIS, MISs in the other complexes are not as fully developed. A task force has mapped out a plan for MIS development in the Administration complex. The Finance complex has created an automation task force and is reviewing its MIS needs. PPR is moving towards use of the OPMIS for its own purposes, pending further review.

A mechanism is now needed to ensure that the four complexes' MISs are developed with compatible concepts, definitions, software, and procedures (e.g., for data transfer, updating, and validation). If such a mechanism is not created quickly to induce convergence, we run the risk of the systems growing in different directions. Vested interests in definitions, conventions, etc, might solidify and a unique opportunity for systems rationalization might well be lost. As a consequence, it could become more difficult for each complex to draw on -- or feed data to -- the other complexes' information systems and more difficult for PPR to aggregate data for the Board and to discharge its duty to monitor progress and flag issues for the Policy Committee.

Therefore, I suggest that we create a "Management Information Steering Group" to help ensure compatibility among the principal management information systems development efforts of the Bank. On the Group should be the principal officer in each complex who is responsible for MIS development, as well as a representative of ITF. Others would participate whenever appropriate. While the focus of the group would be on management information needs rather than technology, having ITF represented would ensure appropriate coordination with the Information Technology Policy Committee.

The Steering Group would work towards harmonizing, to the extent feasible, the continuing development of the MISs.

P-1867

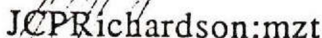
of the four complexes. It would do so by keeping each complex informed of the others' MIS development activities, identifying actual or potential areas of incompatibility, reconciling non-essential divergences, agreeing on information exchange procedures, resolving conflicts that arise, and -- more generally -- establishing principles, ground rules and conventions for cooperation.

If you agree, I would suggest that the Steering Group be chaired by the Director, PBD, as he is responsible for aggregating Bankwide information on plans, budgets and progress related to them for top management and the Board and was charged by the reorganization task forces with the responsibility "to maintain and improve interfaces to the other key data bases ... (e.g., the SVPs' MISs)." PBD's Budget Planning and Systems Division would provide support to the steering group and would coordinate its work with that of ITF's Policy and Strategy Staff.

Subject to your agreement, I have asked Mr. Picciotto to convene the Steering Group early in September upon his return from leave. By January 1, I would expect the Group to have agreed on -- or defined issues and obtained management decisions on -- the principal groundrules and conventions to be followed to promote requisite compatibility and complementarity among the MISs. By April, the Group should have reached consensus on linkages among plans for developing or further developing the complexes' MISs. By June 30, development work (if not already ongoing) should be fully under way -- with consultants, if necessary, selected, hired, and on the job. Thereafter, the Steering Group should oversee -- and resolve issues arising in the course of -- developing and improving the MISs.

I hope you will agree that this mechanism will help us make further important improvements in the Bank's systems for efficiently capturing, using, sharing, and aggregating management information. If you do, could you kindly let Mr. Picciotto's office know whom you have designated to serve on the Steering Group?

cc: Messrs. Conable
Picciotto



JCPRichardson:mzt

August 5 MEETING

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

# OFFICE MEMORANDUM

**DATE:** August 7, 1987

**TO:** Mr. W. David Hopper

**FROM:** Barber B. Conable

**SUBJECT:** Debt Task Force

The Debt Task Force, under the leadership of Jean Baneth, is to be commended for having produced a thought-provoking interim report under a tight deadline. The Task Force now must address the following questions:

(a) On the basis of a careful examination of individual country circumstances and prospects, what is the likelihood of successful adjustment with growth programs in each country? In particular, to what extent is the prospect for successful adjustment constrained by financial difficulties?

(b) What role should the World Bank play in addressing these financial problems through encouraging new or expanded use of new money facilities and other possible mechanisms?

(c) Finally, the Task Force should maintain an ongoing analysis of the major debt relief proposals made throughout the world; monitor such proposals as they arise in important national legislative processes; and advise the President of major developments in such proposals.

I want to be briefed on the progress of the Task Force's work before the Development Committee meeting, and the Task Force should issue a report on its findings by early November for further discussion by the Policy Committee. This is a high priority task on which PPR, Operations and Finance must cooperate fully. I hope that maximum effort will be made to achieve consensus through candid and constructive debate.

cc: Messrs. Qureshi, Stern

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

# OFFICE MEMORANDUM

**DATE:** August 11, 1987

**TO:** Files

**FROM:** Robert Liebenthal, Acting Secretary

**EXT:** 73586

**SUBJECT:** Minutes of Policy Committee Meeting Wednesday, August 5

Attending:

Members

Messrs. Conable, Hopper, Qureshi, Stern, Wapenhans

Acting

Messrs. Adams, Burmester, Scott

Others

Messrs. Baneth, Dubey, Jasperson, Lamb, Liebenthal, Shakow, Stanton, Underwood, Wood, Ms. Maguire

1. Interim Report on the Debt Problems of Middle Income Countries

Mr. Conable opened the discussion by expressing the hope that a consensus could be developed in the Policy Committee on this subject, which he expected would be controversial. He did not want the Bank to move towards fostering massive debt forgiveness, but the Bank should equally remain in communication with all sources of finance and important centers of opinion on the debt problem.

Mr. Qureshi said that the report had been rendered too early, since the areas of agreement and disagreement were not yet clear, and there remained some important analytical questions which had not been addressed. It was true, as the report stated, that the current strategy had not worked as anticipated, because of slow world economic growth, and that this had serious implications. But the approach suggested was not practical; it appeared as an encouragement to default. Furthermore, he did not share the judgement that the major indebted countries cannot grow and reduce their debt burdens. It would be difficult to obtain increases in commercial bank net exposure over the next few years; therefore the burden would inevitably fall on the World Bank and other international and official sources of finance. However, he believed there was scope for greater use of market mechanisms to convert the debt; in the case of countries like Bolivia, arrangements like the recent buy-back could enable the country to benefit from market discounts (since there was a high likelihood that significant amounts would be available on the secondary market), but not for larger

countries like Brazil or Mexico. Our aim, which should be reflected in the annual meeting speech also, should be the restoration of creditworthiness and voluntary lending to these countries within five years. He felt the work of the Task Force should continue in the direction of improving and strengthening the country analysis and examining ways of using the market, but we would not be seen as exercising leadership if we advocated debt relief. It would adversely affect our own ability to borrow money. We should examine ways of developing instruments for passing market discounts to borrower countries.

Mr. Wapenhans concurred, adding that the analysis should focus on conceptualising different country situations and responses, and should focus further on those work-out programs which were underfunded. Part of the pessimism was due to the exclusive focus on countries on the Baker list. At the same time, the debt issue should in no way be belittled; solid analysis was very important. The issue to develop, in each case, was how to fund recovery, not debt relief.

Mr. Stern added that both Turkey and Korea were highly indebted, but have managed their indebtedness successfully. Furthermore, much of the change in the debt ratios, which appeared so consistently negative, was attributable to large devaluations which had affected the denominator of the ratios more than the numerator, but all this showed was that GDP had been overvalued earlier, not that the real debt burden had changed. While he agreed that we should explore the risks, we should not be driven by pessimism, or by the fear of others taking the lead, into a change of strategy. He recommended that country analysis continue, and that financing packages continue to be the focus of action. But debt relief across the board should not be proposed. Not only would this not be acceptable to the Board, the Bank would lose credibility as a mediator. He did not believe that the Task Force was still needed; the country analysis should be part of normal analytical work, while the work on market-based instruments should be carried out in Finance and Operations. The Task Force should, at any rate, not work on debt relief schemes.

Mr. Hopper agreed that the analysis needed to be country-specific, but underlying the analysis was the proposition that, unless something was done to reduce debt burdens, it would be hard to reestablish growth. Existing market instruments did not seem to be succeeding; it seemed desirable at least to explore ways of using the Japanese surpluses and some other public money. The Bank should be seen as an active participant in resolving debt problems and should also take account of the increasing number of reputable agencies that foresaw major difficulties.

Mr. Conable concluded that there would have to be further discussion on the mandate of the Task Force.

2. <u>Annual Meeting Speech</u>

Mr. Qureshi felt that the speech covered too many issues and that several might be presented differently: for example, the Sub-Saharan Africa section, Asia (where the poverty focus should be more strongly

emphasised), the Highly Indebted Countries, where the focus should be on getting to a voluntary lending situation within a target period. Mr. Wapenhans and Mr. Conable both said there should be more on reorganization, which should be presented in forward-looking terms. Mr. Stern suggested that the discussion of the middle income countries should develop more around their development prospects and financing requirements, with a less exclusive focus on debt. The Committee's suggestions would be incorporated.

3. Direct Financing of NGOs

Mr. Conable said that the proposal would help greatly in strengthening political support for the Bank among the NGOs, and could help our development effectiveness by enlisting skilled but relatively low-cost manpower. Mr. Stern saw several problems with the proposal: first, this would be a further claim on an already tight budget and would contribute to the growing number of special programs on which the Board had already expressed concern. A second concern was the possible encouragement to NGOs to circumvent government agencies, especially planning and aid coordination mechanisms which the Bank was otherwise trying to strengthen. In general, it was easier to provide support to NGOs through IDA project components. If the grant option were chosen, it would be important to pay atention to, and develop guidelines for relations with government agencies. Mr. Burmester added that this was also likely to be the concern of Part Two countries at the Board. Mr. Qureshi supported this proposal, since he believed that NGOs could help in many ways, including dealing with the impact of the social cost of adjustment. The funding of the NGO should be cleared with central government--but should not be decided by it. Mr. Hopper added that the proposed fund would be more of an incentive for governments to use NGOs than if the funding were only available, as at present, through IDA projects. It was agreed that PPR should work with Operations to explore ways of carrying this proposal out.

**POLICY COMMITTEE MEETING**

WEDNESDAY, AUGUST 5, 1987

9:30 a.m.

**AGENDA**

1. Interim Report on Debt Problems in Middle-Income Countries
   (Memo from Mr. Baneth dated July 31, 1987)

2. Annual Meeting Speech--Draft
   (Memo from Mr. Shakow dated July 31, 1987)

3. Direct Bank Financing of NGOs
   (Memo from Mr. Hopper to Mr. Conable dated July 30, 1987)

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

# OFFICE MEMORANDUM

DATE: July 31, 1987

TO: Members of the Policy Committee

FROM: David Hopper, SVPPPR

EXTENSION: 75678

SUBJECT: Interim Report on the Debt Problems of the Middle-Income Countries

The Policy Committee, at its July 8 meeting, discussed the debt situation of the highly indebted countries and agreed to set up a Task Force to review the current economic situation in and outlook for these countries, and to assess the prospects of achieving growth with creditworthiness in these countries. The Policy Committee asked that the Task Force report its preliminary findings to the Committee by August 4. The interim report of the Task Force, chaired by Jean Baneth, is attached.

Att.

JUnderwood/kg

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

# OFFICE MEMORANDUM

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DATE July 31, 1987

TO Members of the Policy Committee

FROM Jean Baneth, IECDR

EXTENSION 33800

**STRICTLY CONFIDENTIAL**

SUBJECT Interim Report on Debt Problems of Middle-Income Countries

Following the Policy Committee discussion of July 8, a Task Force was constituted to deal with the issue. Participants in the Task Force meetings were:

Jean Baneth, Chairman, PPR
John Holsen, PPR
Fred Jasperson, PPR
Paul Meo, PPR
Jeff Katz, PPR
Vinod Dubey, EAS
Andrew Steer, Finance
Frank Lysy, Finance
David Goldberg, LEG
Anthony Toft, LEG
Antoine van Agtmael, IFC
David Bock, DFA

This is the interim report of the Task Force.

**EXECUTIVE SUMMARY**

The combination of domestic policy adjustments, increased World Bank lending, and debt rescheduling combined with concerted new money lending by commercial banks, which formed the core of the Baker initiative, is not succeeding in restoring growth to middle-income developing countries. This is depressing the value of the claims of their commercial creditors, and also putting at risk the World Bank's own claims. The Task Force is in broad agreement that the pursuit of this strategy involves high risks, and promises little visible payoff. The Bank should publicly state this view soon.

Debt relief is needed by many middle-income debtors. New calculations still point to amounts that are not radically different from those mentioned in the previous note. This implies that adequate relief could be granted by the commercial banks themselves, broadly within the limits of the provisions they have constituted. Direct public financing is not indispensable. Indirectly, the public would share in the losses through their tax implications (as it shared in the prior notional gains) and probably would have to participate in

the written-down loans, or otherwise comfort their value.

The Task Force has reached no agreement yet as to what the Bank should do: persist with the present strategy, combined with improved financial engineering activities, until political circumstances become more favorable to concerted debt relief; indirectly precipitate default to commercial banks, and debt relief agreements with them, by reducing its lending to countries which carry unduly heavy debt burdens; or directly take the lead in helping countries and their creditors reach workable debt relief agreements. Future work of the Task Force should concentrate on refining these options.

**The current strategy is not working well**

1. A consensus was reached that slow global economic growth has serious implications for the debt problem. On the assumption that global growth rates will remain markedly inferior to real interest rates in the medium run, there were strong a priori reasons to doubt the ability of a substantial number of middle income indebted countries to recover acceptable growth rates without some form of concessional debt relief. This is confirmed by the preliminary results of country by country analysis (Annex I) for at least five of the eight countries examined. Several other countries may not need concessional debt relief, but the current "concerted lending" mechanisms have not brought new money in sufficient amounts to allow them to resume adequate growth, and are not likely to do so in the future.

2. Annex I is a paper prepared in the Country Economics Department of PPR which evaluates the progress of the highly-indebted countries in resuming growth and restoring creditworthiness during the 1982-86 period. It concludes that despite substantial policy reform efforts by the debtor countries, the adjustment which has been achieved has been largely at the expense of growth. No significant growth of GDP per capita has occurred in these countries since 1980; per capita output remains about 10% below the 1980 level. While adjustment efforts have succeeded in reducing these countries' external deficits, there has been a deterioration in their creditworthiness. Tables on page 10 of the paper indicate that the ratios of debt to exports and debt to GNP, two meaningful indicators of creditworthiness, are worse now than in 1982 for 16 of the 17 highly-indebted countries. The paper explains why these countries' efforts to strengthen their creditworthiness and to resume growth have failed.

3. Prospects for a representative sample of eight highly indebted countries have been reviewed (Argentina, Bolivia, Brazil, Chile, Colombia, Nigeria, Philippines and Uruguay). Projections have been prepared based on relatively optimistic assumptions that economic policies in the highly-indebted countries continue to improve, that economic performance of these countries is strengthened and that the world economy is more supportive of their adjustment and recovery. In

each of the countries, economic recovery, defined as per capita growth of GDP between 2 percent and 3 percent, is assumed for 1988-95. It is also assumed that for each, external financing requirements are met.

4. The conclusion is that despite extremely optimistic assumptions about the quality of economic management in these countries, their prospects are bleak. Most will not be able to obtain the level of resources they will require to reestablish adequate rates of economic growth and they will not be successful in reducing their debt service burden to manageable levels. After almost 15 years of adjustment (1982-95), most will not have succeeded in strengthening their external positions sufficiently that they could be classified as even minimally good credit risks.

5. The paper presents estimates of the amount of additional financial relief which each would require in order simultaneously to resume an adequate rate of economic growth and reduce the debt service burden to manageable levels. The results vary by country (Colombia needs no relief; Bolivia needs the equivalent of 70 percent of its current outstanding debt). For the eight countries in the sample, total financial relief required is estimated at US$56 billion, equivalent to about 24 percent of their debt outstanding at the end of 1986. These numbers are not out of line with our earlier findings. They are broad estimates only. Their significance lies in showing that the relief required is not out of line with the provisions already provided by the Bank. In almost all the countries studied, current secondary market discounts are greater than the financial reflief indexes.

**Risks for the World Bank**

6. This diagnosis has serious implications for the World Bank. The debt overhang constitutes an obstacle to its mission, which is to promote development. Particularly in countries where it is heavily engaged in adjustment lending, the resources it provides and the policy improvements it promotes have in recent years served mainly to finance debt service to other creditors, not to further development. This point is clearly illustrated in the tables (Annex II) prepared by Finance for the recent creditworthiness review. By putting a large share of its loans into countries with severely impaired development prospects and debt servicing ability, financing debt service to other creditors, the Bank is also compromising the value of its portfolio, and ultimately its own creditworthiness. In the case of Nigeria, the Bank has recently undertaken a large lending program, under the assumption that private debtors will continue to withdraw funds.

7. The Bank has made large, fast-disbursing, loans to most highly indebted countries since 1982. These large disbursements helped assure continued debt service to the Bank, even when debt service to other creditors was slowed or suspended. Net transfers from the Bank to many of these countries will soon turn negative: i.e. they will owe more in debt service payments to the Bank than they receive in new

disbursements. The Bank's own claims on these countries will then face heightened risks, further enhanced by political considerations. Future governments will generally recognize the value of physical capital financed by the Bank in the past; they may not necessarily value equally the Bank's past help in financing debt service to commercial banks and in implementing policies which facilitated debt servicing. Consequently, they may feel less obligated to honor contractual debt service obligations. To deal with these problems, the Bank faces a number of possible alternatives.

**Alternative 1: Continue the Lending Program Unchanged**

8. The first alternative is to continue large net disbursements to these countries, without a commensurate inflow from other creditors. Without a much more massive capital increase than currently under consideration, the Bank alone cannot lend enough to restore growth even in those countries that, with enough resources, could grow out of their debt problems. This lack of growth puts the new loans, as well as old credits, at risk. In those cases where our analysis indicates that concessional debt relief is required, fast-disbursing Bank loans may prevent imminent default, but only at the cost of larger Bank losses when the eventual default occurs. Meanwhile, the Bank could place increased emphasis on addressing the debt problem at the margin on several fronts, using a menu of financial engineering techniques. It could encourage wider participation in the secondary market, which is currently thin. Together with the IFC, it could increase its encouragement of debt/equity swaps and of new forms of direct and equity investment. It would work to improve the acceptability and marketability of exit bonds, and attempt to enforce the concept of burden-sharing among creditors.

9. The short-term political risk of this approach is low. The danger is the possiblity of seriously eroding the quality of the Bank's portfolio, if these actions are not adequate to restore growth and ultimately creditworthiness in the highly indebted countries. This danger is heightened by the distinct possibility that, were we to continue along this course, another agency or a government--creditor or debtor--would seize the initiative and lead us into positions with undesirable implications for our finances.

**Alternative 2: Limiting Bank Exposure**

10. The Bank could severely limit or even cease new lending to the more risky of these countries in order to limit its losses. This would not sit well with its role as a development institution. Moreover, a sharp reduction in lending would not merely limit losses, but it would also precipitate them, as it would accelerate the transition to negative net transfers from the Bank, and by also inducing other creditors and potential investors to pull back. Data from Finance show that many of the major highly indebted countries are already in a negative net transfer position vis a vis the Bank, and most of the rest are likely to

be in this position by FY1990.

**Alternative 3: Requiring a Restoration of Creditworthiness**

11. Another set of alternatives is open to the Bank if it opts to continue to do business in the highly indebted countries. The Bank is supposed to lend only to further development, and only to creditworthy countries. It could inform borrowing countries and other crditors that the countries need to restore growth prospects and creditworthiness in order to be eligible for further IBRD loans.

12. The Bank would, therefore, require that the country seek adequate debt relief through a negotiated agreement with its creditors. The Bank could provide direct support for this process. Its policy (under this alternative) to lend only to countries which do not carry an excessive debt service burden would indirectly encourage creditors to reach agreement: the real value of reduced claims on a country intensively supported by the Bank would be larger than the real value of the original claims on a country with low growth prospects and receiving limited support from the Bank.

13. The Bank could also take the lead in designing a framework for negotiations between creditors and debtors. This framework would need to be flexible enough to allow simple rollover with minimal provision of new money, (the Baker Plan), where this is adequate, but also allow the incorporation of some forms of concessional debt relief where that is essential to achieve growth and creditworthiness. In formulating a framework, the Bank could draw on a number of proposals that have been put forward.

14. In the event a negotiated agreement proves impossible, or that the negotiated agreement is judged by the Bank to be insufficient to restore solvency, the Bank would maintain its support to countries forced to suspend a portion of their debt service payments to others. Provided the country is following good domestic policies, the country has no other alternative, and the Bank recognizes this.

15. This alternative would involve continued lending by the Bank to countries in default to other creditors. Indeed, it involves increased lending to such countries, and therefore, at least by implication, an encouragement to default. Obviously, such a course could only be pursued with the agreement of major shareholders. Current Bank policy, enunciated in the OMS (Section 1.28, paragraph 9), allows the Bank to commit and disburse funds to countries that, while in default, do not deny their liability but suffer from a shortage of foreign exchange, as long as the Bank's own assessment indicates that the country will be able to repay the Bank.

16. Any negotiating framework endorsed by the Bank should contain the following elements:

The resolution of private claims must not require the direct use of public funds that would be seen as bailing out the commercial banks. (The use of public funds in this manner by governments that wished to support their banks would not be precluded, of course.) Indirect use of public funds, including World Bank lending, guarantees, and other forms of support enhanced by the GCI, will have a role to play in boosting the development prospects of the debtor countries, and in providing comfort to the written-down loans. It is to be noted that the most recent calculations (like those earlier communicated to the Policy Committee) provide no support to the argument that debt relief needs exceed the financial capacity of commercial banks.

The yardstick for debt relief must be the long-term viability of the debtor country's economy. This should be judged by an outside observer. The World Bank is the logical candidate.

The framework adopted must facilitate timely agreements between creditors and the debtor country. The current negotiation process is too prolonged and gives too much power to individual creditors, and too much possibility for free riders.

**Related issues**

17. If the Bank becomes involved with debt relief schemes, either as a leader or a follower, it is likely to be called upon to provide some form of "comfort" for the creditors involved. The comfort requested may take a variety of forms, including guarantees, new cross default clauses, or a subordination of Bank debt service payments to those on the new claims of the creditors that have provided forgiveness. It may also be asked to finance a portion of the program, as in the case of debt buy-back schemes.

18. Another issue for the Bank is its own position as a preferred creditor. Other creditors have not objected strenuously to the Bank's exemption from rescheduling agreements. Would they be as willing to allow the Bank to stay out of schemes that required some form of rescheduling and forgiveness? The Bank will need a clear understanding with its shareholders on these issues.

19. The claims of official bilateral creditors may also be affected. These claims are a relatively small share of the total liabilities of the highly indebted countries but a relatively large share of the claims and contingent claims of the official export credit agencies. To date, the concept of equal treatment of all non-preferred creditors, a cornerstone of the Paris Club framework, has been generally observed. Would equal treatment require concessional debt relief by bilateral creditors in those cases where a restoration of growth with creditworthiness implies concessional relief by commercial banks? Official export credit agencies (the major bilateral creditors in the

highly indebted countries) may be less prepared for this eventuality than are the commercial banks. This issue must be explored with the member governments affected.

**Next steps**

20. There is no consensus within the Task Force as to what the Bank should do. In view of the highly political nature of the debt problem, some participants felt that the Bank should not take any new initiative, because industrial country governments would not be willing to support one yet. The situation would have to deteriorate into a major political crisis before any program could be put forward. This implied the need for continuing on broadly the present course, while recognizing its risks and possibly working behind the scenes to bring about the political conditions which would allow a new course to be adopted later.

21. Others thought that there are at least three reasons why a standback posture is not desirable. First, the Bank's own finances might be severely impaired if it continued with the present strategy, while the economic condition of many debtor countries continued to deteriorate and other creditors pulled back. Second, another agency (or country) might take the lead, essentially imposing on the Bank a posture that could have serious implications for Bank finances. Third, the Bank's leadership role in development finance could be threatened if it stands back from the debt problem. The Bank's past high-profile endorsement of the Baker initiative now makes it necessary, at least, to indicate publicly what results have been achieved and what more can be expected to be achieved from now on.

22. These considerations have led some of the Task Force participants to feel that the Bank itself take the lead, possibly through some variant of the many schemes which have been put forward, inside the Bank and outside. (The Task Force considered a framework that would build on commercial bank writedowns by converting these to forgiveness, where necessary, through private financial intermediaries, controlled by the commercial creditors. These intermediaries, one for each country, would renegotiate debt servicing arrangements with the debtor country. The majority of the Task Force participants felt that the scheme, as currently set out, was impractical, mainly because it offered inadequate protection against free riders.)

23. Still others thought that the only realistic alternative was a major publicly financed debt relief effort, in which the Bank itself would likely have to participate.

24. The Task Force will pursue its work in two directions: the analysis of country cases will be extended to countries not yet covered, and firmed up for all countries, in consultation with the concerned country economists. It will also continue to work on the possible modalities of the debt relief schemes most appropriate for middle income countries, and on the role the Bank should play relative to such

schemes.

25. If the Task Force is to pursue its work efficiently and diligently, working arrangements will have to be modified somewhat. A small working group needs to be constituted, and staff from the various SVP units attached to it full time in a separate office. Only in this way can we explore the many legal modalities of possible options, enquire systematically into the views of commercial creditors and bank regulators, and undertake the necessary detailed economic analyses. Intensive cooperation from relevant operational staff would also be needed. The Task Force would still supervise and direct the Working Group, subject to instructions from the Policy Committee.

## Burden Sharing Implicit in Recent Strategy Papers: Shares of Net External Finance Proposed

| | % Shares | |
|---|---|---|
| | 1987-90 | 1987-95 |
| Nigeria (CSP, May 27, 1987) | | |
| IBRD | 61.1 | 98.2 |
| Commercial | -29.4 | -67.9 |
| IMF | 0 | 0 |
| Other | 68.3 | 69.7 |
| Chile (SAL III IM, June 29, 1987) | | |
| IBRD | 56.8 | |
| Commercial (incl. Debt. Conversion) | 45.9 | |
| IMF | -96.2 | |
| Other | 93.5 | |
| Uruguay (CPP, June 30, 1986) | | |
| IBRD | 81.8 | 27.4 |
| Commercial | 55.3 | 34.1 |
| IMF | -165.9 | -61.1 |
| Other | 128.8 | 99.6 |
| Colombia (Baker Paper, May 14, 1986) | | |
| IBRD | 21.6 | 17.4 |
| Commercial | 52.5 | 67.0 |
| IMF | 0 | 0 |
| Other | 25.9 | 15.6 |
| Turkey (CASB, Jan. 9, 1987) | | |
| IBRD | 50.6 | |
| Commercial | 49.9 | |
| IMF | -14.7 | |
| Other | 14.2 | |
| Philippines (Memo for ERL, Dec. 22, 1986) | | |
| IBRD | 42.4 | |
| Commercial | -11.2 | |
| IMF | -27.1 | |
| Other | 95.9 | |

| | % Shares | |
|---|---|---|
| | 1987-90 | 1987-95 |
| Brazil (DCB, Feb. 6, 1987) | | |
| IBRD | 33.4 | |
| Commercial | 71.5 | |
| IMF | -23.0 | |
| Other | 18.0 | |
| Argentina (DCB, March, 1987) | | |
| IBRD | 44.9 | |
| Commercial | 30.8 | |
| IMF | -0.2 | |
| Other | 24.5 | |

Note: These implicit burden sharing figures must be taken as only rough indications. They are derived from a variety of Regional strategy papers and other documents; they may be based on differing definitions for creditor categories and concepts for total debt (we tried to use the broadest definition possible, i.e., including short-term and private non-guaranteed debt where possible); and sometimes use different base periods (hence different relative exchange rates).

Note also that not all of the lending levels proposed were approved by Senior Management.

FRSRM
20Jul87

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ANNEX 1

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# DEBT Problems of Middle Income Countries: **REAPPRAISAL II** - The Country Perspective

Country Economics Department
July 31, 1987

Final

SUMMARY AND CONCLUSION

i Annex I is a paper prepared in the Country Economics Department of PPR which evaluates the progress of the highly-indebted countries in resuming growth and restoring creditworthiness during the 1982-86 period. It concludes that despite substantial policy reform efforts by the debtor countries, the adjustment which has been achieved has been largely at the expense of growth. No significant growth of GDP per capita has occurred in these countries since 1980; per capita output remains about 10% below the 1980 level. While adjustment efforts have succeeded in reducing these countries' external deficits, there has been a deterioration in their creditworthiness. The tables on page 10 of the paper indicates that the ratios of debt to exports and debt to GNP, two generally meaningful accurate indicators of creditworthiness, are worse now than in 1982 for 16 of the 17 highly-indebted countries. The paper explains why these countries' efforts to strengthen their creditworthiness and to resume growth has failed.

ii Prospects for a representative sample of highly indebted countries have been reviewed for eight countries (Argentina, Bolivia, Brazil, Chile, Colombia, Nigeria, Philippines and Uruguay). While the most plausible assumption that can be made about the future prospects for these countries is that trends of the past five years will continue for the foreseeable future, such projections have not been prepared since the results are clear.[1/] Instead, projections have been prepared based on more optimistic assumptions that economic policies in the highly-indebted countries continue to improve, that economic performance of these countries is strengthened and that the world economy is more supportive of their adjustment and recovery. In each of the countries, economic recovery, defined as per capita growth of GDP between 2 percent and 3 percent, is assumed for 1988-95. It is also assumed that for each, external financing requirements are met.

iii The conclusion is that despite extremely optimistic assumptions about the quality of economic management in these countries, their prospects are bleak. Most will not be able to obtain the level of resources they will require to reestablish adequate rates of economic growth and they will not be successful in reducing their debt service burden to manageable levels. After almost 15 years of adjustment (1982-95), they will not have succeeded in strengthening their external positions sufficiently that they could be classified as even minimally good credit risks.

iv Given the poor prospects for these countries to obtain the level of external resources which they will require, and their inability to make meaningful progress toward restoring even a minimum semblance of creditworthiness, the paper presents estimates of the amount of additional financial relief which each would require in order simultaneously to resume an

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1/ Given the consensus forecast for further slowdown of the world economy, it is entirely possible that the outcome will be even worse than is indicated by extrapolation of the 1982-86 historic trend.

adequate rate of economic growth and reduce the debt service burden to manageable levels.[1] The results vary by country (Colombia needs no relief;Bolivia needs the equivalent of 70% of its debt outstanding at the end of 1986). For the eight countries in the sample, total financial relief required is estimated at US$56 billion, equivalent to about 24 percent of their debt outstanding at the end of 1986. Assuming that the situation of these countries is representative of that faced by the other highly-indebted countries, the entire group of seventeen would require about US$100 billion of financial relief.

v As a rough check on the paper's estimates of financial relief, they are compared to secondary market discounts on external debt. In almost all cases, these discounts are greater than the financial relief indexes. This is a reflection, among other things, of the extremely optimistic assumptions contained in the country projections regarding economic management. Comparisons between estimates of required financial relief and secondary market discounts are tenuous, as secondary markets are thin and notoriously unstable. However, the existence of such discounts validates the finding of the paper that for most of the highly-indebted countries, indexes of financial relief have a positive value.

vi Based on these countries' progress toward strengthening their external position, their prospects for obtaining an adequate level of external resources and the financial relief requirements, three groups can be identified. The first group (countries like Colombia) should be able to sustain an adequate rate of economic growth while simultaneously reducing their external debt service burden to reasonable limits. But this will require resource mobilization efforts on these countries' behalf by the official financial institutions.

vii The second group of countries (e.g., Argentina, Brazil, Chile and the Philippines) will require significant increases in external resources. If their recovery is not to be sacrificed they will require moderate financial relief to limit their debt service burden. Such relief could be provided in many alternative ways (e.g., secondary market buy-back of outstanding debt, etc.).

viii There is a third group of countries (e.g., Bolivia) which will require significantly larger increases of financial relief. They will require solutions which substantially reduce their external debt.

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1/ Financial Relief is defined as the present discounted value of relief (grant equivalent) required to ensure adequate growth (annual GDP growth of about 2.5 percent per capita) while allowing the country to end the projection period with a manageable external debt burden, defined as a maximum 20 percent interest service ratio.

## I. Introduction

1. Since 1982 the highly-indebted developing countries have been engaged in a far-reaching adjustment process. The objectives have been to restore creditworthiness and to reestablish adequate rates of economic growth. Results have varied from country to country. But for the highly-indebted countries as a group these objectives have not been achieved. An adequate and sustainable rate of economic growth has not been reestablished. Lack of progress in restoring creditworthiness indicates that five years after the initial crisis the process is far from complete and the outcome uncertain. Events in a number of these countries during the past year demonstrate the vulnerability of the adjustment process to adverse developments in the world economy and to disruptive domestic social and political forces. Because the sustainability of the adjustment process over the medium term is dependent upon resumption of growth, the necessity of accelerating recovery in the debtor countries could not be more compelling.

2. Previous studies, both within and outside the Bank, have indicated that with continued strong growth in the industrial countries, sustained adjustment efforts in the debtor countries would be rewarded with resumption of growth and a return to creditworthiness. However, these optimistic studies have concluded that even in the best of circumstances the process would be difficult and progress slow. Given the consensus forecast of a slowdown in growth of the world economy for the foreseeable future and the prospect of continued depressed prices for most of the debtor countries'

exports, accelerated retrenchment of commercial banks and the likely increase of social and political constraints which disrupt the adjustment process in debtor countries, it is likely that the economic position of these countries will continue to deteriorate. Action to prevent this from occurring is urgently needed.

3. It is not the purpose of this paper to design such an action plan. Its more limited objective is to review developments in the highly-indebted countries since 1982 to determine whether progress is being made and if not what went wrong. The paper then examines the adjustment and growth prospects of a representative sample of these countries. It concludes (pp. 46-54) by estimating what these countries will require by way of external resources andfinancial relief if they are to reestablish creditworthiness and at the same time sustain adequate rates of economic growth.

## II - Growth and Adjustment in the Highly-Indebted Countries (1982-86)

### A. Background

4. Beginning in 1979 when the industrial countries entered what was to become the longest recession since the 1930s, the highly-indebted countries 1/ have experienced a severe economic contraction and financial

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1/ Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Cote d'Ivoire, Ecuador, Jamaica, Mexico, Morocco, Nigeria, Peru, Philippines, Uruguay, Venezuela and Yugoslavia.

crisis. During the preceding decade most of these countries had been relatively successful in diversifying their economies through accelerated expansion of their industrial and agricultural sectors. Most of them were increasingly able to penetrate international markets. As a group they achieved high rates of growth of their manufactured exports (over 10% annually in real terms). Economic growth was rapid; GDP increased in real terms by about 6 percent annually. Significant gains were made in levels of nutrition, education, housing and health services. The incidence of acute poverty in most of these countries was significantly reduced.

5. As the economies of the highly-indebted countries expanded and their prospects for higher rates of return on investment were enhanced, their access to world capital markets increased. Given the buoyancy of their export earnings, high levels of liquidity in international capital markets, and the negative real interest rates which prevailed, many of these countries increased their external debt at unsustainably high rates. Many borrowed to increase consumption. Others misallocated the proceeds to politically popular projects with little economic value. Many avoided politically unpopular reforms which would have made their economies more efficient and resilient to adverse developments in the world economy. Beginning in 1979, the combination of a severe contraction of these countries' export markets, collapse of world commodity prices and sharp increases in real interest rates (to over 20 percent annually) which persisted through 1982, placed enormous financial pressure on these countries. This culminated in a generalized debt crisis in the summer of 1982, as commercial banks became increasingly concerned about their exposure in these countries and sharply reduced their lending.

6. When the crisis erupted in 1982 it became apparent that the highly-indebted countries could no longer delay difficult policy reforms and would have to adjust their economies in order to restore their liquidity. This adjustment has been undertaken in an adverse external environment. From 1981 to 1985 real interest rates were at the highest level in 50 years, and although nominal rates have declined since that time, they remain high in real terms. While there has been a resumption of growth in the industrial countries, albeit at a diminishing rate, prices of the highly-indebted countries' exports have failed to recover and in real terms remain at the lowest level since the beginning of the century. Since 1984 commercial banks in the U.S. have reduced their exposure in these countries by 10 percent.

B. Adjustment in the Highly-Indebted Countries

7. There have been three phases of the adjustment process in the highly-indebted countries. The first (Recession: 1982-83) resulted in forced massive reductions in their current account external deficit from 6 percent of their combined GDP (US$53 billion) in 1982 to 2% (US$15 billion) in 1983. This was the direct result of lack of external financing and a shift in their trade balance from a deficit of US$14 billion to a surplus of US$19 billion. This in turn was achieved by a sharp cut (25 percent) in imports resulting from tight fiscal and monetary policies aimed at reducing expenditures. Investment was hit hardest. In 1983 output per capita was about 10% below the 1980 level.

8. The second phase (Export Expansion: 1984) resulted in the virtual elimination of the highly-indebted countries' current account deficit as a

consequence of a massive (US$36 billion) surplus in the trade balance. In contrast with the 1982-83 period, this was achieved primarily through a 10 percent increase of export earnings. It occurred in response to the recovery in the industrial countries, a widening of the U.S. trade deficit, and to strengthened export incentives in the debtor countries. Most of the highly-indebted countries eased import restrictions during this period. Expansion of exports together with greater access to imported inputs and capital goods stopped the downward trend in output; nevertheless, GDP per capita showed no significant increase.

9. During phase three (Decline of Export Earnings: 1985-86) there was a deterioration in the creditworthiness of the highly-indebted countries. It is unclear how long this phase will last but given the expected weakening of growth in the industrial countries, it is likely to continue for the foreseeable future. Declining growth in industrial countries in 1985 and 1986 resulted in further weakening of world markets for the highly-indebted countries' major exports. The oil-exporting highly-indebted countries experienced the greatest deterioration; their export earnings fell by a cumulative 30 percent in 1985-86 as a result of a decline in oil prices. The export earnings of the other highly-indebted countries declined slightly despite a 5 percent volume increase. For the highly-indebted countries as a group there was a 50 percent drop in their trade balance to US$18 billion. Despite the decline in world interest rates which occurred in 1986, the overall current account deficit for these countries increased for the first time since 1982 to US$12 billion. These developments led to further deterioration in creditworthiness. The ratio of debt to exports rose from 246 percent in 1985 to 266 percent in 1986; the debt service to exports ratio

rose from 37 percent to 40 percent. Excluding Brazil and Peru, which experienced high rates of growth as a consequence of unsustainable, expansionary policies, the highly-indebted countries' GDP per capita again failed to show any significant increase in 1985-86.

10. Have the highly-indebted countries sustained strong adjustment efforts during the 1982-86 period? The record is mixed. Major policy reforms have been initiated by almost all of the 17 highly-indebted countries. In most, demand has been reduced by a combination of fiscal, monetary and incomes policies. Public sector investment expenditures have been cut and in a number of cases funds have been reallocated to projects which better serve adjustment objectives. Controls on interest rates have been eased in many countries in order to reduce consumption and stimulate savings. Real wages have been restrained to reduce domestic demand and encourage employment growth. Most countries have used commercial policy to cut imports and expand exports. Currencies have been devalued in real terms by almost all of them; the largest increases (over 50 percent) have been achieved by Argentina, Chile, Colombia, Ecuador, Mexico and Uruguay.

11. Because of the greatly increased foreign exchange constraint which they currently face, investment has not recovered and most countries have been slow to undertake more comprehensive trade and longer term policy reforms aimed at improving resource allocation and increasing efficiency. Similarly, implementation of institutional reforms such as overhaul of public enterprise systems, where political constraints appear to be more binding, have also lagged. Despite substantial cuts in public expenditures, commensurate improvements in fiscal deficits have not occurred in most

countries in part because of an erosion of the tax base as economies have contracted. In some countries fiscal deficits increased as a consequence of recession; in others because of failure to control public enterprise deficits.

12. On balance, the policy reform efforts of the highly-indebted countries, while not uniformly successful, have been substantial. Governments have generally acted with resolve to undertake the required policy reforms despite the high political cost of such action. In a few, adjustment weariness has set in and this resolve has eroded. In a number of cases expenditures on nutrition, health and education have been sacrificed. The experience suggests that some reforms (e.g., tax reform) require an expanding economy if they are to be successful. Other reforms (e.g., liberalization of trade regimes) require an adequate level of external resources over the medium term in order to be initiated. Still other reforms (e.g., freeing of interest rates) may have effects which are inimical to growth when carried out by countries that are simultaneously attempting to allocate a substantial portion of their resources to service external debt, as discussed below.

13. The main conclusion to be drawn from the 1982-86 experience is that thus far adjustment has largely been achieved at the expense of growth. Per capita output of the highly-indebted countries is now about 10 percent lower than in 1980. Declines in income per capita have been more acute (30 percent) because of the deterioration of these countries' terms of trade. Education, health and nutrition services have been reduced and gains which occurred in the 1970s are threatened with erosion. The outcome

suggests that the adjustment process has been inefficient, having not only lowered domestic absorption (which was essential) but also and unnecessarily cutting output.

14. A second major conclusion is that the adjustment process is exceedingly fragile and its effectiveness is vulnerable to adverse developments in the world economy. A study of prospects for a group of highly indebted countries submitted to the Board (SEC 4-346) in 1984 noted:

> "Projections carried out in this study indicate that with strong sustained growth in OECD and assuming that the largest, most heavily indebted countries pursue good economic and financial policies, these countries could reestablish a minimally adequate rate of growth by the late 1980s, strengthen their external positions and improve their creditworthiness. But even with these relatively optimistic assumptions, recovery would be painfully slow. For many countries, growth in the range of 5 to 6 percent would not be reestablished until the end of the decade. Currently high rates of unemployment/underemployment would not be reduced until the end of the decade.
>
> This base case is the best outcome that is considered plausible at this time. It assumes both strong sustained OECD recovery (the result of good policies in these countries) and outstanding economic management in the debtor countries. However, it is unlikely that the base case will actually be achieved. Policies will probably not be continuously outstanding across the board in most countries, even though policies could be better than in the recent past. But even with outstanding economic management, social and political constraints will make it difficult for economic managers to consistently achieve their objectives.
>
> The results of the projections for the most heavily indebted countries are very sensitive to changes in assumptions about the world economy. With lower growth of the world economy and of the heavily indebted countries, unemployment would continue to rise in these countries, per capita income would show little recovery and the level of per capita consumption would stagnate through the rest of the decade. In some countries, both per capita income and consumption would decline further up to 1990. For most of the heavily indebted countries, this low case would mean reduced capacity to import, to invest and to reestablish adequate rates of economic growth. With slower recovery of domestic economies and with the growing resource transfers abroad requiring an even greater sacrifice on the part of their population, stabilization and adjustment programs currently being implemented in these countries would likely be increasingly difficult to sustain."

15. The events of 1985-86 support this conclusion. The highly-indebted countries have thus far failed to reestablish adequate rates of economic growth. Recovery has not occurred. There have been no significant increases in GDP per capita since 1980. At the same time, the highly-indebted countries have experienced serious setbacks in their efforts to strengthen their external position and restore creditworthiness. Indicators of creditworthiness were worse at the end of the period than at the beginning (see Table 1).

Table 1: Creditworthiness of Highly-Indebted Countries

| | Long Term Debt as % of Exports (G&S) | | Long Term Debt as % of GNP | |
|---|---|---|---|---|
| | 1982 | 1986 | 1982 | 1986 |
| Argentina | 269.8 | 465.4 | 51.9 | 57.3 |
| Bolivia | 315.5 | 484.6 a/ | 103.4 | 133.3 a/ |
| Brazil | 312.3 | 379.6 | 27.3 | 38.3 |
| Chile | 271.7 | 347.0 | 62.3 | 120.1 |
| Colombia | 135.6 | 198.1 | 18.8 | 41.9 |
| Costa Rica | 246.9 | 312.8 a/ | 129.7 | 113.6 a/ |
| Cote d'Ivoire | 224.7 | 205.0 | 89.1 | 85.7 |
| Ecuador | 201.7 | 273.3 | 47.9 | 66.7 |
| Jamaica | 157.9 | 236.0 | 78.0 | 156.9 |
| Mexico | 215.9 | 379.3 | 38.5 | 74.3 |
| Morocco | 318.5 | 399.7 | 65.6 | 105.2 |
| Nigeria | 77.1 | 297.6 | 13.0 | 42.6 |
| Peru | 205.6 | 364.5 | 34.8 | 50.5 |
| Philippines | 151.9 | 251.6 | 31.0 | 73.3 |
| Uruguay | 113.1 | 207.0 a/ | 21.0 | 58.4 a/ |
| Venezuela | 85.1 | 296.6 | 25.8 | 74.6 |
| Yugoslavia | 106.3 | 107.3 | 25.9 | 28.9 |

Note: These two indicators are the most reliable indicators of creditworthiness since others such as the debt service and interest service ratios show what is actually paid rather than what is owed. For example, a debt service to export ratio may show an improvement (i.e., a decline) when in fact the country has merely stopped servicing its debt, as in the case of Peru.

a/ 1985.

Source: International Economics Department.

16. The deterioration of creditworthiness is one partial explanation why banks have been reluctant to increase their exposure in the highly-indebted countries. The increase in the debt service burden explains in part why there has been a sharp increase in the number of highly-indebted countries which are currently not making interest payments on their external debt (currently 8 of the highly-indebted countries are not making interest payments, up from 3 in 1985).

C. Failure to Achieve Adjustment with Growth

17. In order to simultaneously adjust and strengthen its external position and expand output a country must: (a) reduce domestic absorption (expenditure); (b) switch domestic expenditures away from tradable goods; and (c) expand production of tradable goods (structural transformation). Item (a) reduces growth. Items (b) and (c) increase growth. If (b) and (c) are greater than (a), the net effect will be that growth occurs at the same time that the country's external position improves. There are a number of reasons why the highly-indebted countries have not been able to achieve this during 1982-86.

(i) Insufficient Investment. The highly-indebted countries have been forced to rely unduly on expenditure reduction (item (a) above). This is because structural transformation (item c) requires investment. In most of the highly-indebted countries investment has been cut sharply because of inadequate resources. In the absence of foreign

savings, the pace of structural transformation has been significantly reduced by declining national savings with which to finance investment.

(ii) Social and Political Constraints. In some countries, social and political forces disrupted adjustment management, resulting in short-sighted policy decisions which have neutralized or in some cases reversed adjustment efforts. Collapse of the Cruzado Plan in Brazil, brought about by misconceived incomes and price policies, illustrates the speed in which progress toward adjustment and growth objectives can be dissipated. The fact that such inappropriate policies continued unchecked for a prolonged period was the consequence of conflictive forces within the Brazilian political process which made policy makers unwilling or unable to correct their mistakes. Similar examples, albeit on a smaller scale, can be found in most of the heavily-indebted countries. In some, a continuing anti-export bias reflects deeply entrenched economic and political interests which have been successful in blocking trade policy reform.

(iii) Distortionary Effects of Domestic Financial Transfers. Adequate growth has not been reestablished in the highly-indebted countries in part because of the massive domestic financial transfers from the private to the public sector which are required to service external debt. Debt servicing

demands have pushed real interest rates in many of these countries to extraordinarily high levels incompatible with resumption of private investment and growth. With disposable income declining, real interest rates have had to be correspondingly higher to mobilize a given level of savings from the private sector. In addition, most countries have had to maintain extremely high real rates of interest while they were devaluing their currencies in real terms in order to prevent capital flight.

(iv) Adverse External Environment. The external environment which these countries have faced during 1982-86 has on balance not been supportive of their adjustment efforts. The slowdown of industrial country growth and prolonged weakness of commodity markets have resulted in deterioration of these countries' terms of trade. Persistence of high interest rates in real terms and destabilizing (i.e., pro-cyclical) contraction of external sources of finance, have adversely affected the highly-indebted countries. Adjustment management itself has been made more difficult by the instability and unpredictability of world economic trends. To the extent that external forces are not supportive of the adjustment process and operate to increase the lag between introduction of adjustment measures and their positive results, there is greater likelihood that resolve to sustain such reforms will be dissipated.

## III - Prospects for the Highly-Indebted Countries

18. The most plausible assumption that can be made about the future prospects for the highly-indebted countries at this time is that the trends of the past five years will continue for the foreseeable future. Should this occur, the highly-indebted countries will not have recovered from the sharp declines in per capita output which they experienced in the early 1980s. Development gains which occurred in these countries in the 1960s and 1970s would be further eroded. Their creditworthiness will deteriorate further. These countries' major creditors (including the World Bank) would experience further declines in the value of their portfolios in these countries. Substantial additional provisioning would need to be undertaken by creditors. Given the consensus forecast for further slowdown of the world economy, it is entirely possible that the outcome will be even worse than is indicated by extrapolation of the 1982-86 historic trend.

19. To explore the prospects for individual highly-indebted countries, projections for a representative sample have been prepared for each of eight countries (Argentina, Bolivia, Brazil, Chile, Colombia, Nigeria, Philippines, and Uruguay). While the most plausible assumption that can be made for these countries is that the next five years will bring a repetition of what occurred in these countries during 1982-86, such projections have not been prepared since the results are clear. Instead, projections have been prepared based on more optimistic assumptions that economic policies in the highly-indebted countries continue to improve, that economic performance of these countries is strengthened and that the world economy is more supportive

of their ajustment and recovery. In each of the countries, economic recovery, defined as per capita growth of GDP between 2 percent and 3 percent, is assumed for 1988-95.

20. Policy parameters are assumed to show gradual but significant improvement from what was achieved in the 1982-86 period. It is further assumed that for each, the external financing requirements are met. For most countries, substantial additional resources beyond what they were able to borrow during 1982-86 would be required; these are assumed to be provided. The objective of the exercise is to estimate for each country the external resources which are required for growth to be sustained at an adequate rate. Conclusions are then drawn regarding the amount of financial relief each of these countries would require in order to bring their debt service burden to a manageable level.

COLOMBIA

Prospects

Key Assumptions:

21. The resumption of growth which took place in 1986 is assumed to continue throughout the projection period 1988-95. GDP is assumed to grow between 4 and 4.5 percent in real terms to 1995. This rate of growth would be sufficient to absorb expected new entrants to the labor force and would result in 2.5 percent growth of per capita GDP. The recovery occurs in response to continued improvement in domestic economic management. 2/ It is the result of improved productivity of investment and a greater investment effort. The share of investment in GDP averages about 22 percent during 1988-95. Domestic savings is maintained at a relatively high but manageable level (from 21 percent in 1981 domestic savings to GDP rises to between 22 percent and 23 percent up to 1995). Average real export growth (5 percent annually) is outpaced by import growth (6 percent annually). Modest improvement in the country's terms of trade from the low 1987 level is assumed.

Base Case Results:

22. The assumed modest improvement in terms of trade makes it possible to gradually eliminate the deficit in the resource balance despite more rapid growth of imports than that of exports. Surplus in the resource balance averages 0.5 percent of GDP from 1991-95. Interest payments on the country's

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2/ Adjustment policy improvements are assumed in the following areas: real exchange rate policy; trade reforms including a gradual reduction of import controls over time; reductions in the public sector deficit; improved ordering of public investment priorities, and reduction in the public sector's access to domestic credit.

external debt absorb a significant but declining level of resources (from 4.3 percent of GDP in 1988 to 3.3 percent in 1995). As a consequence, Colombia continues to be a modest (but declining) capital importer to 1995. The current account deficit of the balance of payments falls from 3 percent of GDP in 1988 to 1.4 percent in 1995. As a consequence of reduced net capital inflows, Colombia makes moderate net financial transfers to its creditors throughout the projection period.

23. As a result of restrained moderate growth of export earnings and reduced borrowing requirements, Colombia's creditworthiness indicators improve starting in 1990. After peaking in 1989 at 48 percent, the debt service ratio declines to 33 percent in 1995. The stock of external debt to GDP and to exports declines from 45 percent in 1985 to 31 percent in 1995 and from 223 percent to 151 percent, respectively. The interest payments coverage ratio becomes positive in 1990 as the trade balance shifts into surplus. As this occurs, commercial banks are expected to resume small amounts of net disbursements.

24. Commercial bank lending to Colombia is expected to continue throughout the projection period as the result of the country's avoidance of liquidity problems. However, because of the liquidity problems and reschedulings of major countries in the Latin American region, commercial bank lending to Colombia is likely to be constrained. The country's capacity to reestablish growth, to raise the share of investment financed out of national savings, and to simultaneously strengthen its external position, is a reflection of its low external debt overhang relative to the other highly-indebted countries, and indicates its considerable potential to achieve self-sustained growth through good domestic economic management.

25. Because Colombia is assumed to be able to sustain moderate increases in the investment and savings efforts and to obtain moderate amounts of external resources, it is able to resume adequate rates of economic growth. As a consequence, growth of per capita income and consumption are maintained at a relatively favorable rate after 1988.

Sensitivity of Results:

26. The results for Colombia are most sensitive to assumptions about the quality of domestic economic management. The results depend heavily on increasing the productivity of investment and raising domestic savings and investment by moderate amounts. Equally important is the assumption about growth of export earnings. Large improvements are not necessary; merely sustained, reasonably good performance.

27. The results are quite sensitive to the price of coffee which is assumed and the growth of non-traditional agricultural and manufactured exports. Given the emergence of moderate petroleum exports the projections are sensitive, but to a lesser degree, to the assumed world petroleum price.

28. Given the low level of Colombia's external debt relative to that of the other highly-indebted countries, the results for Colombia are less sensitive to assumptions about international interest rates. They are less dependent on assumptions regarding the willingness of commercial banks to maintain a high level of positive net flows.

COLOMBIA

| | Historical Data | | | | | Estimated | | Projections | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 1980 | 1981 | 1982 | 1983 | 1984 | 1985 | 1986 | 1987 | 1988 | 1989 | 1990 | 1991 | 1992 | 1993 | 1994 | 1995 |
| | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== |
| Real GDP Growth (%) | 4.1 | 2.3 | 0.9 | 1.6 | 3.2 | 2.8 | 5.1 | 4.5 | 4.5 | 4.5 | 4.5 | 4.3 | 4.3 | 4.3 | 4.3 | 4.3 |
| Investment/GDP (%) | 19.1 | 20.6 | 20.5 | 19.9 | 18.7 | 18.5 | 18.3 | 18.1 | 22.0 | 22.3 | 22.1 | 22.0 | 22.3 | 22.8 | 22.8 | 23.2 |
| Domestic Savings/GDP (%) | 19.5 | 16.4 | 14.7 | 14.5 | 15.8 | 17.2 | 21.0 | 18.0 | 21.5 | 22.2 | 22.6 | 22.8 | 23.0 | 23.5 | 23.4 | 23.8 |
| Real Per Capita GNY Growth | 0.9 | -2.1 | -1.5 | -0.3 | 1.1 | 0.4 | 1.5 | -2.2 | 2.8 | 2.5 | 2.8 | 2.6 | 2.6 | 2.6 | 2.6 | 2.5 |
| Real Per Capita Consumption Growth | 1.9 | 1.6 | 1.6 | 0.0 | 0.9 | 0.3 | -1.4 | -0.4 | -1.7 | 1.7 | 2.5 | 2.6 | 2.6 | 2.2 | 2.9 | 2.3 |
| Import Volume Gnfs (% Change) | 19.5 | 8.1 | 16.1 | -8.9 | -2.8 | -2.6 | -4.6 | 11.1 | 13.3 | 0.7 | 3.8 | 4.3 | 6.7 | 6.8 | 6.8 | 6.8 |
| Export Volume Gnfs (% Change) | 14.9 | -9.9 | 2.1 | -11.9 | 11.8 | 6.9 | 26.7 | 22.1 | 6.6 | 3.7 | 4.8 | 4.3 | 4.2 | 4.4 | 4.8 | 5.0 |
| Resource Balance (% GDP) | 0.4 | -4.2 | -5.8 | -5.4 | -2.9 | -1.3 | 2.7 | -0.4 | -1.1 | -0.5 | 0.2 | 0.6 | 0.5 | 0.5 | 0.5 | 0.6 |
| Interest Payments (% GDP) _a/ | 2.1 | 2.0 | 2.8 | 2.5 | 2.5 | 3.6 | 3.9 | 4.1 | 4.3 | 4.3 | 4.2 | 4.1 | 3.9 | 3.7 | 3.5 | 3.3 |
| Current Acct. Bal. (% GDP) | 0.3 | -4.7 | -7.4 | -7.3 | -5.4 | -3.6 | 1.6 | -2.5 | -3.0 | -2.5 | -2.0 | -1.6 | -1.6 | -1.6 | -1.5 | -1.4 |
| Net Long-term loans (% GDP) | 2.4 | 3.9 | 3.2 | 2.7 | 3.6 | 3.7 | 5.1 | 1.4 | 1.7 | 1.1 | 0.8 | 0.8 | 0.5 | 0.5 | 0.6 | 0.6 |
| o. w. Official | 0.8 | 0.8 | 1.0 | 1.4 | 1.7 | 2.7 | 2.0 | 2.1 | 1.7 | 1.1 | 0.4 | 0.3 | 0.1 | -0.2 | -0.3 | -0.2 |
| o. w. Financial Markets | 1.5 | 2.8 | 1.9 | 1.2 | 1.3 | 0.7 | 2.9 | -0.5 | -0.3 | -0.3 | 0.2 | -0.1 | 0.0 | 0.4 | 0.7 | 0.6 |
| Net Financial Transfers (% GDP) _a/ | 0.4 | 1.8 | 0.4 | 0.2 | 1.1 | 0.1 | 1.2 | -2.8 | -2.4 | -2.6 | -3.1 | -3.3 | -3.3 | -3.0 | -2.8 | -2.8 |
| Total External Debt (% GDP) | 20.8 | 23.9 | 26.4 | 29.5 | 32.4 | 40.9 | 44.8 | 45.5 | 44.6 | 42.8 | 41.0 | 38.9 | 36.8 | 34.9 | 33.1 | 31.3 |
| Total External Debt (% XGS) | 111.1 | 163.6 | 194.6 | 263.8 | 259.9 | 274.2 | 222.3 | 243.6 | 223.1 | 214.6 | 201.7 | 191.4 | 180.5 | 170.7 | 160.9 | 151.1 |
| Debt Service (% XGS) _a/ | 15.2 | 21.0 | 28.2 | 37.0 | 34.3 | 38.7 | 35.5 | 45.2 | 46.0 | 48.4 | 45.5 | 41.9 | 39.5 | 37.2 | 35.1 | 33.2 |
| Interest Service (% XGS) _a/ | 11.0 | 14.0 | 20.6 | 22.7 | 19.8 | 23.9 | 19.2 | 22.2 | 21.7 | 21.4 | 20.4 | 20.0 | 19.0 | 18.0 | 16.9 | 15.8 |
| Interest Payments Coverage (%) (Trade Surplus/Interest) | 21.8 | -206.2 | -207.8 | -210.7 | -118.6 | -36.9 | 69.5 | -10.6 | -26.0 | -11.7 | 5.4 | 14.4 | 13.6 | 13.5 | 15.1 | 17.3 |

Footnotes:

_a/For 1980-86 interest is what has actually been paid; for 1987-95 what is due. Includes interest paid on short-term debt.

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BRAZIL

Prospects

Key Assumptions:

29. Brazil is assumed to avoid a return to the contractionary adjustment experienced in the early 1980s. GDP growth of about 5 percent annually which is projected, is sufficient to achieve growth in per capita terms of 3 percent annually. The sustained recovery is made possible by policy-induced improvements which maintain the efficiency of investment, savings and investment performance above the historic average. Average real export growth outpaces import growth during the projection period by a small amount. Terms of trade began to improve gradually in 1988 but by 1995 are still below that of 1979.

Base Case Results:

30. As a result of a sustained large surplus in the resource balance (between 3.5 percent and 4 percent of GDP throughout the projection period) and declining interest payments as a share of GDP, there is a gradual decline in the current account deficit from 2.8 percent of GDP at the beginning of the period to 1.5 percent in 1995. This decline is made possible by the assumed more rapid growth of exports than of imports in current prices. Brazil remains a net capital importer throughout the projection period. Net financial transfers to its creditors remain roughly constant throughout the projection period at about 3 percent of GDP.

31. Creditworthiness indicators improve after 1987. The ratio of the debt outstanding and disbursed to GDP declines from 76 percent in 1987 to 58 percent in 1995. Debt to exports falls from 456 percent to 328 percent. The debt service ratio falls from 98 percent to 56 percent in 1995. While there are modest improvements in the interest coverage ratio, by 1995 Brazil is still unable to cover its interest payments with the surplus in its resource balance. Under these circumstances it is unlikely that Brazil would be able to return to voluntary lending. Despite the long-term gradual improvement in creditworthiness indicators, these remain excessively high through 1995. To deal with this Brazil would require reschedulings of amortization payments throughout the period and would probably experience continuing difficulty making interest payments. Capitalization of a portion of these payments would probably be necessary. Although this would help the country in the short-term, it would increase the rate of growth of the country's external debt.

32. As a result of continuing large interest payments abroad (between 5 percent and 6 percent of GDP) throughout the projection period, investment would be tightly constrained. It is likely that growth of output, income and comsumption would remain well below what was achieved in the 1960s and 1970s. Depressed levels of per capita output, consumption and employment growth would place additional pressure on a political situation which is already under considerable strain. The conclusion of an earlier document (sent to the Board in 1984) is still appropriate.

> "The coincidence of this [slower growth] with opening up of the political process in Brazil suggests the possibility of increased political instability in the 1980s. Should this occur, the range of possible outcomes including unilateral action on external debt is is difficult to predict."

Sensitivity of Results:

33. Because of Brazil's large external debt overhang and heavy dependence on imported petroleum and growth of manufactured exports, the results are quite sensitive to assumptions regarding international interest rates, lower growth of the industrialized countries and petroleum prices. For example, an increase of one percentage point in LIBOR would raise the external financing gap by almost US$1 billion annually. On the domestic side, failure of the current stabilization efforts would delay agreement on the external financing package and would further tighten the foreign exchange constraint.

BRAZIL (1980-1995)

| | Historical | | | | | | | Projections | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 1980 | 1981 | 1982 | 1983 | 1984 | 1985 | 1986 | 1987 _e/ | 1988 | 1989 | 1990 | 1991 | 1992 | 1993 | 1994 | 1995 |
| Real GDP Growth (%) | 7.2 | -1.5 | 1.0 | -3.2 | 4.5 | 8.3 | 8.0 | 5.0 | 5.2 | 5.1 | 5.1 | 5.1 | 5.1 | 5.1 | 5.1 | 5.1 |
| Investment/GDP (%) | 22.5 | 21.2 | 21.2 | 17.0 | 16.4 | 16.3 | 19.3 | 17.5 | 17.5 | 17.5 | 18.0 | 18.0 | 18.0 | 18.0 | 18.0 | 18.0 |
| Domestic Savings/GDP (%) | 20.4 | 20.9 | 20.6 | 19.3 | 22.0 | 21.5 | 22.4 | 20.5 | 20.4 | 20.2 | 20.8 | 20.7 | 20.6 | 20.5 | 20.4 | 20.3 |
| Real Per Capita GNY Growth | 2.9 | -6.1 | -2.3 | -6.2 | 4.2 | .. | 9.2 | 3.0 | 3.3 | 3.1 | 2.9 | 3.1 | 2.7 | 2.8 | 2.8 | 2.9 |
| Real Per Capita Consumption Growth | 1.1 | -2.0 | 1.0 | -4.2 | 0.4 | 5.9 | 9.3 | 2.3 | 3.0 | 3.1 | 2.3 | 2.9 | 2.9 | 2.9 | 2.9 | 2.9 |
| Import Volume GNFS (% Change) | 1.8 | -13.5 | -5.2 | -17.2 | 8.8 | -3.2 | 4.6 | 0.4 | 6.6 | 7.8 | 5.1 | 5.1 | 5.1 | 5.1 | 5.1 | 5.1 |
| Export Volume GNFS (% Change) | 22.6 | 20.7 | -8.2 | 13.1 | 20.2 | -3.4 | -21.9 | -0.6 | 5.3 | 5.2 | 5.2 | 5.2 | 5.2 | 5.2 | 5.2 | 5.2 |
| Resource Balance (% GDP) | -2.1 | -0.4 | -0.7 | 2.4 | 5.6 | 9.0 | 4.6 | 4.0 | 3.9 | 3.8 | 4.0 | 3.9 | 3.8 | 3.7 | 3.6 | 3.5 |
| Interest Payments (% GDP) _a/ | 3.1 | 3.7 | 4.1 | 4.5 | 4.3 | 4.3 | 3.3 | 6.5 | 5.8 | 5.7 | 5.7 | 5.3 | 5.2 | 5.1 | 5.0 | 4.8 |
| Current Acct. Bal. (% GDP) | -5.1 | -4.3 | -5.8 | -3.3 | 0.0 | -0.1 | -1.1 | -2.9 | -2.0 | -2.0 | -1.9 | -1.4 | -1.6 | -1.6 | -1.6 | -1.5 |
| Net Medium and Long-term loans (% GDP) | 1.8 | 3.1 | 2.7 | 2.3 | 3.2 | 0.1 | 0.6 | 4.1 | 3.4 | 3.1 | 2.7 | 2.1 | 2.2 | 2.2 | 2.1 | 2.1 |
| o.w. Official (%GDP) | 0.3 | 0.3 | 0.4 | 0.8 | 0.7 | 0.2 | -0.1 | 1.0 | 1.1 | 0.9 | 0.9 | 0.7 | 0.1 | 0.1 | 0.1 | 0.2 |
| o.w. Financial Markets (%GDP) | 1.5 | 2.7 | 2.2 | 1.4 | 2.6 | -0.2 | 1.5 | 2.7 | 1.9 | 1.9 | 1.2 | 0.4 | 0.7 | 0.1 | -0.4 | -0.8 |
| Net Financial Transfers (% GDP) _a/ | -1.3 | -0.6 | -1.4 | -2.2 | -1.1 | -4.2 | -2.8 | -2.4 | -2.5 | -2.6 | -3.1 | -3.2 | -3.0 | -2.9 | -2.8 | -2.8 |
| Total External Debt (% GDP) | 28.1 | 29.1 | 32.3 | 47.0 | 49.4 | 48.5 | 41.8 | 75.8 | 70.8 | 68.2 | 69.3 | 66.6 | 64.1 | 61.9 | 59.7 | 57.6 |
| Total External Debt (% XGS) | 301.8 | 297.1 | 389.0 | 402.0 | 342.7 | 364.2 | 432.5 | 456.2 | 419.8 | 402.3 | 398.3 | 381.6 | 368.2 | 354.1 | 340.7 | 327.9 |
| Debt Service (% XGS) _a/ | 63.0 | 65.8 | 80.9 | 52.8 | 39.5 | 39.7 | 44.2 | 98.0 | 84.8 | 74.4 | 72.4 | 75.9 | 75.3 | 68.8 | 61.1 | 56.4 |
| Interest Service (% XGS) _a/ | 33.7 | 38.3 | 49.0 | 38.4 | 29.9 | 32.0 | 34.2 | 38.9 | 34.6 | 33.3 | 33.0 | 30.3 | 29.8 | 29.2 | 28.5 | 27.5 |
| Interest Payments Coverage (% of Trade Surplus/Interest) | -67.3 | -9.7 | -16.2 | 52.4 | 130.2 | 100.2 | 64.5 | 62.5 | 67.7 | 66.8 | 69.6 | 73.7 | 73.3 | 72.7 | 72.4 | 72.6 |

Footnotes:
_a/For 1980-86 interest is what has actually been paid; for 1987-95 what is due. Includes interest paid on short-term debt.

CHILE

Prospects

Key Assumptions:

34. A moderate improvement of Chile's terms of trade over the medium trade from their present low level is assumed (copper prices rise by about 4 percent per year), although by 1995 terms of trade remain 5 percent below the 1980 level. Continued efforts to maintain a realistic real exchange rate and some acceleration of growth in Chile's trading partners after 1988 permits export volumes to rise by 5 percent per year from 1986-95. Strong domestic policy performance is assumed to continue through the projections period. Domestic savings rates rise to above 19 percent of domestic income, well in excess of historic performance. A strong domestic savings performance permits a rise in investment while maintaining interest payments on external debt. The combination of a strong domestic policy performance and some eventual improvement in the international economic environment are assumed to enable Chile to achieve a 4 percent growth rate of GDP, equivalent to 2.5 percent per year in per capita terms.

Base Case Results:

35. Under these assumptions, per capita income would rise slightly faster than GDP, and consumption per capita would increase by 2.4 percent a year. However, despite the rise in domestic savings, the increased investment necessary to achieve the target growth rate would require substantial utilization of external resources. Net disbursement of long-term

loans from commercial banks would average 6 percent of GDP from 1988-95, more than 2 percentage points higher than what was obtained in 1982-86. Borrowing of these funds at commercial rates results in a debt service ratio of 47 percent in 1995. This compares to 56 percent in the beginning of 1986. In these circumstances, the ratio of the current account deficit to GDP rises from 6.5 percent in 1986 to an unsustainable 10.5 percent in 1995. With the large external borrowing requirements implied by a current account deficit of this magnitude, Chile's debt service burden would experience explosive increases in the late 1990s. To prevent this from occurring Chile would have to disrupt its recovery at some point in early 1990, and undertake another difficult contracting period to reduce domestic absorption relative to output.

Sensitivity of Results:

36. These results are quite sensitive to the assumptions about the world price of copper. Since copper makes up about 40 percent of Chile's exports, any further deterioration in the real price of copper would greatly increase the external resources necessary to meet the targeted GDP growth rate. The other key assumption in generating these results is that Chile sustains the recent improvement in domestic savings performance. For example, if the ratio of domestic savings to GDP were to remain just two percentages points below the average of 19 percent assumed in these projections, the net external resources necessary to hit the targets would rise dramatically. The debt service ratio would climb to above 60 percent by 1995, and the current account deficit to GDP ratio would be on the order of 20 percent.

CHILE (1980-1995)

| | Historical Data | | | | | Estimated | | Projections | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 1980 | 1981 | 1982 | 1983 | 1984 | 1985 | 1986 | 1987 | 1988 | 1989 | 1990 | 1991 | 1992 | 1993 | 1994 | 1995 |
| | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== |
| Real GDP Growth (%) | 7.8 | 5.5 | -14.1 | -0.7 | 6.3 | 2.4 | 5.7 | 4.6 | 4.1 | 4.1 | 4.1 | 4.0 | 4.0 | 4.0 | 4.0 | 4.0 |
| Investment/GDP (%) | 21.0 | 22.7 | 11.3 | 9.8 | 13.6 | 13.7 | 14.6 | 15.9 | 16.5 | 17.0 | 17.5 | 18.0 | 19.0 | 19.5 | 20.0 | 20.0 |
| Domestic Savings/GDP (%) | 16.8 | 12.4 | 9.4 | 12.5 | 12.6 | 16.5 | 18.4 | 19.4 | 18.6 | 19.1 | 19.0 | 19.0 | 19.4 | 19.2 | 19.4 | 19.4 |
| Real Per Capita GNY Growth | 5.1 | 0.8 | -21.1 | -0.9 | 0.4 | 1.5 | 2.2 | 4.7 | 2.2 | 2.9 | 3.2 | 2.5 | 2.4 | 2.9 | 2.4 | 2.3 |
| Real Per Capita Consumption Growth | 2.4 | 6.7 | -12.2 | -4.6 | -0.4 | -2.6 | 3.0 | 1.4 | 2.7 | 2.1 | 3.5 | 3.0 | 2.0 | 2.9 | 2.3 | 2.6 |
| Import Volume Gnfs (% Change) | 18.7 | 15.7 | -36.3 | -15.1 | 16.5 | -11.0 | 9.7 | 4.2 | 11.9 | 11.7 | 10.2 | 9.4 | 7.5 | 7.4 | 6.3 | 4.8 |
| Export Volume Gnfs (% Change) | 14.3 | -9.0 | 4.7 | 0.6 | 6.8 | 6.9 | 9.8 | 5.1 | 7.0 | 9.0 | 4.0 | 5.2 | 4.6 | 4.0 | 4.9 | 4.3 |
| Resource Balance (% GDP) | -4.2 | -10.3 | -1.9 | 2.7 | -1.1 | 2.8 | 3.8 | 4.8 | 2.8 | 2.8 | 2.0 | 1.3 | 0.6 | -0.5 | -0.8 | -0.9 |
| Interest Payments (% GDP) _a/ | 4.3 | 5.4 | 9.8 | 8.7 | 12.1 | 11.8 | 10.6 | 9.2 | 8.9 | 8.6 | 8.4 | 8.8 | 9.0 | 8.3 | 8.5 | 8.7 |
| Current Acct. Bal. (% GDP) | -7.1 | -14.5 | -9.5 | -5.7 | -10.7 | -8.2 | -6.5 | -4.2 | -5.3 | -5.2 | -6.1 | -7.5 | -8.6 | -9.2 | -10.0 | -10.5 |
| Net Medium and Long-term Loans (%GDP) | 7.7 | 10.4 | 5.8 | 5.7 | 9.1 | 5.3 | 0.7 | -3.1 | 2.3 | 4.3 | 5.1 | 6.5 | 7.7 | 8.4 | 9.2 | 9.7 |
| O.W. Official | -0.5 | -0.2 | -0.3 | 0.5 | 1.3 | 2.8 | 3.4 | 3.2 | 2.2 | 1.7 | 1.4 | 0.9 | 0.6 | 0.1 | -0.3 | -0.6 |
| O.W. Financial Markets | 7.0 | 8.7 | 5.9 | 5.4 | 7.7 | 2.6 | -2.7 | -6.3 | 0.2 | 2.6 | 3.8 | 5.7 | 7.1 | 8.3 | 9.4 | 10.2 |
| Net Financial Transfers (% GDP) _a/ | 3.4 | 5.0 | -4.0 | -3.0 | -3.0 | -6.5 | -6.3 | -12.7 | -7.5 | -5.9 | -4.9 | -2.9 | -1.9 | -0.5 | 0.1 | 0.3 |
| Total External Debt/(% GDP) | 43.9 | 48.1 | 71.3 | 92.1 | 104.0 | 126.4 | 123.3 | 102.4 | 98.5 | 96.9 | 95.7 | 96.0 | 97.4 | 99.5 | 102.2 | 105.3 |
| Total External Debt/(% XGS) | 193.0 | 279.7 | 336.6 | 376.8 | 414.6 | 430.5 | 401.5 | 317.9 | 298.7 | 276.2 | 266.7 | 259.7 | 259.8 | 263.6 | 266.2 | 271.5 |
| Debt Service /(% XGS) _a/ | 42.1 | 63.6 | 70.7 | 54.5 | 58.5 | 61.3 | 56.0 | 58.9 | 41.7 | 40.1 | 37.8 | 44.8 | 44.2 | 44.0 | 43.5 | 46.7 |
| Interest Service/(% XGS) _a/ | 18.8 | 31.5 | 46.3 | 35.5 | 48.1 | 33.1 | 28.6 | 28.6 | 27.0 | 24.6 | 23.5 | 23.9 | 23.9 | 21.9 | 22.1 | 22.6 |
| Interest Payments Coverage (% of Trade Surplus/Interest) | -97.1 | -190.6 | -19.3 | 31.4 | -8.8 | 23.4 | 36.1 | 52.0 | 32.0 | 33.0 | 24.0 | 15.0 | 6.0 | -6.0 | -10.0 | -10.0 |

Footnotes:
_a/For 1980-86 interest is what was actually paid; For 1987-95 what is due. Includes interest on short-term debt.

PHILLIPINES

Prospects

Key Assumptions:

37. It is assumed that the Philippines undertakes the policy reforms necessary to achieve a rise in GDP growth of 5 percent a year, implying an increase of 2.5 percent in per capita terms. Domestic savings are presently at an historic low relative to income as a result of efforts to maintain consumption levels during the recession. Domestic savings are therefore projected to rise only gradually from 18 percent of income in 1986 between 19 percent from 1988-1995. It is assumed that maintenance of a stable real exchange rate permits a rise in export volume growth to 5 percent per annum and encourages some repatriation of flight capital. The terms of trade remain at about 1986 levels, as recovery in the price of some primary commodity exports from present depressed levels is matched by rises in the prices of petroleum and manufactures imports.

Base Case Results:

38. Consumption per capita would rise by 2.5 percent from 1987-95. To achieve the target 2.5 percent average annual increase in per capita output would require substantial inflows of external resources. Net long term lending would have to average 4.5 percent of GDP for the next 9 years, 1 percentage point greater than the 1982-86 average. As a consequence, the debt service ratio is in excess of 40 percent by 1995, compared to 32 percent in 1986. In these circumstances, the ratio of the current account deficit to

GDP moves from a 3 percent surplus in 1988 to a 5 percent deficit by 1995. With such large external borrowing requirements, the Philippines' debt service burden would experience explosive increases in the late 1990s, requiring yet another painful adjustment when access to the necessary funds ends.

Sensitivity of Results:

39. This forecast is highly sensitive to the domestic policy assumption of substantial strrengthening of economic policy. This includes reform of the tax code, liberalization of trade, and rehabilitation of Government financial institutions. This in turn depends heavily on the assumption of political stability.

PHILIPPINES (1980-1995)

| | Historical Data | | | | | Estimated | | Projections | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 1980 | 1981 | 1982 | 1983 | 1984 | 1985 | 1986 | 1987 | 1988 | 1989 | 1990 | 1991 | 1992 | 1993 | 1994 | 1995 |
| | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== |
| Real GDP Growth (%) | 5.3 | 3.8 | 2.9 | 0.9 | -5.7 | -4.0 | 0.2 | 5.0 | 4.8 | 5.0 | 5.1 | 5.1 | 5.2 | 5.2 | 5.3 | 5.3 |
| Investment/GDP (%) | 30.7 | 30.6 | 28.3 | 26.7 | 18.7 | 15.9 | 13.1 | 18.0 | 21.5 | 22.8 | 22.9 | 23.0 | 23.1 | 23.1 | 23.2 | 23.3 |
| Domestic Savings/GDP (%) | 25.0 | 25.1 | 21.6 | 19.9 | 18.6 | 18.8 | 17.6 | 19.1 | 19.6 | 20.2 | 20.1 | 19.8 | 19.6 | 19.4 | 19.0 | 18.8 |
| Real Per Capita GNY Growth | 0.6 | 0.0 | -1.6 | -0.1 | -8.4 | -6.7 | -1.8 | 3.1 | 2.3 | 2.7 | 2.7 | 2.6 | 2.6 | 2.7 | 2.7 | 2.7 |
| Real Per Capita Consumption Growth | 1.7 | 1.3 | 0.8 | -0.5 | -2.2 | -2.3 | -1.6 | 0.6 | 1.4 | 2.0 | 2.8 | 2.9 | 2.9 | 2.9 | 3.1 | 3.0 |
| Import Volume Gnfs (% Change) | 3.2 | -2.6 | 3.2 | 11.8 | -16.6 | -23.0 | 1.7 | 22.9 | 19.0 | 7.7 | 6.6 | 6.3 | 6.1 | 5.9 | 6.1 | 5.8 |
| Export Volume Gnfs (% Change) | 12.7 | 1.1 | -1.1 | 9.0 | 8.0 | -7.2 | 12.0 | 3.9 | 5.6 | 3.9 | 5.2 | 5.1 | 4.9 | 5.0 | 4.6 | 4.6 |
| Resource Balance (% GDP) | -5.7 | -5.4 | -6.8 | -6.7 | -0.1 | 3.0 | 4.6 | 1.6 | -1.5 | -2.4 | -2.4 | -2.7 | -3.0 | -3.3 | -3.7 | -4.0 |
| Interest Payments (% GDP) _a/ | 4.1 | 5.5 | 6.0 | 5.7 | 5.7 | 5.3 | 6.3 | 4.7 | 4.6 | 4.7 | 4.8 | 4.6 | 4.6 | 4.4 | 4.2 | 3.9 |
| Current Acct. Bal. (% GDP) | -5.4 | -5.3 | -8.0 | -8.0 | -3.9 | 0.0 | 2.8 | 0.7 | -2.6 | -3.5 | -3.6 | -3.9 | -4.3 | -4.5 | -4.9 | -5.3 |
| Net Medium and Long-term Loans (%GDP) | 4.0 | 3.9 | 3.7 | 4.9 | 2.9 | 3.0 | 2.2 | 2.8 | 5.5 | 5.7 | 5.2 | 4.9 | 4.9 | 4.0 | 3.3 | 3.8 |
| O.W. Official | 1.2 | 2.0 | 1.2 | 2.9 | 1.8 | 1.2 | 2.6 | 1.6 | 2.0 | 1.7 | 1.6 | 1.1 | 0.9 | 0.5 | 0.6 | 0.6 |
| O.W. Financial Markets | 2.6 | 1.7 | 2.4 | 1.9 | 1.0 | 1.7 | -0.4 | 1.2 | 3.5 | 4.0 | 3.6 | 3.8 | 4.0 | 3.5 | 2.7 | 3.2 |
| Net Financial Transfers (% GDP) _a/ | -0.2 | -1.7 | -2.3 | -0.7 | -2.7 | -2.3 | -5.4 | -2.5 | 0.4 | 0.4 | -0.1 | -0.2 | -0.1 | -0.8 | -1.2 | -0.5 |
| Total External Debt/(% GDP) | 49.5 | 53.9 | 61.0 | 69.6 | 76.1 | 80.3 | 80.1 | 75.7 | 76.3 | 76.8 | 76.9 | 75.1 | 73.4 | 71.0 | 68.2 | 66.0 |
| Total External Debt/(% XGS) | 218.3 | 242.5 | 303.8 | 295.7 | 306.5 | 330.7 | 327.5 | 325.4 | 312.5 | 310.4 | 313.6 | 309.0 | 305.9 | 299.6 | 293.0 | 289.9 |
| Debt Service /(% XGS) _a/ | 24.9 | 33.3 | 42.5 | 35.5 | 29.3 | 29.0 | 31.9 | 23.2 | 23.8 | 25.3 | 27.4 | 29.0 | 31.1 | 36.4 | 41.7 | 41.9 |
| Interest Service/(% XGS) _a/ | 18.2 | 24.9 | 29.8 | 24.1 | 22.9 | 21.7 | 22.1 | 20.1 | 18.9 | 19.1 | 19.5 | 19.1 | 19.0 | 18.6 | 18.0 | 17.3 |
| Interest Payments Coverage (% of Trade Surplus/Interest) | -138.2 | -98.4 | -113.5 | -119.1 | -2.2 | 56.2 | 73.0 | 33.0 | -33.0 | -50.0 | -50.0 | -59.0 | -67.0 | -74.0 | -87.0 | -100.0 |

Footnotes:
_a/For 1980-86 interest is what was actually paid;for 1987-95 what is due. Includes interest on short-term debt.

URUGUAY

Prospects

Key Assumptions:

40. The attached projection shows the implications of an alternative scenario through 1995, using somewhat more conservative assumptions than those of the SAL. Real GDP growth averages 3.2 percent per year during the 1987-95 period. Real exports rise by just over 4 percent per year, and real imports rise by about 4.5 percent per year. Real per capita consumption increases by approximately 2 percent per year.

Base Case Results:

41. Uruguay's resource balance averages about 3 percent of GDP during the projection period. The current account remains in deficit, however, by 1-2 percent of GDP because of interest payments on the external debt. Interest service consumes 25 percent of export earnings in 1987, declining to about 15 percent in 1995. The interest coverage is positive but less than 1.0, rising from 0.5 in 1987 to about 0.7 at the end of the projection period. The debt service ratio rises from 30 percent in 1987 to a peak of 37 percent in 1994 before turning down to about 35 percent in 1995.

42. If the debt relief obtained in July 1986 were removed from the projection, the effect would be to add 25 percentage points to the debt service ratio in 1987-88-89. It is evident that the 1986 Multi-Year Rescheduling Agreement succeeded in reducing Uruguay's medium-term debt-service problem rather dramatically.

Sensitivity of Results:

43. The above results are quite sensitive to assumptions concerning: (a) continued, moderate OECD growth; (b) absence of new restrictions to imports in the industrial countries; (c) reasonable interest rates in world markets; and (d) adequate external support.

44. Domestically, Uruguay must control price inflation and make sufficient credit available to the private sector to permit a revival of private sector activity. If the country is able to fulfill the conditions outlined by the Bank in the recent SAL, the prospects for achieving at least 3.2 percent growth should be quite good.

## Uruguay (1980-1995)

| | Historical | | | | | | | Projections | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 1980 | 1981 | 1982 | 1983 | 1984 | 1985 | 1986 _e/ | 1987 | 1988 | 1989 | 1990 | 1991 | 1992 | 1993 | 1994 | 1995 |
| Real GDP Growth (%) | 6.0 | 1.9 | -9.4 | -5.9 | -2.4 | 0.7 | 6.20 | 3.2 | 3.3 | 3.3 | 3.2 | 3.2 | 3.2 | 3.2 | 3.2 | 3.2 |
| Investment/GDP (%) | 17.3 | 15.4 | 14.4 | 10.0 | 8.8 | 8.2 | 7.79 | 8.81 | 10.73 | 11.23 | 11.95 | 11.76 | 12.11 | 12.68 | 13.27 | 13.91 |
| Domestic Savings/GDP (%) | 11.7 | 11.4 | 11.3 | 11.6 | 13.1 | 12.4 | 12.57 | 12.42 | 13.47 | 14.21 | 15.47 | 15.36 | 15.57 | 16.00 | 16.42 | 16.88 |
| Nat.Savings/Investment (%) | 62.51 | 70.61 | 65.02 | 65.18 | 70.79 | 68.07 | 100.63 | 82.24 | 81.02 | 83.32 | 90.23 | 92.81 | 94.91 | 95.81 | 96.76 | 96.33 |
| Real Per Capita GNY Growth | 5.11 | 2.90 | -10.67 | -13.51 | -5.07 | -0.14 | 11.23 | 0.09 | 2.23 | 2.77 | 3.37 | 3.06 | 2.92 | 2.75 | 2.81 | 2.64 |
| Real Per Capita Consumption Growth | 7.06 | 3.08 | -8.62 | -11.62 | -5.18 | 0.77 | 8.30 | 0.97 | 0.53 | 2.00 | 1.77 | 2.96 | 2.27 | 1.99 | 2.01 | 1.97 |
| Import Volume Gnfs (% Change) | 7.62 | 1.01 | -13.60 | -20.14 | -14.84 | 0.90 | 28.42 | 0.41 | 4.57 | 4.58 | 4.55 | 4.37 | 4.64 | 4.54 | 4.55 | 4.64 |
| Export Volume Gnfs (% Change) | 3.61 | 6.18 | -10.52 | 15.45 | 0.65 | 5.12 | 15.34 | 2.09 | 4.35 | 4.88 | 4.32 | 3.82 | 4.23 | 4.25 | 4.11 | 4.14 |
| Resource Balance (% GDP) | -5.6 | -3.9 | -3.1 | 1.7 | 4.2 | 4.2 | 4.03 | 3.12 | 2.51 | 2.76 | 3.23 | 3.33 | 3.22 | 3.12 | 2.98 | 2.83 |
| Interest Payments (% GDP) _a/ | 1.56 | 1.91 | 2.77 | 5.2 | 6.6 | 6.8 | 5.80 | 6.08 | 5.68 | 5.68 | 5.51 | 5.25 | 4.84 | 4.58 | 4.28 | 4.14 |
| Current Acct. Bal. (% GDP) | -7.0 | -4.1 | -2.5 | -1.1 | -2.5 | -2.1 | -0.71 | -2.06 | -2.27 | -2.09 | -1.46 | -1.12 | -0.86 | -0.74 | -0.61 | -0.66 |
| Net MLT Loans (%GDP) | 2.23 | 3.12 | 2.61 | 7.12 | 0.75 | 0.54 | 3.07 | 2.32 | 2.84 | 2.41 | 0.48 | -0.13 | -0.33 | -0.54 | -0.55 | 0.36 |
| Official | 0.36 | -0.04 | 0.44 | 0.38 | 0.64 | 0.17 | 1.19 | 1.33 | 1.43 | 1.00 | 0.72 | 0.07 | -0.06 | -0.12 | -0.04 | -0.01 |
| Financial Markets | 1.82 | 2.97 | 2.40 | 6.76 | 0.29 | 0.66 | 1.88 | 0.98 | 1.41 | 1.42 | -0.24 | -0.20 | -0.27 | -0.42 | -0.50 | 0.37 |
| Net Financial Transfers(% GDP) _a/ | 0.67 | 1.21 | -0.16 | 1.96 | -5.82 | -6.25 | 3.84 | 2.90 | 3.55 | 3.02 | 0.60 | -0.16 | -0.41 | -0.67 | -0.68 | 0.45 |
| Total External Debt/(% GDP) | 16.38 | 19.21 | 28.61 | 61.46 | 63.74 | 77.37 | 45.42 | 45.16 | 44.75 | 47.86 | 48.54 | 46.98 | 46.91 | 46.47 | 45.83 | 40.59 |
| Total External Debt/(% XGS) | 104.15 | 117.76 | 157.13 | 223.35 | 238.86 | 294.67 | 184.27 | 184.12 | 179.11 | 185.05 | 182.44 | 173.09 | 170.89 | 167.32 | 163.23 | 142.97 |
| Debt Service /(% XGS)_a/ | 18.08 | 17.28 | 32.53 | 26.92 | 35.58 | 40.38 | 28.30 | 29.60 | 29.22 | 30.58 | 36.69 | 36.17 | 36.51 | 37.31 | 37.38 | 34.82 |
| Interest Service/(% XGS)_a/ | 9.93 | 11.71 | 15.23 | 18.73 | 24.62 | 25.84 | 23.53 | 24.79 | 22.73 | 21.98 | 20.71 | 19.35 | 17.62 | 16.50 | 15.23 | 14.59 |
| Interest Payments Coverage (% of Trade Surplus/Interest) | -358.37 | -206.57 | -113.10 | 32.52 | 64.09 | 61.91 | 69.42 | 51.30 | 44.25 | 48.47 | 58.54 | 63.38 | 66.49 | 68.01 | 69.66 | 68.27 |

Footnotes:

_a/ For 1980-86 interest is what was actually paid ; for 1987-95 what is due. Includes interest on short-term debt.

ARGENTINA

Prospects

Key Assumptions:

45. Argentina undertakes stabilization measures and structural adjustment reforms and external finance is available to permit the economy to have a 2.5 percent per annum growth in per capita GDP. The stable economic environment and new resources will generate rapid increase in domestic investment; by 1995 the investment rate would have risen to 18 percent of GDP, comparable to the rates of the seventies. Domestic savings would increase to 26 percent of GDP by 1995. Policy reforms will increase the productivity of investment; ICORs are assumed to decline to 4.5 from 8.6 in 1982-86. Capital flight is assumed to abate. The projections assume that commercial banks will continue to roll over amortization payments due on existing debt.

Base Case Results:

46. Even with improved domestic saving efforts, Argentina would not be able to finance the required external funds if borrowed at conventional commercial terms. The debt service ratio would remain very high, dropping from 62 percent in 1986 to 52 percent in 1995. The debt to exports ratio in 1995 is 352, an improvement from 530 in 1986. Even with the rescheduling Argentina is unlikely to simultaneously achieve reasonable growth in income and creditworthiness.

47. The achievement of these two objectives would require some concessional financial assistance. The provision of debt relief would reduce the borrowing required to achieve 4 percent annual growth rate of GDP. Future debt servicing requirements would decline and over time the country could become creditworthy.

48. The terminal (1995) debt service ratio, with financial relief is 27 percent. Abandoning the rescheduling of commercial banks will increase the present value of financial relief required as it would raise near term debt service ratios.

Sensitivity of Results:

49. The Argentine economy is very unstable and a sustained recovery of economic growth is unlikely if this instability continues. Successful stabilization of the economy is a prerequisite to strutural adjustment reform and growth. Vigorous export promotion through changes in the trade regime to diversify the export base will be required. Substantial progress in the reform of public institutions will permit fiscal restraint as well as enhance production efficiency.

50. The projections have assumed increased saving and investment efforts as a result of a more stable macroeconomic environment. If the

policy climate does not favor domestic saving, the external requirements to achieve the target growth of GDP would be much higher.

ARGENTINA (1980-1995)

| | Historical | | | | | | | Projections | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 1980 | 1981 | 1982 | 1983 | 1984 | 1985 | 1986 e/ | 1987 | 1988 | 1989 | 1990 | 1991 | 1992 | 1993 | 1994 | 1995 |
| Real GDP Growth (%) | 2.4 | -6.8 | -4.5 | 2.8 | 2.6 | -4.6 | 5.7 | 4.0 | 4.1 | 4.1 | 4.0 | 4.0 | 4.0 | 4.0 | 4.0 | 4.0 |
| Investment/GDP (%) | 22.2 | 18.7 | 16.8 | 13.6 | 11.3 | 8.7 | 9.1 | 12.6 | 18.4 | 18.3 | 18.3 | 18.2 | 18.2 | 18.2 | 18.2 | 18.2 |
| Domestic Savings/GDP (%) | 20.0 | 18.3 | 20.0 | 18.1 | 15.6 | 15.4 | 11.3 | 16.0 | 21.7 | 21.7 | 22.0 | 21.7 | 21.4 | 21.2 | 21.0 | 20.9 |
| Real Per Capita GNY Growth | 0.8 | -9.8 | -9.2 | 0.3 | 1.6 | -6.6 | 5.2 | 2.4 | 3.6 | 3.2 | 3.0 | 2.9 | 2.9 | 2.9 | 2.9 | 2.7 |
| Real Per Capita Consumption Growth | 4.8 | -4.1 | -9.7 | 2.2 | 3.9 | -8.0 | 6.8 | 0.7 | -4.1 | 3.0 | 3.0 | 3.0 | 2.9 | 2.9 | 2.9 | 2.9 |
| Import Volume GNFS (% Change) | 45.4 | 0.4 | -41.2 | -2.5 | 4.6 | -13.9 | 16.9 | 9.1 | 7.0 | 6.8 | 6.0 | 6.0 | 5.6 | 5.3 | 5.3 | 5.3 |
| Export Volume GNFS (% Change) | -5.0 | 5.9 | -2.4 | 11.4 | 0.1 | 14.6 | -8.6 | 12.1 | 2.9 | 3.6 | 3.1 | 3.1 | 3.1 | 3.1 | 3.1 | 3.1 |
| Resource Balance (% GDP) | -2.2 | -0.4 | 3.2 | 4.5 | 4.3 | 6.6 | 2.2 | 3.1 | 3.1 | 3.2 | 3.4 | 3.1 | 2.8 | 2.6 | 2.4 | 2.2 |
| Interest Payments (% GDP) _a/ | 4.1 | 6.0 | 6.3 | 8.3 | 5.5 | 7.6 | 5.2 | 5.9 | 5.6 | 5.6 | 5.6 | 5.2 | 4.8 | 4.4 | 4.0 | 3.9 |
| Current Acct. Bal. (% GDP) | -8.4 | -8.2 | -4.1 | -3.8 | -3.1 | -1.4 | -3.4 | -3.4 | -2.8 | -2.5 | -2.2 | -2.1 | -2.0 | -1.8 | -1.7 | -1.7 |
| Net Medium and Long-term loans (% GDP) | 5.0 | 11.1 | 10.1 | 2.3 | 0.0 | 4.2 | 7.2 | 2.7 | 2.5 | 2.4 | 2.2 | 2.1 | 2.0 | 1.5 | 1.3 | 1.4 |
| o.w. Official (% GDP) | 0.1 | 0.1 | 0.2 | 0.5 | -0.1 | 0.1 | 0.9 | 1.2 | 1.4 | 1.5 | 1.4 | 0.7 | 0.1 | -0.1 | -0.2 | -0.3 |
| o.w. Financial Markets (% GDP) | 4.6 | 8.7 | 8.9 | 2.0 | 0.1 | 4.3 | 7.1 | 2.4 | 1.8 | 1.7 | 1.5 | 1.9 | 2.1 | 1.7 | 1.6 | 1.7 |
| Net Financial Transfers (% GDP) _a/ | 0.9 | 5.1 | 3.8 | -6.0 | -5.5 | -3.4 | -5.0 | -3.2 | -3.0 | -3.2 | -3.4 | -3.1 | -2.8 | -2.9 | -2.7 | -2.5 |
| Total External Debt (% GDP) | 47.9 | 61.9 | 76.6 | 69.5 | 60.0 | 73.6 | 61.6 | 71.6 | 69.0 | 66.5 | 64.0 | 61.5 | 59.1 | 56.4 | 53.7 | 51.3 |
| Total External Debt (% XGS) | 226.6 | 286.9 | 434.3 | 453.0 | 455.0 | 461.6 | 529.7 | 492.4 | 446.0 | 418.9 | 409.4 | 399.4 | 389.0 | 376.2 | 363.8 | 351.7 |
| Debt Service (% XGS) _a/ | 34.9 | 43.4 | 48.5 | 67.8 | 49.5 | 57.3 | 66.4 | 56.8 | 44.8 | 47.8 | 51.9 | 53.1 | 54.4 | 52.6 | 51.3 | 51.8 |
| Interest Service (% XGS) _a/ | 19.4 | 27.7 | 35.6 | 54.1 | 41.6 | 47.6 | 44.8 | 40.8 | 35.9 | 35.3 | 36.1 | 33.7 | 31.5 | 29.4 | 27.2 | 26.4 |
| Interest Payments Coverage (% of Trade Surplus/Interest) | -53.0 | -7.2 | 51.3 | 54.4 | 77.5 | 87.4 | 43.2 | 52.5 | 56.4 | 57.6 | 59.9 | 59.5 | 59.4 | 60.0 | 60.7 | 58.1 |

Footnotes:
_a/For 1980-86 interest is what has actually been paid; for 1987-95 what is due. Includes interest on short-term debt.

NIGERIA

Prospects

Key Assumptions:

51. A relaxation of the foreign exchange constraints and vigorous implementation of the SAP to permit the economy to achieve about 2 percent annual growth of real per capita GDP are assumed. The availability of new financial resources from net external financial inflows and increased domestic saving would permit the rebuilding of the productive capital stock. Domestic savings would rise gradually from 12.3 percent of GDP in 1985 to 19 percent in 1995, quite comparable to performance in pre-oil boom period. Similarly investment would rise from the severely depressed rates of 11 percent of GDP in 1986 to 23 percent in 1995. The productivity of investment would also rise from improved policy climate and ICORs would be lower than those of the more normal pre-oil boom period. The debt rescheduling already in place is factored in the analysis. Specifically, it assumes a rescheduling of existing commercial bank debt falling due in 1986-91 and the refinancing of outstanding trade arrears. The projections assume an oil price of US$17 a barrel in 1987, US$19 in 1988-90, and a gradual increase to US$26 in 1995. Robust expansion of non-oil exports in the near term is assumed.

Base Case Results:

52. As the attached table shows, GDP grows at an average of 5.3 percent per annum in 1998-95, a result of the requirement of 2 percent annual growth

in per capita incomes. The rapid growth of output and investment raises the demand for imports and the current account balance deteriorates. The resource gap remains in deficit in 1989-85. The ratio of the current account deficit to GDP averages 3 percent in 1988-95, a marked deterioration of the improvements in external balance in 1984-86. The creditworthiness indicators also deteriorate markedly. The ratio of toal debt outstanding to exports increase from about 300 in 1987 to 450 in 1995. The debt service ratio goes from 34 percent (with debt rescheduling) in 1987 to 66 percent in 1995. The interest to exports ratios also increase markedly.

53. It is unlikely that Nigeria would be able to raise the kind of money incorporated in these projections. It means that for Nigeria to simultaneously achieve 2 percent annual per capita growth in income and improve its long-term creditworthiness, additional financial relief would be needed.

54. This financial relief would reduce the external borrowing required to achieve a sustained 5.3 percent annual growth of GDP. Thus creditworthiness indicators would improve compared to the projection without relief. Debt to exports ratio declines from 450 to 319 in 1995, with unchanged exports. However, creditworthiness indicators continue to be poor with interest and debt service ratios of 22 and 54 percent respectively in 1985. The implication is that Nigeria would continue to need financial assistance after 1995 to maintain GDP growth rates in excess of 5 percent.

55. These results have factored in the debt rescheduling arrangements made in 1986. These reschedulings reduce the near term debt service burden

and increase the longer term. The financial relief required would be higher without rescheduling.

Sensitivity of Results:

56. The price of oil is a key variable and the analysis of creditworthiness and the amount of financial assistance that is required is highly dependent on the price of oil. The vigorous implementation of the policy reform program is critical, particularly the reform of the trade regime to improve export competitiveness and promote non-oil exports.

NIGERIA (1980-1995)

| | Historical Data 1980 | 1981 | 1982 | 1983 | 1984 | 1985 | 1986 | Projections 1987 | 1988 | 1989 | 1990 | 1991 | 1992 | 1993 | 1994 | 1995 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | ==== | === | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== |
| Real GDP Growth (%) | 3.4 | -6.4 | -2.1 | -4.6 | -5.4 | 0.6 | -3.8 | -2.3 | 5.5 | 5.2 | 5.0 | 5.2 | 5.3 | 5.3 | 5.4 | 5.3 |
| Investment/GDP (%) | 24.0 | 20.3 | 21.4 | 14.7 | 10.6 | 10.7 | 11.3 | 7.7 | 10.0 | 12.6 | 15.5 | 17.6 | 18.7 | 20.0 | 21.3 | 22.7 |
| Domestic Savings/GDP (%) | 30.5 | 21.8 | 14.2 | 11.0 | 12.4 | 14.5 | 12.3 | 8.8 | 10.3 | 11.5 | 12.7 | 14.3 | 15.4 | 16.6 | 17.7 | 18.9 |
| Real Per Capita GNY Growth | 8 | -0 | -9 | -10 | -7 | -4 | -12 | -3.3 | 2.3 | 1.8 | 1.9 | 2.4 | 2.4 | 1.2 | 2.2 | 2.1 |
| Real Per Capita Cons. Growth | 9.0 | 12.8 | -2.4 | -8.8 | -11.2 | -8.2 | -10.2 | -2.2 | 0.3 | 0.1 | 0.1 | 0.3 | 0.9 | 0.9 | 0.9 | 0.9 |
| Import Volume Gnfs (% change) | 21.9 | 32.6 | -23.1 | -22.4 | -22.7 | -7.0 | -34.3 | -7.6 | 33.7 | 22.0 | 19.4 | 13.1 | 8.4 | 8.7 | 8.5 | 8.4 |
| Export Volume Gnfs (% change) | -9.5 | -48.5 | -30.6 | -2.6 | 15.6 | 7.8 | -1.5 | -17.0 | 10.8 | 4.7 | 2.4 | 4.3 | 5.0 | 4.1 | 4.0 | 2.5 |
| Resource Balance (% GDP) | 6.5 | -6.6 | -7.2 | -3.7 | 1.8 | 3.8 | 1.0 | 1.1 | 0.3 | -1.0 | -2.2 | -2.4 | -2.2 | -2.0 | -1.9 | -1.9 |
| Interest Payments (% GDP) _a/ | 1.0 | 1.4 | 1.6 | 1.8 | 2.4 | 2.3 | 2.9 | 1.7 | 1.5 | 1.3 | 1.2 | 1.0 | 0.9 | 1.4 | 1.3 | 1.3 |
| Current Acct Bal. (% GDP) | 5.8 | -7.9 | -9.3 | -5.4 | 0.2 | 1.6 | -1.6 | -1.2 | -1.6 | -2.6 | -3.5 | -3.4 | -3.0 | -3.3 | -3.2 | -3.1 |
| Net MLT Loans (% GDP) _a/ | 2 | 3 | 4 | 5 | -0 | -1 | 0.3 | 1.5 | 1.6 | 2.6 | 3.5 | 3.5 | 3.2 | 3.0 | 2.9 | 2.9 |
| O.W. Official | 0 | 0 | 0 | 1 | 0 | 0 | 0.5 | 0.9 | 0.8 | 0.8 | 0.9 | 0.8 | 0.6 | 0.4 | 0.3 | 0.2 |
| D.W. Financial Markets | 2 | 2 | 3 | 4 | -0 | -2 | -0.1 | 0.9 | 0.5 | 0.3 | -0.5 | -0.7 | -1.0 | -1.0 | -0.8 | -0.4 |
| Net Fin. Transfers (% GDP) _a/ | 0.6 | 1.6 | 2.2 | 3.0 | -2.5 | -3.1 | -3.1 | -0.2 | 0.1 | 1.1 | 2.3 | 2.4 | 2.3 | 1.7 | 1.6 | 1.5 |
| Total External Debt (% GDP) | 10.1 | 15.1 | 15.8 | 22.4 | 22.9 | 23.9 | 47.6 | 21.9 | 19.9 | 19.8 | 20.7 | 21.0 | 21.0 | 20.8 | 20.6 | 20.4 |
| Total External Debt (% XGS) | 32 | 61 | 97 | 166 | 147 | 141 | 336 | 299.7 | 264.7 | 288.4 | 336.5 | 360.6 | 379.0 | 401.3 | 421.9 | 450.0 |
| Debt Service (% XGS) _a/ | 4.1 | 9.1 | 16.1 | 23.9 | 33.6 | 35.5 | 39.2 | 34.2 | 29.1 | 29.1 | 41.5 | 41.3 | 44.7 | 60.1 | 65.9 | 66.3 |
| Interest Payments (% XGS) _a/ | 3.3 | 5.9 | 9.7 | 13.2 | 15.7 | 13.4 | 20.4 | 23 | 19 | 19 | 19 | 17 | 16 | 26 | 27 | 29 |
| Interest Payments Coverage Trade Surplus (% Interest) | 629 | -455 | -452 | -207 | 73 | 168 | 36 | 72.5 | 23.1 | -82.1 | -207.0 | -258.2 | -275.2 | -157.5 | -148.5 | -145.8 |

Footnotes:
_a/ For 1980-86 interest is what has actually been paid; for 1987-95 what is due. Includes interest paid on short-term debt.

## BOLIVIA

### Prospects

57. Despite the impressive progress made in the past two years, Bolivia faces many problems in its quest for economic development. The population of 6.5 million is increasing by almost 2.8 percent per year, and it will be difficult to provide employment opportunities to all who seek work. The very process of structural adjustment will aggravate the unemployment problem, in the medium term (a restructuring of COMIBOL, the state mining company, has already entailed lay-offs of about 20,000 miners). The country's extreme dependence on tin and natural gas exports is worrisome, and the identification of new export products merits top priority.

58. The accrued external debt at the end of 1986 represented 120 percent of the country's GDP and 700 percent of its exports of goods and services. Debt relief will be essential if the country is to recover. Domestic savings must be increased dramatically, from about 5 percent of GDP in 1987 to more than 18 percent by 1995. Investment spending must rise from about 9 percent in 1987 to 24 percent by 1995, and the efficiency of investment (the incremental capital output ratio) must improve markedly. It is expected that private-sector interests will play an increasing role in the economy, with the attendant inflow of risk capital. The International Finance Corporation recently approved assistance to the Potosi silver mines in the form of a US$800,000 loan and a US$400,000 equity-convertible loan, and has identified several other potential mining projects.

59. Assuming continued, strong policy improvement efforts and sustained external support, Bolivia might attain a real GDP growth rate on the order of 4.5 percent per annum in 1987-95. This would translate into about 1.6 percent per annum in per capita terms. Depending in part on future natural gas export possibilities, it might be possible to boost the growth rate to more than 5.5 percent in the 1990s. The purchase agreement with Argentina expires in 1992, and its renewal is not assured. Argentina enjoys large gas reserves of its own. Brazil might wish to purchase, but to make this possible would require sizable pipeline investments.

Key Assumptions:

60. The attached projection shows the implications of an accelerating GDP growth scenario, rising from 3.2 percent in 1987 to 5.4 percent in 1995. Almost no growth is envisioned for 1992, it should be noted, because of an expected drop in natural gas export earnings in that year. It should also be noted that growth in 1987 may be lower than projected, on the order of 2 percent, based on partial information for the year.

61. Real exports grow by 2.5 percent in 1988 and accelerate to 7.8 percent in 1995, exhibiting declines in 1987 and 1992. Real imports rise by 11 percent in 1988, following a drop of 14 percent in 1987, and then average a bit more than 6 percent annual growth. The resource balance remains negative throughout the projection period, averaging about 6 percent of GDP.

Base Case Results:

62. Due to the need to make sizable interest payments on the external debt, equivalent to about 7 percent of GDP, Bolivia's current account deficit averages 13-14 percent of GDP in 1987-95. Net term loans might finance about half of this deficit.

63. The financial indicators reveal the need for strong debt relief to make the projection credible. DOD as a percentage of GDP rises to 144 percent in 1995, and as a percentage of exports to 880 percent. The debt service ratio climbs from around 55 percent in 1986 to 87 percent in 1995. Interest charges rise from 41 percent of exports in 1986 to 52 percent in 1995. The interest coverage is negative, since the country has a negative resource balance.

64. It is clear that Bolivia, a very poor country with severe economic problems, requires extraordinary relief from at least half its existing debt burden if it is to grow and adjust in the coming years.

Sensitivity of Results:

65. The projection is sensitive to several assumptions, and is subject to more than the usual caveats. Bolivia is a "debt distress" case, dependent on the willingness of external donors and creditors to accept work-outs that imply deep discounts and to continue to provide new money on highly

concessional terms. In fact, the projected figures understate the magnitude of the debt problem, in that an undetermined amount of relief has been assumed by the country economists in order to close the model. The country requires external assistance to cover nearly half of its investment spending, all of its interest service, and all of its amortization of existing debt.

BOLIVIA

| | 1980 | 1981 | 1982 | 1983 | 1984 | 1985 | 1986 | 1987 | 1988 | 1989 | 1990 | 1991 | 1992 | 1993 | 1994 | 1995 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Historical Data | | | | | Estimated | | Projections | | | | | | | | |
| | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== | ==== |
| Real GDP Growth (%) | -0.6 | -0.3 | -6.6 | -7.3 | -3.1 | -2.1 | -2.9 | 3.2 | 4.3 | 4.3 | 4.3 | 4.5 | 0.7 | 5.0 | 5.2 | 5.4 |
| Investment/GDP (%) | 10.9 | 12.4 | 9.7 | 3.5 | 6.6 | 4.1 | 6.9 | 9.4 | 11.6 | 12.3 | 13.1 | 15.1 | 18.0 | 20.1 | 22.1 | 24.1 |
| Domestic Savings/GDP (%) | 16.3 | 10.0 | 13.6 | 6.3 | 13.1 | 6.9 | 1.9 | 5.4 | 6.4 | 6.9 | 7.5 | 9.6 | 10.9 | 13.5 | 16.0 | 18.6 |
| Real Per Capita GNY Growth | -1.3 | -2.1 | -20.5 | 0.8 | -3.2 | -8.0 | -5.7 | 0.4 | 1.4 | 1.7 | 1.7 | 2.1 | -0.6 | 1.8 | 2.1 | 2.4 |
| Real Per Capita Consumption Growth | -3.8 | -1.0 | -11.1 | -8.5 | -4.4 | -4.7 | -4.7 | -4.7 | 0.7 | 1.1 | 1.0 | -0.5 | -1.4 | -0.8 | -0.6 | -0.4 |
| Import Volume Gnfs (% Change) | -21.3 | 17.0 | -35.2 | -5.4 | -9.2 | 6.4 | 12.2 | -14.1 | 11.2 | 7.3 | 7.1 | 6.5 | 2.6 | 5.3 | 5.5 | 5.8 |
| Export Volume Gnfs (% Change) | -5.3 | 2.1 | -6.6 | -7.0 | -7.3 | -17.6 | 5.6 | -3.1 | 2.5 | 5.6 | 5.2 | 6.0 | -14.7 | 7.6 | 7.8 | 7.8 |
| Resource Balance (% GDP) | 5.4 | 2.7 | 10.0 | 9.3 | 7.7 | 3.0 | -5.0 | -3.9 | -5.2 | -5.4 | -5.5 | -5.5 | -7.1 | -6.6 | -6.1 | -5.5 |
| Interest Payments (% GDP) _a/ | 7.6 | 6.9 | 6.9 | 7.3 | 9.1 | 4.1 | 7.1 | 6.6 | 6.9 | 6.8 | 6.9 | 6.8 | 7.4 | 7.8 | 8.2 | 8.6 |
| Current Acct. Bal. (% GDP) | -0.1 | -14.0 | -5.3 | -4.7 | -6.2 | -9.7 | -13.5 | -11.1 | -12.7 | -12.8 | -13.0 | -12.8 | -15.0 | -14.9 | -14.7 | -14.5 |
| Net Long-term loans (% GDP) | 11.1 | 7.6 | 4.2 | -0.7 | 2.7 | -1.8 | 6.7 | 6.3 | 7.1 | 7.0 | 7.3 | 7.5 | 8.2 | 7.0 | 5.6 | 4.9 |
| o. w. Official | 6.3 | 4.9 | 3.2 | 0.4 | 4.1 | -0.8 | 9.0 | 6.5 | 6.9 | 5.8 | 1.8 | 1.7 | 0.8 | 0.3 | -0.2 | -0.2 |
| o. w. Financial Markets | 5.3 | 3.3 | -0.5 | -0.6 | -0.1 | -0.1 | 1.8 | 1.4 | 2.0 | 2.9 | 7.4 | 8.2 | 10.7 | 10.6 | 10.3 | 9.8 |
| Net Financial Transfers (% GDP) _a/ | 3.5 | 0.7 | -2.7 | -8.0 | -6.4 | -6.0 | 3.8 | 1.6 | 2.7 | 2.7 | 4.4 | 4.6 | 5.7 | 4.8 | 3.9 | 3.3 |
| Total External Debt (% GDP) | 88.9 | 94.2 | 97.7 | 129.3 | 140.3 | 136.8 | 122.0 | 117.9 | 119.6 | 121.1 | 124.3 | 127.6 | 136.9 | 140.1 | 142.4 | 143.9 |
| Total External Debt (% XGS) | 258.3 | 305.6 | 345.1 | 423.2 | 461.5 | 538.6 | 708.7 | 790.1 | 809.8 | 802.1 | 806.1 | 807.5 | 940.5 | 925.6 | 904.4 | 879.7 |
| Debt Service (% XGS) _a/ | 36.0 | 35.0 | 37.6 | 36.2 | 48.3 | 39.2 | 55.4 | 57.9 | 56.0 | 54.8 | 68.7 | 70.5 | 85.1 | 87.1 | 87.8 | 87.3 |
| Interest Service (% XGS) _a/ | 22.1 | 22.4 | 24.3 | 23.9 | 30.0 | 16.3 | 41.2 | 43.9 | 46.4 | 45.4 | 45.0 | 43.0 | 50.8 | 51.8 | 52.3 | 52.5 |
| Interest Payments Coverage (%) (Trade Surplus/Interest) | 71.2 | 38.4 | 145.2 | 126.8 | 84.5 | 72.6 | -71.2 | -59.7 | -76.2 | -78.2 | -80.0 | -81.1 | -96.7 | -84.5 | -73.8 | -64.4 |

Footnotes:

_a/For 1980-86 interest is what has actually been paid; for 1987-95 what is due. Includes interest paid on short-term debt.

28-Jul-87

## IV - Conclusions

### External Resource Requirements

66. The country projections presented in the previous section indicate the level of external resources required to sustain a reasonable pace of economic recovery. The results indicate that during the next five years a few countries (Colombia and Uruguay) would be able to reduce their use of external resources as a share of GDP from what they were able to obtain during the past five years. Others will require about the same magnitude of external resources relative to the size of their economies as they used during 1982-86 (Brazil, Chile and Argentina). Still others will need substantially more external resources during the next five years than they got during the past five years (Bolivia, Philippines, Nigeria). Only the countries in the first group are likely to meet their future external borrowing requirements if historic trends are extrapolated.

67. Country creditworthiness considerations, discussed below, make it unlikely that banks will be willing to provide the level of resources which countries in groups two and three would require. Given the increasing evidence of commercial bank retrenchment in lending to the highly-indebted countries and the likelihood that this trend will accelerate in the immediate future, even the countries in group two, which only need to increase their net foreign borrowing at between 4 percent and 5 percent annually are unlikely to be able to obtain the resources which they would require. Even Colombia and Uruguay which have more modest external capital requirements, will require some assistance (perhaps in the form of special cofinancing arrangements) if the banks are to be induced to maintain their exposure over

the next few years. The third group of countries, those which require substantial increases in their use of external resources, have little prospect of obtaining the magnitudes they will need.

68. There could of course be exceptions to this general conclusion. For countries where substantial, unexpected, and at this point unforeseeable, gains in creditworthiness occur, banks might be willing to provide the external resources required, especially if this occurs for one of the countries in which they already have an important stake. However, the conclusion for the highly-indebted countries as a group is that most will not find it possible to obtain the external resources which they will require to maintain an adequate pace of economic recovery. In these circumstances they will either have to reduce their external resource requirements by reducing economic growth (i.e., forego recovery), reduce their interest payments to their creditors or carry out some combination of the two.

69. The projections on which this conclusion is based assume that the eight countries discussed in Section III will maintain an outstanding domestic savings performance throughout the period 1987-95. For most of these countries this is an unrealistically optimistic assumption (e.g., Chile from 14 percent in 1982-86 to 19 percent in 1995; Argentina from 16 percent to 20 percent; Colombia from 17 percent to 24 percent; Uruguay from 12 percent to 17 percent; Nigeria 13 percent to 19 percent; Bolivia 8 percent to 23 percent, etc.). If it is assumed that domestic savings performance is no better than the average during 1982-86, external borrowing requirements would be about 5 percent of GDP higher for the eight countries as a group than the external financing requirements estimated in Section III. In these

circumstances external resources would be more than twice what these countries were able to borrow during 1982-86. Not even Colombia and Uruguay would be able to obtain sufficient external resources to sustain recovery, and if they were, they would not be able to meet the higher service payments which such an increase would imply. If the eight highly-indebted countries included in this study are not able to achieve these optimistic savings targets, unilateral interest relief would become common practice and recovery would be aborted.

Creditworthiness Prospects

70. Resumed access to international capital markets will only occur for a country which is in the group of highly-indebted countries analyzed in this paper if there are substantial gains in its creditworthiness. The projections presented in section III indicate that only Colombia and Uruguay are likely to achieve creditworthiness gains in the medium term which are sufficient to warrant resumption of some limited access to international capital markets. This will require heroic action on their part to increase sharply their domestic savings. The external debt of these countries is sufficiently low, however, relative to that of the other highly-indebted countries, and their prospects for achieving further improvement in their external positions sufficiently strong, that they should find it possible over the near term to bring their creditworthiness indicators well below what capital markets view as critical limits.

71. For the remainder of the highly-indebted countries, prospects are bleak. For those in the second group (Chile, Philippines, Brazil and

Argentina), the strengthening of creditworthiness which is projected to occur is far too weak to have a meaningful impact on these countries ability to attract market resources. For all of them, creditworthiness indicators in 1995 remain far below what would be required for creditors to classify them even as minimally good credit risks.

72. For the third group of countries, progress toward return to creditworthiness is either insignificant relative to the magnitude of the problem (Bolivia) or absent altogether (Nigeria). For these countries the external debt overhang is too great and/or prospects for their exports too weak for them to be able to make any meaningful headway in restoring creditworthiness. At the end of the projection period their creditworthiness indicators remain far in excess of what is manageable.

## Financial Relief

73. Given the poor prospects for these countries to obtain the level of external resources which they will require, and their inability to make meaningful progress towards restoring even a minimum semblance of creditworthiness, estimates have been made of the amount of additional financial relief which each would require in order to simultaneously resume an adequate rate of economic growth and reduce their debt service burden to levels which are consistent with a sustained return to creditworthiness. The results are as follows:

Table 2: Financial Relief Requirements

| Country | Index of Financial Relief a/ (%) | Disbursed and Outstanding Debt End-1986 (US$ billion) | Financial Relief (US$ billion) |
|---|---|---|---|
| Colombia | 0 | 15.2 | 0 |
| Uruguay | 0 | 2.9 | 0 |
| Chile | 11.6 | 20.3 | 2.4 |
| Philippines | 18.1 | 22.0 | 4.0 |
| Brazil | 19.2 | 107.1 | 20.6 |
| Argentina | 21.0 | 48.5 | 10.2 |
| Bolivia | 70.2 | 4.1 | 3.3 |
| Nigeria | 86.0 | 17.4 | 15.0 |

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a/ The Index of Financial Relief is defined as the present discounted value of relief (grant equivalent) which is required to ensure adequate growth (GDP growth of about 2.5 percent per annum) while allowing the country to end the period with a manageable external debt burden taken as a 20 percent interest service ratio, divided by the country's external debt at the end of 1995.

74. Table 2 indicates the amount of financial relief which each of the countries in this study would require in order to reduce its debt service burden to levels consistent with their growth and adjustment objectives. Bolivia and Nigeria require the greatest debt relief relative to their outstanding debt. The largest absolute amount of relief is required by Brazil, the country with the largest debt outstanding. Total financial relief required for the eight countries is US$56 billion, equivalent to about 24 percent of their debt outstanding in 1986. Assuming that the situation of these countries is representative of that faced by the other highly-indebted countries, the entire group of seventeen would require US$96 billion of financial relief.

75. As a cross-check on the financial relief values shown in Table 2, secondary market discounts on these countries' external debt are shown in Table 3. Comparison of these discounts with the financial relief indexes shown in Table 2 indicates that secondary market discounts are in almost all cases greater than the financial relief indexes. This reflects the extremely optimistic assumptions contained in the country projections presented in this study regarding economic management especially as it relates to the improvement of domestic savings performance. The large discrepancy between the estimated financial relief index and the secondary market discount for some countries may be the result of other country specific optimism. For example, the Brazil projection of Section III assumes that current stabilization and recovery efforts by the Brazilian Government will be successful. The larger secondary market discount reflects the fact that Brazil has stopped making interest payments on its commercial bank debt,

that the government still has no widely accepted recovery program and that there is a reasonable possibility that political forces in Brazil may disrupt adjustment management.

Table 3

Secondary Market Discounts
(% of face value)

| Country | Discount |
| --- | --- |
| Colombia | 16 |
| Philippines | 31 |
| Chile | 31 |
| Brazil | 39 |
| Argentina | 53 |
| Nigeria | 71 |
| Bolivia | 91 |

Source: Salomon Bros. Inc. June 1987.

76. Comparisons between estimates of required financial relief and secondary market discounts are tenuous at best. Secondary markets are thin and notoriously unstable. However, the existence of such discounts validates the finding of this study that for most of the highly-indebted countries, indexes of financial relief have a positive value. Whether secondary market valuations are a good proxy for the amount of financial relief which a highly-indebted country requires is open to debate. Nevertheless the existence of such discounts do have an impact on commercial banks in their decisions regarding the amount of new money they are willing to provide. To the extent that banks are influenced by secondary market discounts and are reluctant to provide sufficient new money because these discounts are too large, such discounts may be a self-fulfilling prophecy of required future relief in that they represent the amount of debt which will not be

serviced if new money flows are not provided by the banks. The results of this study suggest that a portion of the discount may also represent debt that will not be serviced even if new money is provided.

77. Based on the three criteria discussed above (adequacy of external resources, progress toward restoration of creditworthiness, and financial relief requirements) three groups of countries can be identified. The first group, Colombia and Uruguay should be able to sustain an adequate rate of economic growth while simultaneously reducing their external debt service burden to well within reasonable creditworthiness limits provided they are able to achieve the ambitious domestic savings target used in this study. It should not require financial relief. But it will require sustained adequate external financial support. This in turn will probably require resource mobilization efforts on these countries' behalf by the official financial institutions.

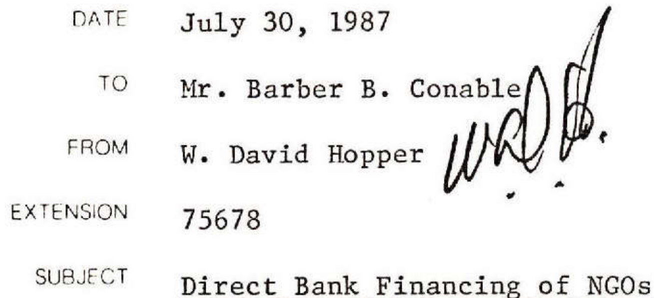
78. The second group of countries, Argentina, Brazil, Chile and the Philippines will require significant increases in external resources. Given their inability to reduce debt service burdens to manageable levels and the increasing reluctance of commercial banks to provide resources, it is unlikely that they will obtain the external resources they will require. If recovery is not to be sacrificed they will require moderate financial relief This relief could be provided in many alternative ways (e.g., buy-back of outstanding debt at a discount, etc.).

79. Projections for the third group of countries indicate that they will require significant amounts of financial relief. Debt increasing

solutions are not feasible for these countries. They will require solutions which substantially reduce their external debt.

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

# OFFICE MEMORANDUM



DATE July 30, 1987

TO Mr. Barber B. Conable

FROM W. David Hopper

EXTENSION 75678

SUBJECT Direct Bank Financing of NGOs

Attached is a proposal for direct Bank financing of NGOs, growing out of suggestions made by the Poverty Task Force, the Bank/NGO Committee and regional staff. In addition to its potential to extend the effective outreach capacity of the Bank's work at the local level, its establishment would send another strong signal of Bank interest in and support for indigenous NGOs, an area of considerable political importance to many of our shareholders.

If you agree that the idea should be pursued, I suggest we have a Policy Committee discussion on the merits and, if there is adequate support, consider then what level of funding would be appropriate and feasible as well as the best timing. While the Poverty Task Force suggested we might ultimately reach a $25 million annual level, it should start at a much lower level to test the idea out.

In any case, I suggest we address the concept first and then see how much resources we should attach to it.

Attachment

## Direct Bank Financing of NGOs

The Poverty Task Force suggested the establishment of a fund to strengthen the poverty efforts of NGOs. Mr. Conable stated at the Development Committee on April 10, 1987 that "we should explore increased Bank funding of NGOs in developing countries where they have a distinct comparative advantage by virtue of these grassroots involvement with the poor." In line with these suggestions, the following proposal for a small grants program, Direct Microproject Financing (DMF), has been developed at the initiative of Bank members of the Bank/NGO Committee. Policy Committee endorsement for this initiative is requested as it would constitute a realistic and effective additional device for funding people-oriented development through the unique outreach offered by developing country NGOs. It would also represent an important political initiative which would find considerable support among many shareholders. We suggest this initiative be mentioned in the annual meeting address.

The general concept of the DMF rests on three basic premises:

1. Direct funding of NGOs would be a significant addition to the array of mechanisms already available to the Bank for cooperation with NGOs. It would not replace or conflict with efforts, already well underway, to involve NGOs in Bank-supported programs through consulting, contracting* and sub-borrowing arrangements; it

* For instance, it would not alter the long-standing and very fruitful contractual arrangements to fund national family health associations--until now reached principally through the International Planned Parenthood Federation--and other population NGOs, such as the African Medical Research Foundation.

would not substitute for the Bank's encouragement to borrowers to collaborate with NGOs in appropriate programs, whether or not financed by the Bank.

2. The DMF would primarily support activities ancillary to or in preparation of a Bank-financed project (the "lead" project). Thus, in the most frequent cases, the NGO activity would either constitute a lead project component, or it would be parallel to the project and benefit the same project population (or portion thereof), or it would facilitate NGO involvement in planning or evaluation of the lead project. In this way, the Bank would operate on already familiar ground, economizing on microproject appraisal and supervision costs and using its general insight to supplement the relatively scant written documentation that can be expected from the grant applicant. Furthermore, the requirement of linkage to a lead project would limit the otherwise overwhelming number of grant requests that could be submitted to the Bank.

It is recognized, however, that Bank staff may identify important needs for microproject support in situations for which Bank or IDA lending is unlikely. Through the DMF the Regions could finance such projects deemed of special value, both in themselves and for their demonstration impact, even though not related to a prospective project.

3. The bulk of the funds allocated to the DMF would be made available to the Regions through an increment of their administrative budgets. A small portion would be allocated to PPR for innovative work on issues as poverty alleviation, environment, and safe motherhood. The announcement of the initiative would stress that the grants are intended for NGOs based in developing countries (either indigenous groups or local chapters of an international organization), and that grant decisions would evolve from practical links between Bank-financed operations and NGO programs verified in the course of sector and project work in the field.

Within this general framework, the major DMF features would be as follows:

Objective of the Grants: to finance, in toto or in part, high priority development (not relief) programs for the poor. The microprojects would be of a sustainable nature, susceptible of replication, and usually related to a Bank-supported lead project -- current or prospective.

Purpose of Grants: to build, maintain and run facilities (e.g. primary health clinics, village schools, cooperative sheds, etc) and provide development services (e.g. training and information, technical assistance for community participation, technical consultation and advice, transport).

NGO Eligibility: legally established, philanthropic or self-help organizations either indigenous to the recipient country, or with a well established activity record in the country and with predominantly indigenous staff. Special weight should be given to applications from NGOs which can (a) disperse the benefits of the grant throughout a large network of members, associates, sympathizers or service users, and (b) carry out the project as part of their normal activities rather than as an *ad hoc* separate assignment. A degree of public sector involvement in the NGO would be admissible, provided the NGO is essentially free to set its priorities and make major decisions on its own.

Country Requirements: Most grants would go to NGOs in IDA-eligible countries, but support could be provided also for very poor areas in other countries. A minimum of official concurrence would be required in the form of a "no objection" statement from the government agency relevant to the activity to be funded. At a later stage some country limits on grants might be necessary.

Eligible Sectors: All development activities that the Region believes would provide important direct benefits to the poor may be considered. While health/population/nutrition and education projects are expected to absorb most of the grants, worthwhile microprojects could also be funded in urban and rural

development, social forestry, water supply, organization of cooperatives, micro-enterprise development, and micro-loans for employment-generation initiatives.

Amount of Individual Grants: While this would depend in part on decisions concerning overall funding (dealt with separately) it would seem sensible to establish limits of a maximum of $100,000 per NGO and an average of $40,000 per grant. Repeat operations would not be favored but would not be excluded in principle. The aggregate amount of repeat grants would not exceed $300,000.

Co-funding Microprojects. Matching of the Bank grant with proportionate local or foreign resources would be highly desirable -- although not indispensable. The matching resources could be financial or in kind: food, volunteers' work, transportation facilities, etc.

Disbursement of Grants. Grants would be disbursed either in a lump sum or in tranches tied to the project progress.

NGO Microproject Monitoring. The microproject would have built-in monitoring and evaluation provisions. Simple but complete progress reports would be prepared by the NGO at main junctures of the project execution. Bank supervision missions

to the lead project would also monitor the microproject. An *ex-post* evaluation report would be expected from the NGO at the completion of the microproject. In some cases, the Region may wish to contract for an external audit.

OMS Guidelines for Grants. Guidelines for making grants along the lines described here would be incorporated in the OMS on Bank-NGO collaboration which is now in preparation. The guidelines need not cover the enormous variety of NGO and microproject situations, but instead would define the broad terms under which operational staff may make DMF grants, using their judgment of the country and of the projects and acting in an innovative and expeditious manner.

Monitoring of DMF. The Regions' work with NGOs would be monitored and backstopped (through provision of expertise for sector/project reviews, research of NGO country profiles, and policy advice) by PPR's Strategic Policy and Review Department (SPRD) SPRD is also the secretariat of the Bank-NGO Committee and the SPRD Director is the Bank co-chairman of that Committee). SPRD would also gather from each Region the lessons of experience to serve as possible operational models to all Regions and as material for public affairs purposes.

Administration of the DMF. The selection and evaluation of the projects to be assisted would be the responsibility of the relevant Bank department. The appropriate division would originate a DMF grant memorandum, which would be sent to the relevant vice-president, through the department director, for final approval. The originating division would be responsible for securing the clearances from other Bank departments (e.g. Legal, Central Operations Department, PPR) which may seem appropriate to the case. A simple grant agreement would be entered in each case to cover the amount of the grant, a summary description of the activities to be financed, disbursements, reporting and other relevant details. The grant would be disbursed through the same departmental offices and channels which handle the department's contractual services.

August 3 MEETING

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

# OFFICE MEMORANDUM

**DATE:** August 7, 1987

**TO:** Files

**FROM:** Robert Liebenthal, Acting Secretary, Policy Committee

**SUBJECT:** Minutes of the Policy Committee Meeting Monday, August 3, 1987

Attending:

Members

Messrs. Conable, Hopper, Qureshi, Stern, Wapenhans

Acting

Messrs. Burmester, Scott

Others

Messrs. Ayres, Dubey, Liebenthal, Lysy, Shakow, Stanton, Steer, Wood

1. Poverty Task Force

Mr. Hopper proposed, and it was agreed, that the work of the Poverty Task Force, which had prepared the preliminary report on April 7, 1987, should now be taken over by PPR, and that Mr. Conable should make a brief Board statement to that effect.

2. Round 2: Managing the Selection Process and the Supplementary Budget

Mr. Wapenhans introduced his memorandum of July 30, which called for a process for managing the Round 2 selection process to ensure that the budgeted limit of $92.7 million on separation packages and the limit of 390 on personnel separated could be observed. He proposed to establish a procedure to monitor and review the evolution of the Round 2 process, provide guidelines for recruitment for specialized positions, and ensure the support of the Policy Committee to review special cases and ensure that institutional objectives were met. Fill ratio targets by VPU might be considered, and the MRG could be used to review selection decisions. This would be the purpose of the first phase of the review process suggested which would be completed at around the middle of August. In the second phase, around September 10, the focus would be on identifying the need for any extraordinary action.

Mr. Stern pointed out that having a fill ratio target for any Vice Presidential Unit, would in effect constitute forced placement, which the Policy Committee had agreed would be undesirable. The MRG furthermore had not been instituted to overrule managers, but to review promotion proposals. Mr. Wapenhans agreed that the main priority was review and monitor the process, with a view to developing a position on voluntary separations by the deadline of August 22. Mr. Conable concluded that a timetable and a process should be set up for reaching the decisions required by August 22 and that the Senior Vice Presidents should pay particular attention to fill ratios, with a view to keeping the budgetary cost of terminations within the figures approved by the Board and keeping the number of separations within the ceiling also agreed with the Board.

3. Draft President's Report to the Development Committee

The consensus was that the draft report was a good one, but that some important points were missing, or should be made differently:

(a) We should report that some countries have made quite good progress;

(b) The attention given to the international economic environment for developing countries and specifically on aid flows was excessive, and had, in some cases, led to misinterpretations. For example, for some of the poor performing countries in Africa (for example, Sudan) aid flows should be going down. Statements on economic performance generally could be more upbeat.

(c) Section 3 on the middle-income high-debt countries should be written somewhat differently. The treatment in the draft report was confused and did not to reflect a clear sense of priorities. Messrs. Stern and Qureshi both stated that we should start out the section with our traditional view, namely that a large number of middle-income countries have been making progress but are still meeting significant problems, as a result of which some key assumptions about the environment need to be reviewed. We should say that the commercial banks have not been providing the support needed, that the World Bank has been asked to do more, but is presently constrained from doing so. In this context, reviving proposals like the "World's Bank's Bank" did not appear appropriate, and seemed to suggest a backing away from growth-oriented adjustment programs. We should stick to our normal "balanced prescription", unless we had something more specific in mind. Mr. Wapenhans suggested

that we should add some material on which debt workouts had worked and why. This would moreover provide a stronger basis for saying what the future emphasis of financial structuring, and specifically Bank responsibility should be. He added that all our workout proposals developed during recent years had assumed faster world economic growth, and that the failure of this to materialize naturally meant a larger financing burden. Mr. Stern added that the Bank had long been on record stating that adjustment would take many years, and that since there were practically no countries that had started a meaningful adjustment process prior to 1983, it would be surprising if there was already much success to report;

(d) On Section 4, the role of the World Bank, Messrs. Stern and Qureshi agreed that the discussion should be cut down considerably and that the Bank should stay away from the issue of the size of the GCI, or at least remain neutral, unless the US had shown willingness to see this discussed further. In particular, some sections, notably para. 66, appeared to advocate an $80 billion GCI. Mr. Qureshi suggested instead that we argue for a lending program which would meet the resource needs implied by the discussion in earlier parts of the paper, and leave it to the reader to draw the appropriate implications. Mr. Shakow, however, pointed out that it would be difficult to discuss the resource needs of the Bank without mentioning some orders of magnitude. In conclusion, it was agreed that drafting suggestions be made available within two days to the authors who would then prepare a revised draft by the end of the week.

4. Update of 1987 Creditworthiness Review

Mr. Stern introduced his memorandum of July 24, 1987, saying that the paper was designed to provide a background for the analysis of issues for the Fall Portfolio Review. It focused on three key issues: the growing arrears problem, the appropriate level of exposure in a situation of general deterioration and the need to reexamine our stance on B-loans and guarantees in a situation where the prospects for such lending had deteriorated. The situation warranted a more serious look, and the Committee was invited to provide guidance to those preparing the Fall Review. Should we reexamine our guidelines; provide criteria for exceptions; undertake an education effort vis-a-vis our market partners or position ourselves differently?

Mr. Qureshi stated that he saw little change in the situation since the April creditworthiness review. While the numbers had become larger for most of the countries at risk, no new countries had been added to the list and there was no basic change in the nature of the problem. He did not believe that a new look at the creditworthiness guidelines was required since these are, in any case, used flexibly. There was no need to adjust Bank strategy either. Since many of the countries in difficulties do not have an effective dialog with the Bank, retrenchment of lending would not be the solution. The issue was rather how to use the lending program to be more supportive, and how to establish an effective dialog in those cases where we did not have one. He felt that both net transfer and net disbursement questions were important. The role of a GCI would be to help generate confidence in the institution as a whole rather than to help sustain exposure in any given case. Mr. Qureshi added that a plan was now available for every country in arrears to the Bank. Mr. Wapenhans said that a GCI would enable the Bank to take more risks and stated that while some countries in non-accrual status should be considered for concessional funding, for others, e.g. Romania, Yugoslavia, the approach would have to be very different.

On the arrears problem, it was agreed that more could be done to sensitize Board members through informal consultation, and that depending on the specific countries concerned this process could be very helpful. Mr. Conable concluded by saying that pressure mechanisms for countries in arrears should be given serious examination. It was agreed that caution should be exercised on B-loans, in particular there should be no B-loans as part of a debt restructuring. Guarantees were to be preferred, but Board support would continue to be elusive. On exposure management, no general conclusion was reached, but Mr. Stern noted that debt service ratios were now extremely high, and that it was becoming more difficult to rely on goodwill as a basis for ensuring the servicing of debt to the Bank. More specific criteria for approving these high debt service levels should be considered, for example, the use of new money packages as a condition for approving adjustment loans.

**POLICY COMMITTEE MEETING**

MONDAY, AUGUST 3, 1987

10:00 a.m.

**AGENDA**

1. Updating of 1987 Creditworthiness Review

2. Draft President's Report to the Development Committee
(Memo from Mr. Shakow dated July 30, 1987)

3. Miscellaneous:

    (a) Poverty Task Force--Next Steps

    (b) Round 2: Managing the Selection Process
    and the Supplementary Budget
    (Memo from Mr. Wapenhans dated July 30, 1987)

Mr Conable

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

# OFFICE MEMORANDUM

DATE: July 31, 1987

TO: Members of the Policy Committee

FROM: Moeen Qureshi MAQ

EXT: 78051

SUBJECT: Update of 1987 Creditworthiness Review

This memorandum sets out some general reactions and some specific comments on the Creditworthiness Update" paper which may help in focusing the discussion of the subject on Monday.

In general I do not believe that developments since April 1987 require any modification of the conclusions that were reached during the discussion of the paper on "1987 Review of Country Creditworthiness and Bank Loan Portfolio Issues". These conclusions were summarized in a joint memo from Mr. Stern and me to Mr. Conable dated April 8, 1987 and are essentially similar to the discussion at the Financial Policy Committee, the minutes of which are attached to the "Update".

I do not agree with the "Update" that developments over the past few months should induce greater pessimism about the external environment than in April. In fact there have been some positive developments since then such as the negotiation of the Argentina financing package and the apparent end of the period of policy drift in Brazil. The performance of Mexico based on a remarkable response to the reform measures continues to be heartening. The positive results of efforts to mobilize additional resources for sub-Saharan Africa and the more concessionary approach to rescheduling by the Paris Club are also cause for some satisfaction. There is no indication of a recession in the United States despite the speculation in para. 2 of the paper. This is not to deny the situation is still fragile and needs careful monitoring and period review.

As regards the discussion of "exposure management" it is important to remember that the different guidelines are not and have not been treated as equally significant. For example, the guidelines relating to the share of debt to preferred creditors and the Bank's share of total debt service have been regarded as light relative to the guideline on Bank portfolio exposure ("the 10% limit"). More importantly these guidelines should not, and have not been, interpreted in a mechanistic way. The guidelines have to be applied in the context of country circumstances and judgements have to be made. For example, a Bank share of 20% of the debt service in a country which is following responsible economic policies may be less risky than a 15% share in a country with poor policies.

Considering the 14 countries with a Country Rating of III listed in Attachment 2 of the Update it is interesting to note that only four (Honduras, Peru, Romania and Paraguay) do not have adjustment operations in

P-1867

place or under active discussion. The appropriate response by the Bank in these cases is not necessarily retrenchment but a flexible approach to expose management on the basis of judgements regarding the quality of the adjustment programs, government commitments, and the role of other donors. The issue of appropriate burden-sharing, particularly in countries with other multilateral and bilateral donors will be given increased attention.

As regards the arrears problem, it is indeed a matter for serious concern. It is evident that there is little correlation between exposure and the emergence of arrears. In this context the net transfer situation is clearly important. However, again a mechanical approach is not useful. The April Creditworthiness Study (Table 8) indicated that there were 35 countries in Category III where net transfer in FY87 was expected to be negative. Only three of these are in non-accrual status and one in provision. This is not to dismiss the importance of addressing the issue at the country level before it becomes the basis for an arrears problem.

On the basis of the dialogue we are engaged in with Brazil and the leverage we may have for the adoption of a good adjustment program and putting together of a financing package, I believe that an expanded lending program may be justified there. The illustrative reference to a package for Brazil and the implication for IBRD headroom in para. 9 is somewhat misleading since it would imply larger lending levels than the "expanded levels" we are contemplating in case of agreement on an adjustment program. Further, our calculations indicate on the basis of the May 31 headroom of 13.2 billion that the "sizeable" part on this headroom would be less than 20%.

In conclusion, it is very important that the Bank maintain a medium-term perspective in evaluating country risk and exposure questions. I believe that at present an expanded role for the Bank in countries with bold adjustment programs is justified and concur with the position taken by the OVP meeting in April 1987 that "an increase in Bank's exposure in the short-run could ultimately reduce the overall role to the institution if adjustment programs....are carefully designed and implemented". The role has to be played in the context of more appropriate burden sharing by other parties. An early GCI would help us play this role effectively.

cc: Mr. Husain
Mr. Jaycox
Mr. Karaosmanoglu
Mr. Thalwitz

THE WORLD BANK / INTERNATIONAL FINANCE CORPORATION

# OFFICE MEMORANDUM

PCFIN87-7

TO: Members, Policy Committee

July 24, 1987

FROM: Ernest Stern, SVPFI

SUBJECT: Update of 1987 Creditworthiness Review

Attached is a brief note updating and highlighting some key creditworthiness considerations in our portfolio for discussion on Wednesday, July 29, 1987.

While there have been no major changes since the Creditworthiness Review last April, the issues raised in the attached will require close attention as individual country lending strategies are developed.

Attachment

cc: Ms. Haug

UPDATE OF 1987 CREDITWORTHINESS REVIEW

Issues in Country Risk Management

1. Since the most recent overall review of the loan portfolio was completed in March this year, it has not seemed necessary to revisit the detailed country classification presented in that review. Accordingly, apart from a few general comments about changes in risk classification which may soon be necessary, this update focusses mainly on three issues that we believe will be important for country risk management over the coming year:

- Loan arrears: Here the issue is what, if anything, can be done to increase the pressure on countries that are in a position to service IBRD debt but choose not to.

- Exposure management: Existing exposure guidelines are likely to pose problems in several countries over the coming year. The portfolio diversification limit (10%, flexibly applied) may pose a problem in Brazil and the "share of debt service" limit will affect a number of countries where our exposure, or that of preferred creditors in the aggregate, is already high. Even where exposure guidelines are not now a problem, there can be risk management issues if the country strategy proposes a sharp increase in fast-disbursing loans in the next year or two without any clear plan for dealing with the subsequent fall off in net flows.

- Use of guarantees/constraints on B-loans: We believe that risk considerations favor a more cautious attitude toward B-loan participations than in the past. On the other hand, use of guarantees in the context of a suitably balanced overall external financing plan may be encouraged, if major shareholders' objections can be overcome.

Country Risk Classification

2. The viability of growth-oriented adjustment strategies has always been seen as requiring a reasonably supportive external environment. In particular, trading opportunities need to be expanding, not stagnating, and adjusting countries need to be able to count on net inflows of external capital to supplement their own savings. Developments over the past few months are--with some exception such as the firming of oil prices and lots of talk about reduction of agricultural subsidies--not very encouraging. Significant reduction of imbalances among the major industrial countries now looks more likely to require recession in the United States. Moreover, many observers predict that the Citibank-led increase in commercial bank reserves will lead to greater difficulties in mobilizing net new money from commercial banks.

3. To the extent that greater pessimism about the external environment is prevalent in borrowing countries, it is bound to have an impact on the political sustainability of adjustment efforts in these countries. Doubts about political sustainability have always been there, of course, but they have probably intensified in recent months and are clearly leading creditors to discount the short-term gains which austerity is producing in such countries as Chile and Nigeria.

4. Pessimism about the external environment and scepticism about the political sustainability of adjustment efforts thus combine to call into question the viability of growth-oriented adjustment strategies in some middle-income countries. Every one can agree that Bolivia needs relief (and indeed may get it via the debt buy-back scheme), but opinions differ on whether less extreme cases (e.g., Costa Rica, Morocco, Ivory Coast, Ecuador, Nigeria) remain viable in the absence of favorable commodity prices or increases in concessional financing from official or private sources. The Debt Task Force (established following the July 8th discussion of the Policy Committee) will be reviewing the viability of current work-out plans in the more vulnerable countries. Pending completion of that work, we propose to defer reclassification of particular countries.

The Arrears Problem

4. Table 1 shows the continuous deterioration of the arrears position over the last two years.

Table 1: SUMMARY OF OVERDUE SERVICE PAYMENTS TO IBRD
(US$ million)

| | Arrears as of | | | | | |
|---|---|---|---|---|---|---|
| | Sep 4 1985 | Dec 5 1985 | Jun 3 1986 | Dec 2 1986 | Jun 2 1987 | Jul 2 1987 |
| Arrears 30-60 days | 41 | 55 | 85 | 158 | 203 | 155 |
| Arrears over 60 days | 41 | 50 | 118 | 142 | 245 | 317 |
| Total arrears over 30 days | 82 | 105 | 203 | 300 | 448 | 472 |
| No. of countries in arrears | 17 | 24 | 27 | 30 | 36 | 31 |

Source: Cashier's Department

The impact on the Bank of loan arrears depends upon the proportion of its loan portfolio that is affected; table 2 illustrates the potential magnitude of the problem. If it is assumed that those countries currently on non-accrual status plus those which are now expected to enter non-accural status in August, remain in arrears indefinitely, the effect of non-accrued interest and loan loss provisions would be to reduce the Bank's income by $335 million in FY88 and approximately $650 million in FY89. More generally, should borrowers accounting for only about 8% of the portfolio cease their debt service payments to the Bank, projected IBRD net income would turn negative.

Table 2: INTEREST LOSSES AND LOAN LOSS PROVISIONS UNDER CONTINUED ARREARS, AND EFFECT ON IBRD NET INCOME

| | | FY88 | FY89 |
|---|---|---|---|
| | | -(US$ million)- | |
| I. | Already Provisioning | | |
| | Nicaragua | 56 | 55 |
| II. | Already Non-Accrual Status | | |
| | Guyana | 22 | 22 |
| | Liberia | 9 | 34 |
| | Syria | 30 | 114 |
| III. | Likely Non-Accrual Status | | |
| | Peru | 154 | 293 |
| | Sierra Leone | 2 | 3 |
| | Zambia | 60 | 127 |
| IV. | Total Deductions | 333 | 648 |
| V. | Estimated Net Income Before Deduction | 1220 | 1427 |
| VI. | Deductions as % of Net Income (IV/V) | 27.3% | 45.4% |

Source: See Attachment 1.

6. Recent discussion of the arrears problem has distinguished (although this is not always easy) between those countries which can't pay and those which could but won't. For countries which can't pay and are IDA-eligible (e.g., Zambia), the current strategy is to provide quick-disbursing IDA funds in support of work-out programs that include timely servicing of IBRD (and IMF) debt. This strategy works if, and only if, a satisfactory adjustment package can be agreed with the country and a sufficient volume of net concessional funding can be mobilized. The viability of this strategy will obviously be enhanced if the current effort to raise additional funding for debt-distressed African borrowers

proves successful. Moreover, for this particular group of countries the Bank can readily afford to take a strong position against rescheduling proposals affecting IBRD debt, since the Bank as a whole (including IDA) can be a source of net finance if an adequate adjustment effort is made. Our position is much less strong in countries not eligible for IDA funding (e.g., Syria). It is these cases where defense of our preferred creditor status is likely to prove most difficult, which underlines the importance of our exposure guidelines (cf. paras.9-10 below).

7. Our tools for dealing with those which could but currently won't pay (Peru, Romania, Yugoslavia, etc.) are limited. The only current penalty is the suspension of disbursements after 75 days, and some countries are becoming adept at "flirting" with this limit. For countries where there are no undisbursed balances (Romania) or where net transfers are negative (Peru, Kenya, Yugoslavia, etc.) the penalty is not very effective. Hence we have had to seek the help of shareholders in mounting a "political effort" to convince non-payers that their action could hurt other borrowers and should not be viewed as a purely bilateral matter. For the year ahead, the Policy Committee may wish to consider what further steps in this area seem appropriate. Possibilities include (a) the establishment of an informal group of Executive Directors to address the problem and lobby those governments in arrears, and/or (b) a formal Board discussion of the problem. (This has been requested by several Directors, including the British.)

Exposure Management

8. There was some apprehension in the OVP discussion of the Creditworthiness Review that its diagnosis of increased vulnerability would lead the Bank into a more cautious, risk-averse posture vis-a-vis some of the heavily indebted borrowers. Most felt this would be precisely the wrong way to react, since it could undercut the adjustment efforts of borrowers and damage the Bank-borrower relationship. Hence, it could bring about the very debt-servicing problems that we want to avoid. This is agreed by all. However, while we would not wish to advocate retrenchment as a general response to the current problems, the management of IBRD exposure clearly needs careful attention over the coming years.

9. Diversification Guideline. One exposure guideline which could well be the focus of discussion during FY88 is the 10% limit ("flexibly applied") to exposure in any single borrowing country. In the most recent memorandum to the Board on this subject (M85-850 dated July 17, 1985), Management took the position that relaxation of the limit to, say, 12.5% would be acceptable in terms of the financial impact on the IBRD. The more serious concern was how to assure that a few countries did not preempt an excessive share of scarce lending authority in the period prior to agreement on a GCI. The current pressure on IBRD headroom adds a new urgency to this problem. If, for example, the Bank were to be asked to contribute \$2.5 billion of new money (i.e., net disbursements) to a \$10 billion financing package for Brazil in 1987-88, this would "use up" a very sizable part of the available headroom. Accordingly, pending the GCI, proposals for exceeding the diversification guideline will need to be

accompanied by a plan to deal with potential Board concerns over excess concentration of net disbursements in a single borrowing country.

10. "Share of Debt Service" Guideline. The other exposure management guideline that is likely to raise questions during FY88 is the one limiting IBRD exposure to 15% of the country's total debt service in those cases where preferred creditors as a group (i.e., including the Regional Banks and the IMF) account for more than 33%. We are already at or in excess of that guideline in a number of cases (listed in Attachment 2). Exceptions are allowed if the country is relatively creditworthy (IIc or above) or if debt service due the IBRD is less than 3% of the country's exports. But that still leaves a number of potential problems.

11. While the appropriate response will vary from case to case, one or two comments may be generally applicable. First, a special effort should be made in these countries to extract the maximum contribution from other sources of external finance. The new program of untied cofinancing by the Japanese ExIm Bank could prove especially useful in these cases, for example. Secondly, IBRD guarantees of later maturities of commercial bank loans may actually be preferable to direct loans in some of these cases, if the guarantees can be leveraged so as to improve the burden-sharing between the IBRD and commercial banks. (cf. para. 15-17 for more on guarantees).

12. Managing Exposure over the Medium Term. Exposure management questions may arise even if IBRD exposure falls within the established guidelines. The concern here is to avoid a rapid build-up of fast-disbursing loans over the next year or two without any clear plan for dealing with the fall off in net flows which inevitably arises once the acceleration of disbursements tapers off.

13. As with the exposure guidelines, the appropriate posture for the Bank will depend upon the particular circumstances of the borrower. However, it will generally be important to demonstrate that every reasonable effort has been made to keep the IBRD from taking on an excessive share of the increase in exposure over the next few years. Attachment 3 summarizes the present indications with regard to burden- sharing between the IBRD and other creditors in a sample of heavily indebted borrowers; it suggests that the Bank may be bearing considerably more of the burden (and the commercial banks less) than was initially envisaged.

14. Greater attention may also be paid to thinking through possible "fall-back positions." There are two related questions here. First, what should our strategy be if the bulge in policy lending in the second half of the 1980s does not result in a restoration of a more sustainable balance of payments position just before we exceed acceptable exposure limits (as is assumed in many lending strategy papers)? How can we plan to manage our net exposure over the medium term so as to position the IBRD better in the event that adjustment programs go off the tracks or the external environment worsens? Second, what should the strategy be in the situation in which non-payment of debt service to the IBRD is a serious possibility? How can net disbursements be managed so as to minimize the probability of default while not increasing our exposure further? The

Peru situation illustrates the point; disbursements had fallen below amortization payments due to poor project performance and poor policy-making in general, thus giving the authorities a clear incentive to cease service payments. The Region's proposal was to restructure the pipeline of undisbursed operations so as to permit more rapid disbursement that would effectively offset scheduled amortization payments due the IBRD. If successful, such a step would stabilize IBRD exposure while efforts are being pursued to put in place an adjustment program that the Bank can support.

Promoting Commercial Flows - B-Loans and Guarantees

15. The risks taken by the Bank are affected not only by the volume of exposure accepted but also by the form which that exposure takes. B-loan participations are a very risky technique for giving comfort to commercial banks if there is any serious risk of interruption in the servicing of interest payments. When this instrument was designed, the focus of attention was on rescheduling of principal payments.[1/] But a growing number of borrowers (including Brazil, Costa Rica, Ecuador, Ivory Coast, and Peru) are now not meeting scheduled interest payments, implying a reduced usefulness of the B-loan approach.

16. Two responses may be considered. One is simply to stop using B-loans in countries where there is thought to be any significant risk of interest arrears. We already refuse to participate in B-loans in concerted lending situations, and this posture could be applied to a wider group of borrowers (e.g., IIIa countries). Alternatively, the B-loan documentation could be amended to exclude the sharing of interest payments (thus permitting the borrower to remain current with the IBRD even if it is in arrears to commercial creditors). Such an amendment would obviously be resisted by the banks, who could be expected to charge that the IBRD is becoming less catalytic when the times call for a more positive catalytic role.

17. Hence it might make sense to link a tightening up of our posture on B-loans with an indication of greater willingness to use the IBRD's guarantee powers. At the moment, guarantees are very unpopular amongst some of the Bank's major shareholders, but it may be feasible to overcome this reluctance through a concerted "educational" effort. Some work along these lines has already begun, with the assistance of the Canadian authorities. The Policy Committee may wish to consider whether this effort ought to be broadened.

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1/ Since the B-loan program was approved by the Board in FY83, $297 million of Bank funds have been committed in direct participations in five countries (Cameroon, Colombia, Hungary, Thailand and Turkey), of which more than 80% has been concentrated in Hungary and Turkey. The corresponding commercial participation from these operations has amounted to slightly less than $2 billion through FY87.

## Countries on Non-Accrual Status and Loan Loss Provisioning: Potential Income Impact

| | Risk Rating | DOD FY87/a ($m) | Portfolio Share FY87 | FY88 Interest Impact ($m) | FY88 Loan Loss Provisioning ($m) | FY88 Total | FY89 Interest Impact ($m) | FY89 Loan Loss Provisioning ($m) | FY89 Total | FY90 Interest Impact ($m) | FY90 Loan Loss Provisioning ($m) | FY90 Total |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **I. Countries Currently on Provisioning Status** | | | | | | | | | | | | |
| Nicaragua | IIIc | 213.3 | 0.28 | 13.6 | 42.7 | 56.3 | 12.3 | 42.7 | 55.0 | 11.1 | 42.7 | 53.8 |
| **II. Countries Currently on Non-Accrual Status** | | | | | | | | | | | | |
| Guyana | IIIc | 83.1 | 0.11 | 5.5 | 16.6 | 22.1 | 5.0 | 16.6 | 21.6 | 4.4 | 16.6 | 21.0 |
| Liberia | IIIc | 127.1 | 0.17 | 9.3 | | 9.3 | 8.3 | 25.4 | 33.7 | 7.3 | 25.4 | 32.7 |
| Syria | IIIc | 419.1 | 0.55 | 30.4 | | 30.4 | 30.1 | 83.8 | 113.9 | 30.6 | 83.8 | 114.4 |
| Sub-total | | 629.3 | 0.83 | 45.2 | 16.6 | 61.8 | 43.4 | 125.8 | 169.2 | 42.3 | 125.8 | 168.1 |
| **III. Countries Most Likely to Go on Non-Accrual Status during FY88** | | | | | | | | | | | | |
| Peru | IIIc | 1026.7 | 1.35 | 154.0 /a | | 154.0 | 87.4 | 205.3 | 292.7 | 82.2 | 205.3 | 287.5 |
| Sierra Leone | IIIc | 9.8 | 0.01 | 1.5 /a | | 1.5 | 0.5 | 2.0 | 2.5 | 0.5 | 2.0 | 2.5 |
| Zambia | IIIc | 481.3 | 0.64 | 60.0 /a | | 60.0 | 30.7 | 96.3 | 127.0 | 28.2 | 96.3 | 124.5 |
| Sub-total | | 1517.8 | 2.00 | 215.5 | | 215.5 | 118.6 | 303.6 | 422.2 | 110.9 | 303.6 | 414.5 |
| TOTAL I + II + III | | 2360.4 | 3.11 | 274.3 | 59.3 | 333.6 | 174.3 | 472.1 | 646.4 | 164.3 | 472.1 | 636.4 |
| **MEMO:** | | | | | | | | | | | | |
| **IV. Countries with Significant Arrears Which Could Go on Non-Accrual Status during FY88** | | | | | | | | | | | | |
| Romania | IIIa | 1901.4 | 2.51 | 251.3 /a | | 251.3 | 122.8 | 380.3 | 503.1 | 106.6 | 380.3 | 486.9 |
| Yugoslavia \b | IIIa | 2955.4 | 3.90 | 343.6 /a | | 343.6 | 203.3 | | 203.3 | 192.4 | 591.1 | 783.5 |
| Sub-total | | 4856.8 | 6.41 | 594.9 | | 594.9 | 326.1 | 380.3 | 706.4 | 299.0 | 971.4 | 1270.4 |
| TOTAL I + II + III + IV | | 7217.2 | 9.5 | 869.2 | 59.3 | 928.5 | 500.4 | 852.4 | 1352.8 | 463.3 | 1443.5 | 1906.8 |

/a Includes interest reversed out from FY87.

/b Yugoslavia has been chosen as an example of a large and risky country having more arrears to the Bank ($93.4 million as of July 2, 1987) than any other country and with a large negative net transfer from the Bank.

NOTE: (a) Interest impact is based on position of arrears as of June 30, 1987 and does not take into account payments which may have been made subsequently to that date; interest estimates for FY88 for Peru, Sierra Leone, Zambia, Romania and Yugoslavia were provided by Controllers; all other interest estimates were taken from RM/FRS files.

(b) The following assumptions have been made:

| | Non-Accrual Date | Provisioning Date |
|---|---|---|
| Peru | 8/01/87 | FY89 |
| Sierra Leone | 8/15/87 | FY89 |
| Zambia | 8/15/87 | FY89 |
| Romania | 10/01/87 | FY89 |
| Yugoslavia | 2/01/88 | FY90 |

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20-Jul-87

## Countries in Excess of Bank Exposure Guidelines in 1987

| | Country Rating | Share of Total Debt Service to: IBRD | Share of Total Debt Service to: Preferred Creditors | Debt Service to IBRD as % of Exports | Share in IBRD Portfolio | Year IBRD & IDA Net Transfers Turn Negative |
|---|---|---|---|---|---|---|
| **I. Bank Exposure around or above 20% Preferred Creditor less than 33%** | | | | | | |
| Cameroon | IIc | 21.9 | 28.1 | 2.6 | 0.6 | Already |
| Tunisia | IIc | 19.6 | 23.2 | 5.1 | 1.2 | FY91 |
| **II. Bank Exposure above 15% Preferred Creditor around or above 33%** | | | | | | |
| Botswana | IIb | 39.3 | 61.9 | 2.2 | 0.2 | Already |
| Colombia | IIc | 27.6 | 33.6 | 8.3 | 4.7 | Already |
| Cote d'Ivoire | IIIb | 24.1 /a | 23.4 /b | 6.0 | 2.0 | FY90 |
| Fiji | IIa | 18.4 | 49.2 | 1.8 | 0.1 | Already |
| Honduras | IIIb | 22.8 | 39.7 /b | 5.7 | 0.6 | Already |
| India | IIb | 16.4 | 51.6 | 3.7 | 4.9 | After FY96 |
| Jamaica | IIIb | 14.2 /a | 45.9 | 6.0 | 0.8 | Already |
| Kenya | IIIb | 27.3 | 50.5 | 7.4 | 1.3 | Already |
| Mauritius | IIb | 20.0 | 63.6 | 3.1 | 0.2 | Already |
| Morocco | IIIb | 18.1 | 46.6 | 5.9 | 2.8 | FY90 |
| Peru /c | IIIc | 64.8 | 92.4 | 5.8 | 1.4 | Already |
| Romania | IIIa | 18.2 | 32.8 /b | 4.4 | 2.5 | Already |
| Swaziland | IIc | 25.7 | 48.6 | 1.6 | 0.1 | Already |
| Thailand | IIa | 22.3 | 47.0 | 3.4 | 3.9 | Already |
| Turkey | IIIa | 19.9 | 31.5 /b | 5.6 | 7.1 | FY88 |
| **III. Countries with Significant Levels of IBRD Exposure** | | | | | | |
| Indonesia | IIc | 17.1 | 17.5 | 4.4 | 7.8 | FY89 |
| Malawi | IIIb | 11.3 | 49.3 | 4.0 | 0.1 | After FY96 |
| Mexico | IIIb | 7.8 | 11.5 /b | 4.5 | 8.3 | FY88 |
| Nigeria | IIIb | 16.7 | - | 4.7 | 2.9 | After FY96 |
| Paraguay | IIIb | 25.8 | - | 7.6 | 0.5 | Already |
| Philippines | IIIb | 16.2 | 27.6 | 5.6 | 4.4 | Already |
| Yugoslavia | IIIa | 13.2 | 30.7 | 2.9 | 3.9 | Already |

/a Share of IBRD DOD to total DOD.

/b Preferred Creditors includes only IBRD, IDA,& IMF

/c Note that these calculations were made when Peru was adhering to its earlier policy of restricting debt service to 10% of goods and services and giving preference to multilaterals (IBRD and IDB) and of not repaying the IMF. The IBRD share of scheduled debt service would be much lower.

Source: Creditworthiness Review, April 1987.
FRS - 22Jul87

**Burden Sharing Implicit in Recent Strategy Papers: Shares of Net External Finance Proposed**

| | % Shares | |
|---|---|---|
| | 1987-90 | 1987-95 |
| Nigeria (CSP, May 27, 1987) | | |
| IBRD | 61.1 | 98.2 |
| Commercial | -29.4 | -67.9 |
| IMF | 0 | 0 |
| Other | 68.3 | 69.7 |
| Chile (SAL III IM, June 29, 1987) | | |
| IBRD | 56.8 | |
| Commercial (incl. Debt. Conversion) | 45.9 | |
| IMF | -96.2 | |
| Other | 93.5 | |
| Uruguay (CPP, June 30, 1986) | | |
| IBRD | 81.8 | 27.4 |
| Commercial | 55.3 | 34.1 |
| IMF | -165.9 | -61.1 |
| Other | 128.8 | 99.6 |
| Colombia (Baker Paper, May 14, 1986) | | |
| IBRD | 21.6 | 17.4 |
| Commercial | 52.5 | 67.0 |
| IMF | 0 | 0 |
| Other | 25.9 | 15.6 |
| Turkey (CASB, Jan. 9, 1987) | | |
| IBRD | 50.6 | |
| Commercial | 49.9 | |
| IMF | -14.7 | |
| Other | 14.2 | |
| Philippines (Memo for ERL, Dec. 22, 1986) | | |
| IBRD | 42.4 | |
| Commercial | -11.2 | |
| IMF | -27.1 | |
| Other | 95.9 | |

| | % Shares | |
|---|---|---|
| | 1987-90 | 1987-95 |
| **Brazil** (DCB, Feb. 6, 1987) | | |
| IBRD | 33.4 | |
| Commercial | 71.5 | |
| IMF | -23.0 | |
| Other | 18.0 | |
| **Argentina** (DCB, March, 1987) | | |
| IBRD | 44.9 | |
| Commercial | 30.8 | |
| IMF | -0.2 | |
| Other | 24.5 | |

Note: These implicit burden sharing figures must be taken as only rough indications. They are derived from a variety of Regional strategy papers and other documents; they may be based on differing definitions for creditor categories and concepts for total debt (we tried to use the broadest definition possible, i.e., including short-term and private non-guaranteed debt where possible); and sometimes use different base periods (hence different relative exchange rates).

Note also that not all of the lending levels proposed were approved by Senior Management.

FRSRM
20Jul87

THE WORLD BANK/INTERNATIO' FINANCE CORPORATION

# OFFICE MEMORANDUM

DATE: April 8, 1987

TO: Mr. Barber B. Conable

FROM: Moeen A. Qureshi and Ernest Stern

SUBJECT: Creditworthiness Review

1. We have just completed our annual review of the Bank's loan portfolio. The full Report was discussed by the Operational Vice Presidents on March 18th and by the Financial Policy Committee on March 19th. The minutes of the latter meeting are attached for your reference. We would like to call your attention to some of the highlights of the Report and of the discussion which it triggered.

2. Much of the Report is devoted to a description of the riskiness of the Bank's loan portfolio. Countries are rated using a methodology that has been refined over the years and which appears to produce results which the senior Operations managers find generally plausible. The classification of the loan portfolio into the various categories of risk did not show much change this year as compared to last year. About 60% of IBRD loans are to countries that are considered to have high risk of debt-servicing difficulties, of which half (i.e. 30% of total loans) are what we call "conditionally creditworthy". That means we only lend if the country has in place an effective stabilization and adjustment program.

3. While the risk classification has not changed materially over the past year, the Bank's vulnerability to debt servicing difficulties has, the Report argues, increased substantially. Increased vulnerability is evident in three areas:

- first, the IBRD's share of borrowing countries' total debt service has gone up sharply, partly because of increased IBRD lending and partly because of exchange rate changes which particularly affect debt service due the IBRD. One indicator of this exposure is the ratio of debt service owed the Bank as a percentage of a borrowing country's export earnings. Since 1980 this ratio has (on average) tripled in the Baker list of countries and quadrupled in developing countries as a whole.

- second, IBRD net transfers are turning negative for an increasing number of borrowing countries. If a country finds itself in a liquidity squeeze, it is a natural temptation to pay only those creditors with whom it has a favorable net transfer position.

- third, the IBRD's financial ratios have declined significantly, again partly because of growth and partly because of exchange rate changes. (You have received a separate note on our concerns relating to Bank capital adequacy.) Net income, while large in absolute terms, remains vulnerable to protracted arrears. Should borrowers accounting for about 6% of the current portfolio fall into this position, the Bank's projected net income would be wiped out.

What Can Be Done?

4. The discussion of this year's Report revealed widespread agreement about the riskiness of the position in which the Bank finds itself. Where differences arose was in the discussion of what, if anything, the Bank can (or should) do in response to this diagnosis that it isn't doing already.

5. Exposure management. There was some aprehension in the OVP discussion that the diagnosis, if accepted, would lead the Bank into a more cautious, risk-averse posture vis-a-vis some of the heavily indebted borrowers. Most felt this would be precisely the wrong way to react, since it could undercut the adjustment efforts of borrowers and damage the Bank-borrower relationship. Hence it could bring about the very debt-servicing problems that we want to avoid.

6. In fact, the Report does not advocate retrenchment as a general response to the problem of high relative exposure. What it does do is underline the importance of a reasonable sharing of financing burdens between the IBRD and other sources of finance, particularly in a list of eleven countries where IBRD exposure is especially high. At the OVP meeting doubts were expressed about the practicality of doing much more to influence the financing package than we are already doing.

7. Increasing net transfers. The Report cites a number of ways in which the Bank could alter the net transfer prospects for individual countries or groups of countries. One way is to increase the share of fast-disbursing loans; another is to shift part of the disbursements (temporarily) to other lenders. The techniques were not discussed in any depth. The discussion focussed instead on whether --or in what circumstances--it would make sense to try to change the level of projected net disbursements and net transfers.

8. Steps taken to increase net flows to borrowers will typically increase IBRD exposure in the longer run. While debt-servicing risks may be diminished in the near-term, they may be increased in later years. Hence the attractiveness of steps taken to increase net flows depends very much on one's judgment regarding the borrowing country's capacity to service debt in the future. It is a gamble which wins if the borrower's creditworthiness improves, but which increases the scale of potential loss if it does not.

9. Some of those at the OVP meeting were quite sceptical about the wisdom of further increasing the share of fast-disbursing loans because the share already exceeds 50% in a number of instances. Moreover, they have seen that the relief bought by an increased share is only temporary, and tends to be followed by even greater pressure to "do something" to offset downturns in net flows. At the FPC meeting the main emphasis was put on achieving a close linkage between steps designed to increase net flows and steps designed to improve borrowers' future creditworthiness.

10. **Strengthened IBRD finances**. At both meetings there was a strong appeal to raise the consciousness of shareholders regarding the increased risks that the Bank is taking on. Shareholders need to understand that the Bank cannot take on ever increasing levels of risk without added capital backing. One member of the FPC went so far as to urge that the Bank decline to participate in any sizeable "new money" packages in Baker list countries until the United States agrees in principle to a GCI. Others felt that a GCI, while obviously desirable, would not by itself reduce the risks faced on the lending side. These risks could be addressed through Bank support for well-designed adjustment programs, although a few members expressed the view that new approaches to the debt situation (e.g. LaFalce proposals) might prove to be necessary as well.

11. We have, as you know, had informal discussions with Executive Directors regarding the structure of IBRD loan charges. In these sessions the primary emphasis was placed on the "credit" risks facing the Bank. We argued that projected net income could well be more than adequate to cover "market risks" (i.e. exchange rate and interest rate changes), but that it might not enough to cope with "credit" risks (i.e. non-accrual or provisioning for loans not being serviced).

12. As a means of informing the Directors about the Bank's increased risk-taking and increased vulnerability, we could arrange a follow-up set of informal meetings with Directors shortly after the Development Committee meeting. Such meetings could "raise the consciousness" of Directors on these issues without there having to be a formal Board or Committee of the Whole meeting.

13. We recommend that, once you have had a chance to examine the minutes and the attached Report, we meet to discuss whether to proceed with informal briefings and, if we do proceed, what line we ought to take.

Attachment

cc: Mr. Shihata
Mr. Thahane

Record: April 3, 1987

# FINANCIAL POLICY COMMITTEE

## MINUTES OF MEETING OF THURSDAY, MARCH 19, 1987

Members Present: Messrs. Qureshi (Chairman), Asser, Gue, Hasan, Inakage, Paijmans, Rotberg and Wood.

Also Present: Ms. Hadler and Messrs. Asanuma, Baneth, Baudon, Jansen, Lysy, McPheeters, Mistry and Talvadkar.

## I. 1987 Review of Country Creditworthiness and Bank Loan Portfolio Issues, FPC/87-4.

1. The Chairman opened the meeting by asking for a summary of the OVP discussions on the same subject held on March 18, so as to brief the FPC members on the essential reactions of the Operations Complex to the report. A member then reported that the key views expressed during the OVP meeting in reaction to the deteriorating trends pointed out in the report, were:

(a) That the Bank should not consider retrenchment in lending as a viable option;

(b) That the trade-off between the financial strengthening of the institution and the "optimal" use of Bank funds would be difficult;

(c) That the increase in Bank exposure in selected countries should not be viewed in a static sense; a number of countries especially in Latin America were making good adjustment efforts and that the high exposure had been accompanied by increased Bank involvement in policy dialogue on macro and sector management issues. In specific cases, there had been deliberate decisions to increase Bank exposure beyond "norms";

(d) That while increased burden-sharing with other sources of funding could be explored, there were real constraints imposed by our limited leverage with commercial banks and inability to use guarantees; and

(e) The option of using quick disbursing assistance to manage debt service profile is already being used to the limit in many cases; further increases will lead to severe volatility in future disbursements.

The same member noted that the OVP meeting had concluded that the country ratings in the report were generally appropriate. OPC members had also expressed an overwhelming concern about the fast deteriorating global environment and the increasing risk which the institution confronted.

2. At the Chairman's request, another member summarized the purpose and broad conclusions of the paper. He first stated that the report had a "stock-taking" objective for the institution as a whole. From that point of view, the central message is very sobering: the Bank has now a high risk portfolio and is becoming increasingly vulnerable to protracted arrears in the servicing of its loans. He illustrated this by mentioning that the ratio of Bank debt service to exports has increased three or fourfold in many countries over the recent past. He then said that the second objective of the report was to point out that the Bank does have some capacity to manage its rising exposure. This could in particular be achieved through: (a) increases in the share of fast-disbursing operations in the lending program whenever possible and desirable; (b) a liberalization of repayment terms; and (c) changes in the loan charge structure to better withstand increased risk of non-accruals from small borrowers. However, the same member noted that the first action can reduce our exposure risk in the short-run only (by temporarily raising the level of net transfers), but would then lead to higher exposure levels in the future. In that sense, restored growth and improved fiscal/current account balances in borrowing countries will be crucial to avoid unmanageable Bank risk in the medium-term. He then concluded by saying that despite the "exposure management" tools it can develop, the Bank is in an increasingly difficult situation. The need for a General Capital Increase thus becomes paramount to avoid severe impairment of the Bank's capacity to absorb potential shocks in the future.

3. Before opening the discussions, the Chairman stated that in his opinion, the paper served several essential purposes in the present difficult environment: first, it triggered a Bank-wide debate and highlighted the riskiness of the situation; second, it put things in perspective by demonstrating that, contrary to what a purely static analysis would indicate, an increase in Bank's exposure in the short-run could ultimately reduce the overall risk to the institution if adjustment programs in borrowing countries are carefully designed and implemented; third, it showed that the problem of burden-sharing was real and; fourth, it provided additional evidence that a GCI will be a necessary part of the answer, even though it would not reduce the risk factor itself, but rather allow the Bank to withstand it better.

4. The Committee then focused its discussion on the following points:

(a) The lack of a fully satisfactory solution in the present world economic environment to deal with the deteriorating situation of the portfolio and the extent to which a GCI would be instrumental in giving the Bank additional strength and leverage to adjust to the increased risk factor; and

(b) The specific proposals made in the report with respect to the management of Bank exposure (country-specific limitations in lending and total exposure; the use of policy-based, fast-disbursing operations to manage the debt service profile; optional new Bank lending terms; and improved burden-sharing with other creditors).

5. *The need for a broader response to an increasing risk and the potential contribution of a GCI*. One member stressed that the main conclusion he drew from the report was the absence of a satisfactory solution at hand to deal with the increasingly difficult situation faced by the Bank. He felt that a GCI, though desirable, would not by itself be an adequate answer, and that a conflict situation is gradually arising between the Bank's need to protect its financial situation and the need to meet its basic mandate by assisting its member countries. Another member supported this by adding that the world economic environment was difficult and could deteriorate further, and that retrenchment by the Bank at this point could increase the likelihood of defaults rather than reduce it; he agreed that a GCI would not be sufficient, although it would definitely have the two major advantages of increasing financial flows to developing countries and allowing the adjustment process to continue. The same member pointed out that in his view the real issue was the debt problem, and how we could tackle it. He felt that the Bank should fully acknowledge the variability of situations among debtor countries and not put excessive hope in a quick resumption of voluntary lending by the commercial banks. The Chairman then stated that a GCI was absolutely essential and would greatly contribute to restoring the Bank's ability to cope with the deteriorating situation. It would bring back the Bank's financial ratios to more satisfactory levels and allow the institution to continue to meet its normal obligations by offsetting the constraints that sharp exchange rate movements will soon impose on our aggregate borrowing and lending capacity.

6. A member then said the situation had become so serious that the Bank should refuse to participate in any new concerted lending package unless it receives assurances by the major shareholders that a GCI will be implemented soon. In his opinion, the combination of slow growth prospects of the world economy with deteriorating Bank financial ratios and "headroom" was unprecedented and justified such a strong stance regarding a GCI. The Chairman replied that these were certainly valid causes for concern but that he did not see a drastic deterioration in either the situation of borrowing countries or the Bank portfolio itself over the last year. He noted that none of the underlying trends were new, but rather that we were one year farther along the path that we have been on for some time. He reiterated that the recent deterioration in financial ratios stemmed almost exclusively from exchange rate movements, i.e., the decline of the US dollar vis-a-vis other major currencies. A member emphasized, however, that what was new was the convergence at one time of several key adverse trends.

7. Several members expressed the view that the past year had been the fifth consecutive one of declining creditworthiness for our borrowers, despite the adjustment measures undertaken by a number of them. The cumulative effect of this steady degradation, which is likely to continue given the expected evolution of the terms of trade during the coming year, will ultimately take its toll if nothing is done to alleviate the excessive burden that debt service puts on several countries. They thought that the Bank should: (a) increase its reserves as quickly as possible; and (b) seriously consider a broad new approach to the global

problem of LDC debt and debt service. The Chairman also noted that the issue of net transfers is indeed a real one, and that the Bank should be very concerned about it. While the maintenance of positive net transfers over time was neither sustainable nor a realistic position, it would be equally wrong to ignore this aspect at a time when members countries' external positions were so heavily burdened.

8. Specific proposals with respect to management of Bank exposure. The discussion then turned to the specific recommendations made in the report to improve the management of Bank exposure. A broad consensus emerged in the Committee on the following points:

(a) The Bank should maintain a degree of flexibility in managing exposure limits and not be excessively bound by formal ratios; this would be justified in particular if a country is pursuing a high quality adjustment program. Retrenchment in lending, especially to the highly indebted countries, could prove to be a more risky proposition than continued support through increased capital flows, provided sound economic policies are being implemented; the risks associated with this proposition were fully acknowledged by Committee members, who agreed, nevertheless, that the Bank should preserve the option to pull out or retrench in certain specific cases;

(b) The liberalization of lending terms is a sound proposition which could benefit both the borrowers and the Bank, but further detailed work needs to be done before a fully operational proposal can be presented. In addition, the Bank should be sensitive to the timing of this proposal in relation to the discussions on the GCI; premature adoption of a liberalization policy could undermine the GCI process itself. A member pointed out that this liberalization would not have much effect in the short run; it was noted, however, that even modest positive effects are worth considering, particularly during the interim period preceding the implementation of the GCI; and

(c) Portfolio concentration in high risk countries could be alleviated in part, should the Bank decide to offer more attractive terms or better tailored products to its most creditworthy borrowers. This would increase their interest in borrowing from the Bank.

9. With respect to the Bank's vulnerability to arrears and the possible measures the Bank could take to avoid a significant deterioration in net income, the Chairman asked that reference to a contingent charge be dropped for the time being, pending conclusion of the on-going discussions on the structure of loan charges.

10. In conclusion, the Chairman stated that the discussion had highlighted the urgency of a GCI and increased the Bank-wide awareness of risks to which the Bank is increasingly exposed. He hoped that this awareness would be reflected in our policies and approaches: (a) on the operational side, our criteria for lending should remain as strict as possible since the quality of the programs we support is the key to restoring a viable situation; and (b) on the financial side, the Bank should be more sensitive than ever to financial policies and ratios and more broadly to its image in the financial markets; it should also be adequately prepared to deal with crisis situations should they arise.

## METHODOLOGY FOR ASSESSING AND CLASSIFYING COUNTRY RISK

1. As has long been recognized, there is no one analytically correct approach for assessing country risk given the complexity of the economic, political, institutional, and behavioral factors that have to be considered. Thus, our approach to country risk analysis remains highly judgmental, and has relied primarily on the broad range of information available in CPPs, country economic reports and other internal Bank economic analysis. We also took into account country-specific information and analysis from a variety of external sources.[1/] However, to facilitate inter-country comparisons and therefore the classification of country risk, we have adopted a structured approach to synthesize and interpret the quantitative and qualitative information contained in both internal and external sources.

2. The analysis has been undertaken for all countries for which lending was proposed in the FY87-91 Regional lending programs submitted in November 1986, including those countries which remain in the graduation phase, namely the Bahamas, Barbados, Cyprus and Oman. In total, this includes 58 borrowers (including the Caribbean Development Bank), which accounted for 94.5% of the Bank's loan portfolio at the end of FY86 and, on the basis of current lending plans would account for over 94.5% by FY91. The balance of the portfolio is held by past Bank borrowers and former blend countries. Past Bank borrowers (including *inter alia* Iran, Iraq, Nicaragua and Seychelles), most of which have graduated from Bank lending, were reviewed only superficially to ascertain whether the risk ratings that they have received in previous reports are still valid (see Table 1, attached, for a list of their ratings). In addition, the analysis was undertaken for those former blend countries where Bank lending has ceased because of a deterioration in their creditworthiness and which also pose some risk to the portfolio (namely, Bolivia, Ghana, Guyana, Liberia, Sudan, Tanzania, Zaire and Zambia). The analysis was also undertaken to a lesser extent for six former blends whose portfolio shares are smaller (Guinea, Malawi, Mauritania, Senegal, Sierra Leone and Togo). There are, further, three former blend countries which are not considered to pose a significant risk to the portfolio and which have not been analyzed (Bangladesh, Ethiopia and Madagascar). With the exception of Malawi, the former blend countries are all rated IIIc (Table 2, attached, identifies all IIIc countries with IBRD loans outstanding). Trinidad and Tobago is a past borrower and has been excluded from this report. Although not included in the November 1986 lending programs, Venezuela and Paraguay have been reviewed in the expectation that lending will occur in these countries in the near future. The only borrower not covered is the International Finance Corporation, which is excluded from all portfolio estimates in this report.

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1/ Among these are papers and reports prepared by the IMF, BIS, and major commercial banks.

Time Horizon of Analysis

3. Our country assessments and our system for ranking and classifying country risk focus on long-term debt servicing prospects. However, we believe that some attention to short-term prospects is also important for two reasons. First, the Bank cannot be absolutely certain of being able to keep its preferred creditor status at all times, especially in countries in severe liquidity difficulties and where its exposure, singly or jointly with other preferred creditors, is high. Second, the reluctance of commercial creditors to maintain their exposure in countries with severe liquidity problems has exacerbated these problems, putting the Bank's ability to insulate itself from debt servicing difficulties at even greater risk. Since the Bank's policy is not to reschedule its loans, the capacity of the country to meet its Bank obligations in the short term is therefore of concern, even when the country in question may be fully capable of meeting its Bank obligations in the longer term. Also, sustained non-payment of Bank loans in the short term could have adverse consequences for the market standing of the Bank. Finally, actions which a country takes to deal with its short-term problems can either introduce or remove significant distortions in the economy (e.g, exchange and import controls), with important consequences for the country's longer-term growth and creditworthiness prospects.

4. In light of these considerations, our country assessments are explicitly divided into assessments of debt service capacity in the short term (next 2-3 years) and in the longer term. For instance, countries with debt servicing problems in the next two to three years may have a stronger debt servicing capacity than indicated by their short-term position, or alternatively may experience recurring, or even increasing problems in the longer term. Conversely, some countries may currently enjoy a strong liquidity position, but because of structural and/or institutional problems, may have a much weaker capacity to service debt in the longer term.

Assessing Short-Term Debt Service Capacity

5. In assessing the likelihood of debt servicing problems over the next two to three years we first consider a country's vulnerability to balance of payments problems, 2/ based on an evaluation of its recent

2/ Defined broadly as a situation where the supply of foreign exchange generated by exports, capital inflows, and other autonomous transactions may fall short of the demand for foreign exchange to pay for imports, external debt service, and other autonomous transactions to the point where a country has to draw down its reserves well below "normal" working balances, engage in compensatory borrowing, including IMF borrowing, deflate demand for imports, incur arrears on its loans, or a combination of these actions.

and projected balance of payments. Subsequently, we make a judgment as to whether these balance of payments problems would lead to debt service arrears and rescheduling, taking into account a country's adjustment capacity and the magnitude of its debt service burden.

6. In making these assessments, we initially review country performance against quantitative indicators of exchange rate, trade and monetary policies, external liquidity and debt service burden. This quantitative analysis is complemented by a qualitative analysis of the capacity of the country's economic managers to respond to balance of payments problems; the degree of compressibility of imports; the effects of ongoing debt rescheduling efforts; and, for some countries, relevant political developments which could affect short term prospects. For those Bank borrowers who are also significant borrowers from commercial banks and whose ability to repay existing debt depends on the willingness of banks to maintain if not increase their country exposure, market perceptions of country creditworthiness as reflected, for example, in the country risk rankings of Institutional Investor is also evaluated.

Assessing Long-Term Debt Service Capacity

7. Our analysis of a country's creditworthiness in the longer term is focused on its ability to repay outstanding as well as future external loans while maintaining an "acceptable" level of per capita consumption over time. Given the longer time horizon for these assessments, we give greater emphasis to factors affecting the fundamental or intrinsic creditworthiness of a country rather than the cash flow or liquidity measures which are more appropriate for short-term analysis.

8. A broad range of quantitative and qualitative factors are considered in our assessments of long-term debt service capacity. The quantitative analysis reviews past economic performance as well as trends in the balance of payments and other debt indicators as projected by the Region.[3/] Countries are compared against a number of quantitative measures of performance, derived from key analytical relationships of the growth-cum-debt theoretical framework. These measures include indicators of the level of development and growth performance, export performance, resource mobilization and external debt burden.

9. The assessment based on the preceding quantitative analysis is complemented by a structured evaluation of various aspects of a country's development situation which are considered to have some bearing on its long-term creditworthiness, but which are not adequately reflected in historical data. To broaden the basis for these fundamentally subjective assessments, we draw on CPPs and economic reports and on country performance assessments undertaken annually in connection with the 5-year lending program.

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3/ A practical limitation on using such projections for cross-country comparison is that they are not strictly comparable because they are prepared at various points in time and hence are not based on a consistent set of external assumptions. Also, recent projections for a number of countries are not available.

10. Our qualitative assessments consider the following determinants of long-term debt service capacity:

a. Quality of development management. This includes an overall evaluation of a country's long-run growth strategy; its development program and investment priorities; resource mobilization and allocation policies; structural adjustment/improvement policies; quality of the government's financial and external debt management; economic planning and programming expertise; quality and effectiveness of major economic policy makers; and administrative efficiency and management of public enterprises.

b. Basic economic factors. Assessment of a country's natural resource endowment, human resources and entrepreneurial skills, and economic infrastructure.

c. Economic and trade structure. Assessment of the strengths and weaknesses of a country's productive and trade structure as they affect its long-term ability to service external debt, focusing on the present degree of diversification of production and the prospects for efficient structural change; export orientation of the economy, diversification of exports and markets; extent of import dependence and possibilities of efficient import substitution; and size of the debt burden.

d. Political and social factors. Evaluation of relevant political and social factors which could significantly affect a country's future economic performance. Political assessments, drawn primarily from CPPs, focus on the commitment and ability of the political leadership to carry out effective development programs and policies.

Risk Classification System

11. Our assessments of debt service capacity in the short term categorizes countries into five risk groups: very low, low, moderate, high, and very high risk of debt servicing problems in the short term. Countries are also categorized into five risk groups based on our assessments of debt service capacity in the long term: very low, low, moderate, high, and very high risk of debt servicing problems in the long term. The separate assessments of short- and long-term debt service capacity are then merged into an overall creditworthiness assessment with approximately twice as much weight given to long-term as against short-term debt service capacity. Further adjustments are made in the overall assessments in light of other judgmental factors not previously considered and in order to ensure better internal relativities in overall risk position between countries. Based on these overall assessments, countries are classified into the various risk groupings used since the 1982 Creditworthiness and Portfolio Review. It should be pointed out that while a structured approach is used to assess country creditworthiness, the risk categories cannot be described in terms of specific values or ranges of values of one or even several factors or indicators. Our

overall assessments are based on the multiplicity of factors described above and weak performance on some could be more than compensated for by a strong showing on the others. For example, countries with the highest debt service and debt-to-exports ratios are not automatically consigned to the bottom risk categories if their economic management and policies were such as to enable them to reduce these ratios overtime to more manageable levels. Conversely, countries with the lowest debt indicators are not necessarily considered a low risk if they face serious structural, institutional, or political problems.

12. The various risk categories are described below together with the recommendations for the Bank's lending posture.

Category I - Minimal Risk of Debt Servicing Difficulties

This category includes countries with a very low probability of debt servicing difficulties both in the short term and in the longer term. Most of the Bank's past borrowers, which are now developed economies but still have some outstanding Bank debt, are included in this category.

Category II - Some Risk of Debt Servicing Difficulties

This category covers a wide range of countries which in relation to Category I countries are considered to have a low to moderate probability of debt servicing difficulties in either the short or long term. All of them are therefore considered relatively good risks, although at the lower end of the Category II scale, a few countries could become marginally creditworthy if external economic conditions deteriorate and especially if adjustments in domestic policies are not sustained. Since Category II is a miscellaneous assortment of countries, it has been divided broadly into three groups.

Category IIa includes coutries considered to have a low probability of debt servicing problems in the short as well as longer term. In relation to their level of development, Category IIa countries have highly favorable debt indicators. Historically, they have performed impressively on a sustained basis, with high long-term growth rates, high marginal savings rates, and high returns on investment. They are well managed and are projected to maintain a sound balance of payments and debt position. Countries classified as IIa are considered fully creditworthy for Bank lending. Bank lending to these countries could be constrained by other criteria (per capita income, portfolio share, etc.).

Category IIb includes countries with short-term prospects comparable to those of IIa countries but with a somewhat less robust longer-term outlook either because of longer term political uncertainties or because of structural and institutional constraints. This category also includes countries with longer-term prospects comparable to those of IIa countries but with a somewhat

less favorable, but still adequate liquidity position. Countries classified as IIb are also considered fully creditworthy for Bank lending.

Category IIc includes countries with favorable liquidity indicators but whose longer-term creditworthiness prospects are not as strong as those of IIb countries because of their more serious structural and institutional problems. Countries with longer-term prospects broadly similar to those of some IIb countries but with a less favorable liquidity position have also been rated IIc. For countries classified as IIc, country creditworthiness is not a constraint to Bank lending. However, given the downside risks facing countries in this category, the situation should be monitored.

Category III - High Risk of Debt Servicing Difficulties

This general category includes all countries considered highly likely to experience debt servicing difficulties in the short term and/or in the longer term. Category III countries are also divided into three groups.

Category IIIa consists mainly of countries facing serious liquidity problems but with fair to good global prospects, and with a continuation of the stabilization and adjustment programs that they are pursuing, these countries are expected to be creditworthy over the longer term. However, the downside risks to both the short-term and longer-term prospects of these countries remain significant. Under an adverse global environment characterized by higher international interest rates and weak markets for developing country exports, most of these countries are likely to experience serious debt servicing problems in the longer term as well as in the short term. Other Category IIIa countries include borrowers whose short-term position is much better than that of the preceding IIIa countries but whose longer-term prospects are relatively less promising because of structural, institutional, and/or political factors. The serious short-term difficulties confronting most Category IIIa countries and, for some of them, the prospect of recurring difficulties over the next several years should be taken into account in determining the level of future Bank lending. As a general rule, following the decisions taken by Senior Management in the review of recent CPPs, the level of Bank lending needs to be explicitly linked to progress being made by these countries in carrying out stabilization and adjustment measures. For the Category IIIa countries which are considered to pose a signficant direct financial risk to the Bank's loan portfolio, country performance and prospects need to be followed closely.

Category IIIb includes countries which have serious liquidity problems and a significantly weaker longer-term creditworthiness, relative to Category IIIa countries, on account of their more limited management and institutional capacity and less diversified

economic and export structures. The economic prospects of some of these countries are clouded by longer-term political uncertainties. A majority of them have initiated stabilization and/or structural adjustment programs. Bank lending to Category IIIb countries is preconditioned on actions being taken by these countries to resolve their immediate debt servicing problems as well as to improve their long-term creditworthiness. Country performance and prospects for the Category IIIb countries which pose a significant direct risk to the Bank's portfolio are closely monitored.

Category IIIc includes countries which have serious liquidity problems and, compared to Category IIIb countries, have a higher risk of recurring debt difficulties over the longer term because of more severe structural problems and/or poorer management. Category IIIc also includes countries which are not creditworthy for Bank lending because of unsettled political conditions, including situations in which governments are unwilling to service their sovereign debt obligations. Former blend countries which are no longer considered creditworthy for Bank lending are also included in Category IIIc. Given the lack of creditworthiness of Category IIIc countries and their uncertain prospects for improvement, a continued suspension of Bank lending to these countries is warranted. In addition to this suspension, monitoring of the economic situation in Category IIIc countries which pose a significant direct threat to the Bank's portfolio on account of their past borrowings in also warranted.

**Table 1**: LOANS OUTSTANDING TO PAST BORROWERS AND REGIONAL BORROWERS, END-FY86

| | DOD ($m) | Portfolio Share (%) |
|---|---|---|
| **Category I** | | |
| Australia | 39.0 | 0.1 |
| Finland | 5.1 | 0.0 |
| Iceland | 18.0 | 0.0 |
| Ireland | 50.3 | 0.1 |
| Japan | 121.1 | 0.2 |
| New Zealand | 0.1 | 0.0 |
| Norway | 5.4 | 0.0 |
| Spain | 86.0 | 0.1 |
| **Category IIa** | | |
| Greece | 155.4 | 0.2 |
| Singapore | 63.8 | 0.1 |
| Taiwan | 132.6 | 0.2 |
| **Category IIc** | | |
| Gabon | 11.7 | 0.0 |
| Israel | 59.3 | 0.1 |
| Trinidad & Tobago | 36.9 | 0.1 |
| **Category IIIa** | | |
| Venezuela | 35.0 | 0.1 |
| **Category IIIb** | | |
| Caribbean Dev. Bank | 36.8 | 0.1 |
| **Category IIIc** | | |
| EAC | 7.5 | 0.0 |
| Iran | 343.6 | 0.6 |
| Iraq | 60.1 | 0.1 |
| Nicaragua | 186.0 | 0.3 |
| W. African Region | 25.9 | 0.0 |

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**Table 2**: LOANS OUTSTANDING TO IIIc COUNTRIES, END-FY86[a]

| | DOD ($m) | Portfolio Share (%) |
|---|---|---|
| E. Africa | | |
| EAC | 7.5 | 0.0 |
| Ethiopia | 52.6 | 0.1 |
| Madagascar | 29.8 | 0.1 |
| Sudan | 44.7 | 0.1 |
| Tanzania | 284.5 | 0.5 |
| Zaire | 47.4 | 0.1 |
| Zambia | 420.6 | 0.7 |
| W.Africa | | |
| Ghana | 129.1 | 0.2 |
| Guinea | 60.6 | 0.1 |
| Liberia | 116.2 | 0.2 |
| Mauritania | 61.8 | 0.1 |
| Senegal | 101.6 | 0.2 |
| Sierra Leone | 9.1 | 0.0 |
| Togo | 2.0 | 0.0 |
| W.African Region | 25.9 | 0.0 |
| EMENA | | |
| Iran | 343.6 | 0.6 |
| Iraq | 60.1 | 0.1 |
| Lebanon | 38.9 | 0.1 |
| LAC | | |
| Bolivia | 228.0 | 0.4 |
| Guyana | 72.7 | 0.1 |
| Nicaragua | 186.0 | 0.3 |
| Peru | 847.4 | 1.4 |
| S.Asia | | |
| Bangladesh | 59.1 | 0.1 |

[a] Includes former Bank borrowers, former blend and enclave countries.

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## PORTFOLIO PROJECTIONS AND SENSITIVITY

### Methodology and Assumptions

1. Projections of the Bank's loan portfolio in this report have been based on projected disbursements and service payments for loans approved through end-September 1986, on country lending programs in the Operations MIS for FY87-91 [1/] and on an assumed nominal 3% annual increase in lending commitments beyond FY91. The projections are based on the maturity and grace periods appropriate for each country and estimated disbursement profiles of Bank loans for the various lending instruments. Interest charges assumed for the projection period are taken from the draft FY88 Mid-Year Budget Review.[2/] The projections are considered reasonably reliable through FY94, since until that time they are based largely either on lending decisions already taken or on the size and composition of the FY87-91 program. Estimates for the portfolio composition in the years beyond FY94, however, have an increasingly notional character. Projections of the shares of the Bank portfolio in future years are based on current country creditworthiness ratings, i.e., the ratings are static and do not attempt to predict the share in the portfolio of, say, IIIb countries in FY93 based on possible future revisions in country creditworthiness ratings.

2. Reflecting the increase in the number of policy-based, and hence, faster-disbursing loans since the early 1980s, projections are based on three instrument-specific disbursement profiles corresponding to fast-disbursing loans, which disburse within three years including the year of Board approval; medium-fast disbursing, which are 70% disbursed in 5 years and fully disbursed within eight years; and slow-disbursing or traditional loans, which disburse within nine years. These profiles, which are used for all operations (IBRD and IDA), are as follows:

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1/ These were adjusted to conform to the central case lending assumptions underlying the FY88 Budget exercise: FY87 - $14.5 billion; FY88 - $16.5 billion; FY89 - $17.5 billion; FY90 - $19.0 billion; FY91 - $20.5 bilion. It should be noted that the projections are based on a lending program proposed at one point in time, and that subsequent adjustments can have a significant impact on individual country programs.

2/ The interest charges are: FY87 - 8.2%, FY88 - 7.80%, FY89 - 7.69%, FY90 - 7.68%, FY91 - 7.64%, FY92 - 7.53%, FY93 - 7.46%, FY94 - 7.40% and FY95 through FY2000 - 7.35%.

| | Loan Types | Percent Disbursing Annually |
|---|---|---|
| o Fast: | SALs<br>Sector Adjustment | 21, 64, 15 |
| o Medium: | Financial intermediaries<br>Technical assistance<br>Emergency reconstruction<br>Specific investment loans, in energy and industry | 1, 8, 18, 22, 21, 15, 10,5 |
| o Slow: | Specific investment loans (excluding energy and industry)<br>Sector investment loans. | 0,5,12,17,18,17,14,10,7 |

These profiles are derived from a weighted average of disbursements for all operations (IBRD and IDA) in these categories since the early 1980's. In contrast to previous reports, no country specific disbursement profiles are used in this report. It should be noted that for FY92 and beyond the share of fast/medium/slow disbursing loans in individual countries' lending programs for FY89-91 is retained.

3. Beyond FY91, it is assumed that all non-IIIc countries retain their FY89-91 shares of the lending program. The projections also assume that after FY91 there is no IBRD lending to Regional borrowers or IIIc countries (including former blends and countries with projects identified in the FY87-91 lending program) and that there is no program for graduating countries namely, Bahamas, Barbados, Cyprus and Oman. For countries close to graduation, namely, Algeria and Korea in FY92, lending is phased out in equal increments over a five year period beginning the year after a country reaches the graduation threshold ($2850 in 1985). Finally, to obtain total Bank group net transfers and disbursements, projections of the IDA portfolio are also necessary. As with the IBRD portfolio projections, the IDA projections are based on the FY87-91 lending programs submitted by the Regions in November 1986. Beyond FY91 no growth in commitments (nominal) is assumed. The same disbursement profiles for credits have been used as for IBRD operations.

Sensitivity

4. Given prevailing uncertainty as to the share of adjustment lending in the portfolio, two scenarios have been run. The first, or base, case assumes that beyond FY91, 13% of commitments would be fast-disbursing and 25% medium-disbursing. The second, or fast-disbursing, scenario assumes that beyond FY91 22% of commitments would be fast-disbursing and 23% medium. The same 3% nominal growth in total lending is assumed in both cases. Although the impact of the faster-disbursing (22%) scenario in terms of portfolio composition is small, the impact on the higher risk

countries and on net disbursements and transfers in individual countries can be significant. By FY93, the faster-disbursing scenario would result in an increase in the portfolio outstanding by $2 billion and by FY98, by $7 billion. In terms of distribution within risk categories, the faster-disbursing scenario leads to a further increase in concentration in the higher risk categories (IIIa and IIIb). Specifically, well over 90% of the increase in lending in the faster-disbursing scenario in both FY93 and FY98 goes to categories IIIa and IIIb, with approximately 60% of the increase through FY98 going to category IIIb. These results are shown in Table 1, attached.

5. In an attempt to clarify the Bank's ability to influence net disbursements and transfers and the distribution of the portfolio across risk categories, a second variant on the base case has been run in which the grace period for all loans in all countries has been extended to six years. In this scenario, the lengthening of the grace period has almost twice as much impact on the amount of Bank loans outstanding as the fast-disbursing scenario. In FY93, DOD rises by almost $5 billion compared to the base case and $3 billion compared to the fast-disbursing scenario. By FY98, the extension of grace periods results in an increase in DOD by $15.5 billion and $9 billion in the corresponding scenarios. As in the fast-disbursing scenario, the extension of grace periods leads to a slightly greater concentration in category III (60% in FY93 in both the fast-disbursing and extended grace period scenario compared to 59% in the base case). In contrast to the fast-disbursing scenario, however, the extended grace period scenario leads to a somewhat greater concentration in category IIIa and a lower concentration in category IIIb. This difference reflects the country income composition of the two categories -- namely, in FY87, 53% of the DOD in category IIIa is held by high income countries whereas 56% of the DOD in category IIIb is held by low income countries. Although in percentage terms the differences between the base and extended grace period scenarios are small, their impact on the higher risk countries is not insignificant. In total, the DOD outstanding in FY98 in category III increases by $11 billion, or more than 70% of the total increase in DOD, of which $6 billion is in category IIIa and $5 billion in category IIIb.

Table 1: PORTFOLIO SHARES BY RISK CATEGORY: COMPARISON OF BASE CASE WITH FAST-DISBURSING AND EXTENDED GRACE PERIOD SCENARIOS
(Percent of total IBRD loans outstanding)

| Risk Category | Actual | Projections | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | | Base Case | | | Fast-Disbursing (22%) | | | Extended Grace Period | | |
| | FY86 | FY88 | FY93 | FY98 | FY88 | FY93 | FY98 | FY88 | FY93 | FY98 |
| Category I - Minimal Risk | 7.4 | 5.6 | 2.9 | 1.4 | 5.6 | 2.9 | 1.3 | 5.6 | 3.0 | 1.6 |
| Category II - Some Risk | 29.9 | 31.6 | 37.6 | 40.5 | 31.6 | 37.1 | 39.0 | 31.6 | 37.0 | 39.0 |
| IIa | 6.6 | 6.3 | 8.6 | 11.7 | 6.3 | 8.5 | 11.1 | 6.3 | 8.4 | 11.0 |
| IIb | 6.7 | 7.8 | 12.2 | 13.1 | 7.8 | 12.0 | 12.5 | 7.8 | 12.0 | 12.6 |
| IIc | 16.6 | 17.5 | 16.8 | 15.7 | 17.5 | 16.6 | 15.4 | 17.5 | 16.6 | 15.4 |
| Category III - High Risk | 62.7 | 62.8 | 59.5 | 58.1 | 62.8 | 60.0 | 59.6 | 62.8 | 60.0 | 59.4 |
| IIIa | 28.0 | 27.6 | 25.7 | 25.3 | 27.6 | 25.8 | 25.7 | 27.6 | 26.4 | 26.9 |
| IIIb | 29.4 | 31.1 | 32.1 | 32.3 | 31.1 | 32.5 | 33.5 | 31.1 | 32.0 | 32.1 |
| IIIc | 5.3 | 4.1 | 1.7 | 0.5 | 4.1 | 1.7 | 0.4 | 4.1 | 1.6 | 0.4 |
| Portfolio Outstanding (US$ bil.) | 60.0 | 75.0 | 101.1 | 133.4 | 75.0 | 103.0 | 140.3 | 75.0 | 105.9 | 148.9 |

Note: Individual items may not add to totals due to rounding.

03/03/87

## SUMMARY OF POLICIES AND PROCEDURES REGARDING COUNTRY RISK RATINGS AND EXPOSURE MANAGEMENT

(Circulated to Operational and Financial Staff, January 1987)

### I. COUNTRY RISK RATINGS

1. The core of the Bank's system for managing credit risk is an assessment of individual country creditworthiness for all current and prospective borrowers, as well as for past borrowers with debt still outstanding if the level of such debt is significant. The overall structure of the risk rating system is illustrated in the chart on page 2, below. As the chart indicates, borrowers are classified into three broad groups defined roughly as those with minimal, moderate, or high risk of encountering debt servicing difficulties either in the immediate future and/or over the medium to longer term. As the chart also indicates, the two higher risk categories (II and III) are divided into three sub-categories each in order to further differentiate both individual country situations as well as the related operational policy implications.

2. The categories in the risk rating system reflect an assessment of the likelihood that the country will encounter difficulties in servicing its debt to some or all of its creditors in general. In assessing the probability that debt owed to the IBRD itself will be at risk, the country risk ratings are supplemented by a more specific examination of the exposure in the country's debt and debt service of preferred creditors as a whole and of the IBRD in particular. This is spelled out in more detail in Part II, below.

3. The seven categories and subcategories of the risk rating system are defined operationally. Senior Management has determined that the Bank's lending posture in each borrowing member country should be related directly to the country's risk rating. In the lower risk categories (I, IIa, IIb, and IIc), IBRD lending is not constrained by creditworthiness conditions. The situation in these countries is such that they normally enjoy voluntary access to financial resources on commercial terms.

4. Countries in Category IIIa are expected to be able to service their outstanding debt, and certainly debt to preferred creditors, on original terms. However, most of them have experienced debt servicing difficulties in the past, and frequently have had to reschedule their commercial and/or Paris Club debt, often on multiple occasions. Furthermore, additional restructuring of long-term debt is anticipated in many of these countries, and they are not currently able to borrow commercially on a voluntary basis. On the other hand, with creditor cooperation, effective policies and sustained performance, the situation in these countries is considered viable and there is a reasonable expectation that they should eventually be able to restore their capacity to service external debt on normal terms. As a consequence, these countries are considered conditionally creditworthy for IBRD lending. Senior Management has determined, however, that the scale of lending should take into account the progress being made by these countries in carrying out stabilization and adjustment measures.

STRUCTURE OF THE WORLD BANK RISK RATING SYSTEM

| Risk Rating | Summary of Typical Country Situations | Operational Implications |
|---|---|---|
| Category I | Minimal Risk of Debt Servicing Difficulties | |
| | Countries with a very low risk of debt servicing difficulties in both short and medium term. Includes several graduated borrowers which still have debt outstanding to the Bank | Fully creditworthy for Bank lending. |
| Category II | Some Risk of Debt Servicing Difficulties | |
| | Covers a wide range of countries with low to moderate risk of debt servicing difficulties in either the short or medium term. | |
| Category IIa | Countries with a low probability of debt servicing problems, highly favorable debt indicators, impressive historical performance and a record of competent management. | Fully creditworthy for Bank lending. |
| Category IIb | Mostly countries with short-term prospects comparable to IIa countries, but with less favorable long-term outlook, mainly because of political uncertainties or structural or institutional problems. | Fully creditworthy for Bank lending. |
| Category IIc | Includes countries with relatively favorable short-term prospects, but potentially more serious structural or institutional problems than Category IIb. Also includes some countries with roughly comparable long-term outlook but weaker liquidity situation. | Fully creditworthy for Bank lending, but careful monitoring of creditworthiness indicated. |
| Category III | High Risk of Debt Servicing Difficulties | |
| | Includes all countries with high risk of debt servicing difficulties in either the short term or medium term. | |
| Category IIIa | Mainly countries facing serious liquidity problems. However, given a reasonably favorable global outlook and a continuation of stabilization and adjustment programs, medium term prospects are for a restoration of voluntary market access. | Conditionally considered creditworthy for Bank lending. However, the level of lending should be linked to progress in stabilization and adjustment programs. Country performance and prospects to be closely monitored. |
| Category IIIb | Countries with serious liquidity problems and significantly weaker long-term prospects, due primarily to limited management and institutional capacity and less diversified economic and export structures. Prospects for many of these countries are also clouded by longer-term political uncertainties. | Only marginally creditworthy. Bank lending. preconditioned on agreement with the borrower on the policy measures needed for a return to creditworthiness and the actual implementation of an adequate program of reforms. Country performance and prospects to be monitored closely. |
| Category IIIc | Mainly countries with both a severe liquidity situation as well as intractable longer-term institutional and structural problems. Covers former blend countries no longer considered creditworthy, and also countries where Bank operations are suspended because of unsettled political conditions, including situations in which governments are unwilling to service sovereign debt obligations. | Bank lending normally precluded except for enclave projects with guaranteed debt servicing provisions. Monitoring of economic conditions required if debt outstanding from past borrowing poses a signific[illegible] threat to the Bank's portfolio. |

Operations in IIIa countries would normally include a significant volume of adjustment-support lending and other types of loans designed to improve creditworthiness prospects.

5. Countries in Category IIIb are broadly defined as those having serious debt servicing problems -- and whose prospects can be improved only through sustained implementation of an adequate reform program. Given such performance, together with debt relief in most cases, these countries should eventually be able to restore their debt servicing capacity. Adjustment policy and performance is thus critical. Although risky, lending to IIIb countries can be justified in those cases where the Bank is satisfied that the country has in place a reform program which holds out the promise of eventual success in resolving debt servicing problems. In effect, this requirement separates IIIb countries into two subgroups: those with and those without adequate adjustment programs in place. For those without such a program, new IBRD lending should be suspended, or reduced to a token amount until implementation of the necessary reforms has been demonstrated. Where adjustment programs are in place in IIIb countries, Bank support, especially through policy-based lending, is appropriate.

6. Category IIIc includes a disparate group of countries: very poor countries with limited resources, countries which are somewhat better endowed but with thoroughly inadequate policies and/or performance, countries where political conditions prevent normal Bank operations, and countries otherwise unable or unwilling to meet international financial obligations. Senior Management has determined that Bank lending to countries in this category should be precluded other than for enclave projects with secure debt servicing arrangements.

7. The Planning and Budgeting Department carries out creditworthiness assessments for all Bank borrowers routinely once a year. The initial risk assessment uses methodology which takes into account a broad range of both quantitative and qualitative information. In view of the long-term financial involvement of the Bank with its borrowers, long-term (solvency) factors are given roughly twice the weight of short-term (liquidity) factors in arriving at an overall asssessment. Although the system uses a uniform set of data and ranking criteria for all borrowers, it remains highly judgmental. Country-specific information not captured by the uniform data in the original assessment can, and often does, result in modification of the ultimate ratings. Country ratings and related policy recommendations are reviewed systematically in the Operations and the Financial Complexes of the Bank before review and endorsement by Senior Management.

8. For countries in the higher risk categories (IIIa, IIIb, IIIc), country strategy documents are expected to give specific, prominent attention to the formulation of medium-term work-out programs, including in particular assessment of downside risks and the prospects for burden sharing with other creditors. Further, for countries in the highest risk categories (IIIb, IIIc), the Executive Summary for projects submitted to the Loan Committee should note whether the proposed operation conforms to

the lending strategy adopted in a recent country strategy paper. If there is no recent strategy document and if changing conditions in the country have resulted in a material change in the country's creditworthiness, then the Executive Summary should have attached a special statement summarizing the Region's revised assessment of creditworthiness prospects as well as the Bank strategy in the country and indicating how the proposed operation fits into the strategy.

## II. MANAGING EXPOSURE

9. Portfolio risk arises not only from poor creditworthiness in borrowing members, but also from a concentration of Bank exposure in the borrower's total debt and debt service.[1/] Even in moderate risk countries, when the Bank accounts for a large share of debt or debt service, debt servicing difficulties could pose a threat to the Bank's preferred creditor status.[2/]

10. In order to monitor Bank exposure and establish a framework for managing it, two basic guidelines have been adopted:

- First, the Bank's share of a borrowing member's public and publicly-guaranteed MLT debt or debt service should not normally exceed 20%.[3/]

- Second, if the share of public and publicly-guaranteed MLT debt or debt service to preferred creditors exceeds 33%, then the Bank's share of the total should not normally exceed 15%.

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1/ In assessing the Bank's exposure in the borrower's total debt, guarantees extended by the Bank are to be treated in the same manner as Bank loans. Specifically, the amount of the guarantee is to be added to the amount of loans disbursed and outstanding from the date the guarantee is callable, and should remain in the total for as long as the guarantee is estimated to be outstanding.

2/ Preferred creditors are defined as the IBRD, IDA, the regional multilateral development banks (IDB, ADB, AfDB, EIB), the IMF, and the BIS. Note that the preference given to these creditors is based on convention; it has no strict legal basis.

3/ Short-term debt should be included to the extent it clearly exceeds short-term (trade) financing needs. This will need to be considered if short-term credit exceeds the equivalent of, say, three months worth of commercial imports.

11. It has been recognized that in isolation these basic guidelines are not entirely adequate, and could in fact be misleading. For example, Bank exposure could be low and thus of no apparent concern when a country has a very large total debt outstanding or faces a near-term debt service hump; in such cases, however, the situation could be very risky. Conversely, when a borrower concludes a major long-term debt restructuring arrangement, Bank and/or preferred creditor exposure in debt service tends to increase sharply, and sometimes even goes from below to above the guidelines. In such a situation, however, the debt restructuring should in principle strengthen the country's medium-term prospects and thus reduce the risk to the Bank's portfolio. These examples illustrate why Bank exposure cannot be evaluated solely in relation to the country's total debt or debt service, but must also be examined in relation to the country's debt servicing capacity. Accordingly, the Bank's exposure management framework also includes a third specific guideline, namely:

- o Debt service to the Bank should normally not exceed 5% of the borrower's total exports of goods and services, including workers' remittances. Further, a ratio in the 4-5% range indicates a situation calling for close monitoring.

12. These guidelines are not intended to be applied mechanically. Supplementary analysis based upon the specific country situation may justify exceptional treatment (i.e., acceptance of higher, or insistence upon lower, exposure.) Among the additional factors which should be taken into account in evaluating exposure risk, the following have been identified as meriting specific consideration:

- o <u>Country Risk Rating</u>. Exposure in excess of the guidelines is of less concern the higher the creditworthiness ranking of the borrower.

- o <u>Status of Net Disbursements</u>. As long as the Bank is providing a net flow of new capital to a borrower, it will be in the country's own interest to maintain its relationship with the Bank and to continue to service Bank debt. Moreover, as long as net disbursements are positive, other creditors will have little incentive to demand Bank participation in debt relief. Exposure may thus be of less concern where the net flow is positive and when there is a history of close and effective collaboration between the Bank and borrower, suggesting that the risk of interruption in the flow is minimal.

- o <u>Domestic Resource Mobilization</u>. In most cases consideration of exposure risk focuses on foreign exchange availability. In some countries, however, the critical constraint may well be the ability of the public sector to mobilize the domestic resources needed to acquire foreign exchange for debt service. Where relevant, this factor should also be considered in evaluating exposure risk.

- Position of Other Creditors. The Bank's relative exposure may be increasing simply because a borrower is systematically retiring debt to other creditors as a means of reducing overall debt service requirements.

13. Based on considerations such as these, Country Strategy Papers for countries where exposure is judged to be an issue are expected to address the means available to moderate the implied risk. In the short term there may be only limited possibilities, particularly if the country is already experiencing debt servicing difficulties. Reduced lending -- the most obvious approach -- may not be the preferred means, and may in fact only exacerbate the situation in the short term. Typically, emphasis will be placed on helping the government formulate a medium-term strategy. In the context of such a strategy explicit consideration may be given to the appropriate mix of fast-disbursing and more traditional loans and to the phasing of the lending program. Special attention should be paid to the relative financing contributions expected from the Bank and other principal creditors. The objective is to develop a financing plan for the country's adjustment program that takes appropriate account of the consequences for IBRD exposure and does not leave this exposure to be determined as the residual outcome of decisions made with other considerations in view.

PBDCP
01/16/87

## Table 1: SELECTED INDICATORS OF ECONOMIC PERFORMANCE AND CREDITWORTHINESS

| Country | 1985 GNP p.c. (US$m) | GNP p.c. Growth Rate /a 1975-85 | GNE/ GDP/b 1975-85 | GDI/ GDP/b 1975-85 | Export Growth Rate /b (Nom.$) 1975-85 | Export Concentration Ratio/c 1981-83 (%) | Essential Imports /Total Imports/d 1983 (%) | Real Effective Exchange Rate 1978-86/e (%) | Average Annual Rate of Inflation/f 1985 | Current Account Deficit/ Exports 1986 (%) | Debt to Exports /g 1985 | Debt to Exports /g 1990 | Debt Service Ratio /h 1985 | Debt Service Ratio /h 1990 | Interest Service Ratio/i 1985 | Interest Service Ratio/i 1990 | Reserves/ Months of Imports/f 3/31/86 | IMF Credit % of Quota/j 10/31/86 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **EAST AFRICA** | | | | | | | | | | | | | | | | | | |
| Botswana | 840 | 7.2 | 9.6 | 36.4 | 17.0 | 18.5 | 29 * | -12.4 | 8.1 | -11.5 | 34.5 | 50.2 | 5.2 | 8.0 | 2.5 | 3.6 | 15.2 | — |
| Kenya | 290 | 0.2 | 15.5 | 23.7 | 3.1 | 41.3 | 45 | -19.8 | 13.1 | 18.9 /p | 265.4 | 244.2 | 40.1 | 31.2 | 15.7 | 14.0 | 3.2 | 260.9 |
| Lesotho | 480 | 2.9 | 1.5 | 35.0 | 14.8 | 12.9 | | 5.6 | 14.8 | -2.0 | 52.3 | 76.0 | 5.6 | 4.1 | 1.3 | 1.8 | 2.4 | — |
| Malawi | 170 | -0.6 | 11.9 | 26.3 | 5.4 | 86.5 | 23 * | -3.6 | 10.5 | 39.0 | 394.1 | 340.0 | 39.6 | 23.7 | 16.9 | 10.3 | 0.9 | 287.7 |
| Mauritius | 1070 | 1.1 | 17.3 | 25.0 | 4.1 | 61.9 | 44 | -10.0 | 6.7 | -4.3 | 103.7 | 63.9 | 24.4 | 15.2 | 9.1 | 5.6 | 1.7 | 254.9 |
| Seychelles | 2500 | 2.8 | 0.0 | 0.0 | 3.6 * | 90.0 * | 42 * | 26.3 | 0.9 | 44.8 | 86.6 | .. | 30.2 | .. | 3.7 | .. | 0.2 | — |
| Sudan | 330 | -1.1 | 2.8 | 15.5 | 5.5 | 37.0 | 38 * | -18.0 | 45.4 | 78.7 | 1052.8 | 225.6 | 153.8 | 69.3 | 67.0 | 29.5 | 0.3 | 356.7 |
| Swaziland | 650 | 0.7 | 11.6 | 30.2 | 9.4 | 42.0 | | -6.5 | 19.8 | 9.2 | 45.6 | 31.3 | 6.7 | 5.2 | 2.8 | 2.3 | 2.4 | 31.9 |
| Tanzania | 270 | -2.4 | 10.7 | 20.9 | 2.2 | 48.1 | 38 * | 9.4 | 35.8 | 129.6 | 1188.3 | 542.3 | 22.5 | 27.3 | 7.7 | 7.9 | 0.2 | 28.8 |
| Zaire | 170 | -2.6 | 11.3 | 26.1 | 9.9 | 89.1 | | -72.1 | 52.2 | 11.1 | 284.3 | 347.4 | 27.3 | 44.0 | 15.8 | 15.3 | 2.5 | 229.1 |
| Zambia | 400 | -2.8 | 11.9 | 20.6 | -0.4 | 95.8 | 28 | -65.9 | 37.4 | 47.4 | 492.0 | 242.2 | 77.2 | 38.0 | 31.0 | 13.0 | 0.7 | 249.5 |
| Zimbabwe | 650 | 0.6 | 13.5 | 17.3 | 6.4 | 32.2 | 32 * | -14.7 | 8.5 | 2.3 | 160.3 | 104.0 | 34.6 | 16.7 | 14.2 | 6.3 | 2.3 | 107.4 |
| **WEST AFRICA** | | | | | | | | | | | | | | | | | | |
| Cameroon | 810 | 4.1 | 22.7 | 23.8 | 15.8 | 38.7 | 13 | 10.0 | 1.3 | -2.2 | 100.6 | 133.1 | 22.8 | 19.0 | 6.4 | 7.9 | 0.9 | — |
| Congo | 1020 | 5.7 | 23.0 | 37.5 | 22.3 | 96.6 | 32 | -0.9 | 6.1 | 43.6 | 201.0 | 317.2 | 32.3 | 35.3 | 14.4 | 23.4 | 0.1 | 25.5 |
| Cote d'Ivoire | 610 | -1.4 | 14.4 | 22.8 | 5.3 | 57.3 | 39 | -13.2 | 1.9 | 0.9 | 261.9 | 190.7 | 30.2 | 48.1 | 21.3 | 19.0 | 0.4 | 311.1 |
| Ghana | 390 | -2.7 | 5.9 | 6.8 | 1.7 | 44.1 | 25 * | -67.7 | 10.3 | 45.8 | 340.9 | 313.7 | 36.6 | 40.7 | 17.2 | 13.9 | 6.9 | 300.0 |
| Guinea | 330 | 0.2 | 8.4 | 13.8 | 12.3 | 55.6 | | 28.4 * | | | .. | .. | .. | .. | .. | .. | .. | 38.3 |
| Liberia | 470 | -2.4 | 11.7 | 27.4 | 1.6 | 88.0 | 42 | 9.9 | -0.6 | -2.6 | 261.5 | 177.1 | 6.2 | 22.5 | 3.1 | 7.6 | 0.0 | 288.1 |
| Mauritania | 410 | 0.6 | -3.2 | 32.7 | 8.9 | 57.2 | | 1.2 | 7.0 | 28.4 | 346.7 | 276.5 | 18.8 | 30.7 | 7.7 | 8.8 | 1.2 | 102.4 |
| Nigeria | 760 | -3.8 | 21.2 | 23.2 | 2.0 | 92.4 | 24 | 29.3 | 5.5 | 21.2 | 144.6 | 181.7 | 33.3 | 42.8 | 10.9 | 19.2 | 1.4 | — |
| Senegal | 370 | -1.3 | 0.6 | 16.0 | 2.1 | 28.3 | 57 * | 7.0 | 13.0 | 43.7 | 305.9 | 227.7 | 24.4 | 31.0 | 13.5 | 11.7 | 0.1 | 232.8 |
| **EMENA** | | | | | | | | | | | | | | | | | | |
| Algeria | 2530 | 2.7 | 37.7 | 42.9 | 11.8 | 38.1 | 23 | 46.3 * | 10.8 | 19.3 | 116.0 | 141.0 | 45.3 | 48.4 | 10.6 | 13.1 | 3.8 | — |
| Cyprus | 3790 | 6.0 | 17.7 | 32.5 | 20.0 | 0.5 | | -10.0 | 5.0 | 5.6 | 87.7 | 80.3 | 14.3 | 17.4 | 6.8 | 7.5 | 6.2 | — |
| Egypt | 680 | 4.6 | 18.8 | 29.8 | 17.0 | 70.1 | 33 | 31.1 | 13.3 | 28.5 | 193.9 | 203.1 | 34.2 | 32.5 | 20.9 | 21.1 | 1.6 | 5.4 |
| Hungary | 1940 | 2.1 | 27.7 | 32.0 | 6.8 | .. | 30 | 10.3 | 7.0 | 7.1 | 123.2 | 94.0 | 32.1 | 20.4 | 10.2 | 7.2 | 4.5 | 166.5 |
| Jordan | 1560 | 4.3 | 40.3 /m | 38.1 | 19.3 | 23.7 | 36 | -3.0 | 3.0 | 8.2 | 108.6 | 133.9 | 13.2 | 15.5 | 6.8 | 9.0 | 2.1 | 77.7 |
| Morocco | 610 | 0.8 | 13.5 | 24.3 | 6.2 | 31.9 | 39 | -27.7 | 7.7 | 4.2 | 321.4 | 158.3 | 38.7 | 44.8 | 18.6 | 13.6 | 1.0 | 289.7 |
| Oman | 7100 | 1.3 | 33.3 | 28.5 | 17.0 | .. | 16 | 31.6 * | /k | 51.5 | 36.7 | 136.8 | 7.6 | 19.7 | 3.0 | 8.2 | 2.7 | — |
| Poland | 2120 | .. | .. | .. | .. | .. | 36 | 113.6 | .. | 9.5 | 554.5 | 455.5 | 101.7 | 77.5 | 39.4 | 33.5 | .. | — |
| Portugal | 1970 | 1.6 | 12.5 | 29.0 | 12.2 | 2.3 | 41 | -1.9 | 19.6 | -12.4 | 221.8 | 152.2 | 43.0 | 48.4 | 19.3 | 11.7 | 10.6 | 151.9 |
| Romania | 2200 | 4.2 | 33.3 | 37.0 | | 42.0 * | 31 * | 2.4 | 1.1 | -15.9 | 97.5 | 36.0 | 31.5 | 11.9 | 10.3 | 3.2 | 1.7 | 122.4 |
| Syria | 1630 | 1.4 | 13.9 | 27.4 | 10.6 | 68.7 | 39 * | 84.6 * | 9.0 | 50.4 | 137.1 | 185.0 | 16.7 | 23.8 | 6.5 | 13.1 | 1.2 | — |
| Tunisia | 1220 | 2.7 | 21.9 | 29.9 | 9.1 | 49.4 | 27 | -20.0 | 8.0 | 25.9 | 167.6 | 181.7 | 25.1 | 33.3 | 10.0 | 10.9 | 0.5 | — |
| Turkey | 1130 | 0.9 | 17.3 | 21.4 | 20.6 | 12.6 | 46 | -43.6 | 45.0 | 12.6 | 193.8 | 188.9 | 30.4 | 34.7 | 13.3 | 14.5 | 2.2 | 215.7 |
| Yemen, AR | 520 | 4.0 | -6.2 | 29.2 | 27.0 | 29.3 | | -14.5 /l | 12.3 | 62.4 | 157.7 | 177.9 | 10.6 | 20.7 | 1.6 | 8.0 | 2.9 | 16.9 |
| Yugoslavia | 2070 | 2.1 | 31.5 | 35.6 | 7.8 | 5.1 | 33 | -27.0 | 74.4 | -4.0 | 131.4 | 71.2 | 21.1 | 20.7 | 12.6 | 6.6 | 1.4 | 291.6 |
| **LAC** | | | | | | | | | | | | | | | | | | |
| Argentina | 2130 | -1.6 * | 18.1 | 20.0 | 8.4 | 27.9 | 14 | -19.7 | 672.2 | 25.2 | 460.3 | 448.4 | 77.6 | 63.5 | 48.9 | 36.2 | 4.1 | 204.7 |
| Bahamas | 7150 | 3.8 | 13.7 | 14.7 | 11.0 | .. | | 6.5 | 4.6 | -2.3 | 16.3 | 5.4 | 4.2 | 1.8 | 1.8 | 0.6 | 2.1 | — |
| Barbados | 4680 | 1.3 | 14.2 | 22.5 | 16.5 | 9.8 | | 20.9 | 4.0 | -3.3 | 62.0 | 34.2 | 8.7 | 13.3 | 4.0 | 3.2 | 2.0 | 89.4 |
| Belize | 1130 | -0.1 | 3.1 | 14.5 | 0.2 | 39.8 | | 9.8 * | 4.0 | -6.4 | 100.5 | 79.6 | 15.9 | 14.8 | 6.5 | 5.4 | 2.2 | 100.4 |
| Bolivia | 470 | -4.6 | 15.0 | 20.4 | 7.7 | 32.5 | 14 | -8.9 | 1281.6 | 59.5 | 523.8 | 724.4 | 68.9 | 66.8 | 44.8 | 43.0 | 6.2 | 54.5 |
| Brazil | 1640 | 0.7 | 18.9 | 22.5 | 12.2 | 19.5 | 64 | -23.6 | 226.9 | -0.9 | 353.5 | 238.7 | 74.0 | 50.4 | 37.8 | 21.7 | 4.2 | 262.2 |
| Chile | 1440 | 0.6 | 8.1 | 15.3 | 9.2 | 56.5 | 27 * | -31.7 | 30.7 | 24.3 | 443.9 | 349.5 | 56.9 | 57.3 | 41.3 | 27.0 | 5.5 | 234.3 |
| Colombia | 1320 | 1.5 | 16.3 | 18.9 | 6.5 | 56.0 | 23 | -30.7 | 24.0 | -5.9 | 265.0 | 201.1 | 38.7 | 36.1 | 23.5 | 17.5 | 4.5 | — |
| Costa Rica | 1290 | -1.7 | 12.8 | 24.8 | 7.3 | 56.0 | 29 | -18.4 | 15.0 | 14.6 | 348.2 | 244.5 | 38.9 | 30.8 | 29.3 | 19.3 | 3.6 | 180.5 |
| Dominican Rep. | 820 | 0.0 | 14.3 | 23.5 | 10.5 | 52.7 | 50 | -25.7 | 37.5 | 9.7 /p | 195.9 | 183.2 | 23.5 | 26.9 | 12.2 | 12.9 | 1.7 | 227.6 |
| Ecuador | 1160 | 0.1 | 17.9 | 23.6 | 13.0 | 65.4 | 7 | -22.9 | 28.0 | 31.3 /p | 265.1 | 287.1 | 34.6 | 34.4 | 27.6 | 23.6 | 2.6 | 265.4 |
| El Salvador | 710 | -4.8 | 11.7 | 17.2 | 2.2 | 66.7 | 43 | 20.2 | 22.3 | 23.9 /p | 217.9 | 135.8 | 29.1 | 12.5 | 10.0 | 4.8 | 3.2 | 43.9 |
| Guatemala | 1220 | -2.6 | 11.6 | 16.2 | 5.2 | 41.3 | 44 * | -14.1 | 18.7 | 6.0 | 203.2 | 156.2 | 26.9 | 26.8 | 12.7 | 12.7 | 4.4 | 64.2 |
| Guyana | 570 | -3.2 | 9.5 | 29.0 | -3.5 | 74.1 | | 48.6 | 13.3 | | 561.9 | .. | 91.6 | .. | 48.7 | .. | 0.2 | 145.8 |
| Honduras | 730 | -0.2 | 10.2 | 20.7 | 3.1 | 56.2 | 32 | 28.0 | 3.3 | 24.7 /p | 264.4 | 209.5 | 32.9 | 20.1 | 14.8 | 12.3 | 1.0 | 129.6 |
| Jamaica | 990 | -3.3 | 6.7 | 19.1 | 3.3 | 23.4 | 48 | -31.8 | 25.7 | 8.7 | 287.5 | .. | 49.3 | .. | 24.8 | .. | 1.7 | 398.7 |
| Mexico | 2080 | 1.0 | 21.8 | 23.9 | 22.3 | 77.8 | 20 | -27.7 | 57.8 | 15.0 | 346.5 | 371.4 | 54.7 | 74.2 | 36.1 | 32.4 | 2.2 | 250.0 |
| Nicaragua | 850 | -4.7 | 5.3 | 16.6 | 2.0 | 60.7 | 35 | 695.7 | 219.5 | .. | .. | .. | .. | .. | .. | .. | 4.7 | — |
| Panama | 2020 | 2.1 | 17.7 | 26.5 | 10.0 | 39.6 | 36 | -7.6 | 1.0 | 5.8 | 117.0 | 58.6 | 21.4 | 9.2 | 10.6 | 4.6 | 0.2 | 280.7 |
| Paraguay | 940 | 4.0 | 17.8 | 25.1 | 20.7 | 57.2 | 37 | 1.1 | 25.2 | 88.0 | 327.6/n | .. | 43.3/o | .. | 23.2/o | .. | 3.8 | — |
| Peru | 960 | -1.8 | 11.2 | 15.7 | 9.3 | 30.8 | 20 | 16.8 | 163.4 | 6.9 | 332.1 | 586.4 | 24.5 | 13.1 | 11.4 | 9.1 | 8.0 | 180.2 |
| Uruguay | 1660 | -0.6 | 9.4 | 13.7 | 8.2 | 38.1 | 43 | -2.1 | 72.2 | -1.3 | 316.8 | 222.2 | 45.5 | 44.9 | 35.2 | 22.3 | 10.8 | 205.8 |
| **EAST ASIA & PACIFIC** | | | | | | | | | | | | | | | | | | |
| China | 310 | 6.4 | 30.1 | 30.4 | 16.2 | 19.0 | 16 | -50.2 | 2.7 | 33.6 | 68.1 | 87.5 | 6.8 | 12.8 | 3.4 | 6.0 | 4.6 | — |
| Fiji | 1700 | 0.6 | 18.1 | 25.3 | 8.3 | 51.2 | | -4.4 | 4.4 | 6.2 | 87.1 | 49.7 | 17.5 | 9.1 | 7.3 | 3.3 | 3.9 | 22.2 |
| Indonesia | 530 | 3.7 | 18.0 | 21.1 | 10.3 | 53.9 | 33 | -37.2 | 4.7 | 27.5 | 174.7 | 193.6 | 25.6 | 33.2 | 12.3 | 13.5 | 3.4 | 4.2 |
| Korea | 2180 | 5.0 | 23.5 | 30.0 | 17.3 | 1.3 | 15 | -19.1 | 2.5 | -5.1 | 143.7 | 79.9 | 22.3 | 17.0 | 11.7 | 7.1 | 2.9 | 282.8 |
| Malaysia | 2050 | 4.3 | 27.6 | 30.3 | 15.1 | 51.9 | 23 | -12.9 | 0.3 | 9.0 | 104.4 | 86.8 | 29.2 | 17.5 | 9.0 | 8.0 | 4.0 | — |
| PNG | 710 | -1.3 | 11.1 | 24.4 | 6.0 | 59.4 | 38 | -7.6 | 3.7 | 28.0 /p | 213.4 | 174.7 | 34.5 | 37.6 | 15.4 | 13.3 | 4.8 | — |
| Philippines | 600 | 0.5 | 21.8 | 27.4 | 9.8 | 23.7 | 35 | -12.6 | 23.1 | -3.5 | 331.5 | 311.8 | 40.4 | 40.2 | 26.5 | 23.0 | 2.6 | 233.6 |
| Thailand | 830 | 3.6 | 20.7 | 24.8 | 14.3 | 28.4 | 28 | -7.7 | 2.4 | 10.9 | 168.2 | 128.6 | 26.2 | 21.1 | 11.7 | 9.1 | 3.4 | 206.9 |
| **SOUTH ASIA** | | | | | | | | | | | | | | | | | | |
| India | 250 | 1.9 | 20.1 | 23.6 | 7.2 | 17.3 | 44 | -9.6 | 5.6 | 18.5 | 272.9 | 189.2 | 21.7 | 17.5 | 11.2 | 6.2 | 6.7 | 161.4 |
| Pakistan | 380 | 3.4 | 12.3 | 17.5 | 12.9 | 28.3 | 42 | -25.8 | 5.8 | 16.3 | 203.2 | 176.4 | 19.0 | 18.5 | 7.8 | 6.4 | 2.2 | 169.7 |
| Sri Lanka | 370 | 3.2 | 12.3 | 24.0 | 7.8 | 44.8 | 41 | 24.7 | 1.4 | 30.6 | 240.3 | 270.4 | 17.7 | 17.4 | 7.3 | 7.7 | 1.9 | 112.8 |

.. Data not available.

— Indicates that a figure is zero or less than half of a significant digit or that data do not exist.

* Data from 1986 Creditworthiness Report.

/a Computed from EPD database using least squares method.
/b EPD database.
/c Share of the country's three major exports in total export earnings, Commodity Trade & Price Trends, 1985 edition.(EPD).
/d WDR 1986. Ratio of food and fuel imports to total merchandise imports.
/e Change in index between 1978-86; IMF, Indicators of Real Effective Exchange Rates EBS/86/208 September 5, 1986.
/f IMF/IFS October, 1986.
/g Ratio of total debt (disbursed and outstanding including short-term, and IMF) to exports of goods and services; Regional estimates.
/h Ratio of total debt service including interest on short-term, to export of goods and services; Regional estimates.
/i Ratio of total interest payments including short-term, to exports of goods and services.
/j IMF, International Financial Statistics, December, 1986.
/k Estimated by Region at less than 5%.
/l Nominal exchange rate.
/m Using GNE including net current transfers - 40.3; excluding net current transfers - 3.14. (World Tables 1983)
/n 1985-86.
/o 1986.
/p excludes grants.

| | IBRD Debt Service as % share of Exports | | | % of External Public Debt Outstanding /a | | | % of Public Debt Service /b | | | % Share of Public Debt Service Due in 1987 /c | | | % Share in IBRD Loan Portfolio /e | | | 1987-91 Lending Prog./f ($m) | | Country Assessments: PBD | | | Country Assessments: Institutional Investor /g | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 1987 | 1990 | 1995 | 1987 | 1990 | 1995 | 1987 | 1990 | 1995 | IDA | IMF | Pref. Cr./d | FY87 | FY90 | FY95 | IBRD | IDA | 1985 | 1986 | 1987 | Sep. 1983 | Sep. 1985 | Sep. 1986 |
| **EAST AFRICA** | | | | | | | | | | | | | | | | | | | | | | | |
| Botswana | 2.2 | 2.2 | 1.7 | 29.4 | 21.1 | 15.6 | 39.3 | 27.1 | 19.2 | 0.5 | 0.0 | 61.9 | 0.2 | 0.2 | 0.1 | 97 | | IIb | IIb | IIb | .. | .. | .. |
| Kenya | 7.4 | 7.3 | | 24.1 | 18.5 | | 27.3 | 29.1 | | 1.3 | 21.9 | | 1.3 | 1.0 | 0.5 | 180 | 591 | IIIb | IIIb | IIIb | 72 | 64 | 63 |
| Lesotho | 0.0 | 0.1 | 1.3 | 0.0 | 1.7 | 11.3 | 0.0 | 3.7 | 21.7 | 9.7 | 0.0 | 76.6 | 0.0 | 0.0 | 0.0 | 50 | 45 | IIIc | IIIc | IIIa | .. | .. | .. |
| Malawi | 4.0 | 3.5 | 2.3 | 7.3 | 6.7 | 3.4 | 11.3 | 16.0 | 13.9 | 4.0 | 34.5 | 49.3 | 0.1 | 0.1 | 0.1 | | 393 | IIIb | IIIb | IIIb | 32 | 34 | 32 |
| Mauritius | 3.1 | 3.3 | 3.1 | 26.7 | 33.9 | 53.2 | 20.0 | 23.3 | 46.3 | 0.3 | 35.6 | 63.6 | 0.2 | 0.2 | 0.2 | 179 | | IIb | IIb | IIb | 79 | 74 | 72 |
| Seychelles | 0.4 | | | | | | | | | | | | 0.0 | 0.0 | 0.0 | | | IIc | IIc | IIc | 91 | 94 | 94 |
| Sudan | 0.7 | 0.5 | 0.0 | 0.8 | 0.7 | 0.9 | 0.8 | 0.8 | 0.1 | 0.8 | 13.6 | 18.7 | 0.1 | 0.0 | 0.0 | | 470 | IIIc | IIIc | IIIc | 101 | 104 | 105 |
| Swaziland | 1.6 | 1.1 | 1.0 | 23.7 | 17.2 | 19.8 | 25.7 | 21.0 | 16.2 | 0.6 | 0.0 | 48.6 | 0.1 | 0.1 | 0.1 | 68 | | IIIa | IIc | IIc | .. | .. | .. |
| Tanzania | 8.6 | 4.7 | | 6.9 | 4.6 | | 13.6 | 17.8 | | 2.6 | 2.1 | 23.9 | 0.4 | 0.2 | 0.1 | | 490 | IIIc | IIIc | IIIc | 96 | 98 | 98 |
| Zaire | 1.0 | 0.8 | 0.4 | 0.6 | 0.9 | 0.5 | 1.7 | 2.0 | 2.1 | 0.7 | 19.2 | 30.1 | 0.1 | 0.1 | 0.0 | | 1048 | IIIc | IIIc | IIIc | 104 | 100 | 100 |
| Zambia | 6.0 | 4.6 | 2.2 | 12.3 | 11.2 | 4.2 | 8.2 | 13.5 | 25.3 | 0.3 | 35.6 | 49.3 | 0.6 | 0.4 | 0.1 | | 483 | IIIb | IIIc | IIIc | 97 | 96 | 95 |
| Zimbabwe | 2.1 | 3.2 | 3.4 | 18.3 | 22.9 | 26.9 | 7.8 | 21.9 | 27.7 | 0.1 | 22.0 | 30.3 | 0.4 | 0.6 | 0.7 | 615 | | IIIb | IIIb | IIIa | 75 | 76 | 75 |
| **WEST AFRICA** | | | | | | | | | | | | | | | | | | | | | | | |
| Cameroon | 2.6 | 3.2 | 2.8 | 19.7 | 18.1 | 14.0 | 21.9 | 26.9 | 29.9 | 0.9 | 0.0 | 28.1 | 0.6 | 0.5 | 0.5 | 182 | | IIb | IIc | IIc | 52 | 52 | 52 |
| Congo | 1.3 | 2.4 | 4.5 | 4.1 | 8.6 | 19.0 | 7.2 | 8.4 | 15.1 | 0.4 | 0.6 | 25.6 | 0.1 | 0.2 | 0.3 | 297 | | IIIb | IIIb | IIIb | 81 | 79 | 85 |
| Cote d'Ivoire | 6.0 | 7.0 | 7.4 | 24.1 | 36.2 | | 13.1 | 18.6 | | 0.3 | 10.0 | | 2.0 | 2.3 | 1.9 | 1477 | | IIIb | IIIb | IIIb | 58 | 68 | 67 |
| Ghana | 2.5 | 1.5 | 0.8 | 4.4 | 2.7 | 1.1 | 4.7 | 3.8 | 2.7 | 0.5 | 48.9 | 59.5 | 0.2 | 0.1 | 0.0 | | 748 | IIIc | IIIc | IIIc | .. | .. | .. |
| Guinea | | | | | | | | | | | | | 0.1 | 0.0 | 0.0 | | 367 | IIIc | IIIc | IIIc | .. | .. | .. |
| Liberia | 3.8 | 3.5 | 1.6 | 9.6 | 8.7 | 5.0 | 11.2 | 16.5 | 14.3 | 0.5 | 41.6 | | 0.2 | 0.1 | 0.0 | | 55 | IIIc | IIIc | IIIc | 92 | 95 | 96 |
| Mauritania | 2.7 | 2.3 | 0.3 | 4.9 | 2.9 | 0.5 | 6.9 | 7.7 | 2.0 | 0.7 | 4.7 | | 0.1 | 0.1 | 0.0 | | 105 | IIIc | IIIc | IIIc | .. | .. | .. |
| Nigeria | 4.7 | 4.6 | 5.7 | 10.7 | | | 16.7 | | | 0.1 | 0.0 | | 2.9 | 4.2 | 5.9 | 5213 | | IIIa | IIIb | IIIb | 55 | 69 | 76 |
| Senegal | 1.6 | 1.2 | 0.6 | 4.0 | 2.7 | 0.8 | 4.8 | 4.0 | 2.3 | 1.1 | 19.7 | 35.0 | 0.2 | 0.1 | 0.0 | | 305 | IIIc | IIIc | IIIc | 83 | 83 | 90 |
| **EMENA** | | | | | | | | | | | | | | | | | | | | | | | |
| Algeria | 1.6 | 2.1 | 1.7 | 5.3 | 6.2 | 8.6 | 3.3 | 4.5 | 5.8 | 0.0 | 0.0 | | 0.9 | 0.9 | 0.9 | 1285 | | IIb | IIc | IIc | 33 | 32 | 40 |
| Cyprus | 1.4 | 1.4 | 0.5 | 8.1 | 6.4 | 2.0 | 11.3 | 8.9 | 3.2 | 0.0 | 0.0 | 25.0 | 0.1 | 0.1 | 0.0 | 33 | | IIb | IIb | IIa | 59 | 53 | 50 |
| Egypt | 2.3 | 2.2 | 1.9 | 7.8 | 9.5 | 10.2 | 7.7 | 7.9 | 8.3 | 0.3 | 0.0 | | 2.1 | 2.7 | 2.6 | 1630 | | IIIa | IIIb | IIIb | 61 | 55 | 65 |
| Hungary | 0.8 | 1.6 | 1.7 | 7.9 | 13.2 | 13.9 | 2.8 | 7.9 | 12.8 | 0.0 | 11.0 | | 1.0 | 1.6 | 1.3 | 1110 | | IIc | IIc | IIc | 44 | 39 | 38 |
| Jordan | 1.4 | 1.7 | 1.6 | 9.0 | 5.8 | 2.8 | 12.6 | 12.4 | 5.2 | 0.3 | 0.7 | 17.7 | 0.4 | 0.4 | 0.4 | 384 | | IIb | IIb | IIb | 53 | 51 | 54 |
| Morocco | 5.9 | 5.2 | 4.5 | 15.5 | 24.9 | 29.9 | 18.1 | 12.1 | 23.5 | 0.1 | 22.0 | 46.6 | 2.8 | 3.1 | 3.1 | 7383 | | IIIb | IIIb | IIIb | 68 | 73 | 74 |
| Oman | 0.4 | 0.5 | 0.2 | 1.6 | 1.0 | 0.3 | 2.7 | 2.6 | 0.7 | 0.0 | 0.0 | 3.4 | 0.1 | 0.1 | 0.0 | 23 | | IIb | IIb | IIc | 41 | 34 | 35 |
| Poland | 0.0 | 0.4 | | 0.0 | 1.2 | | 0.0 | 0.5 | | 0.0 | 0.0 | | 0.0 | 0.4 | 1.2 | 1113 | | | | IIIb | .. | .. | 86 |
| Portugal | 1.3 | 1.0 | 0.6 | 3.3 | 2.8 | 2.4 | 3.3 | 2.3 | 1.7 | 0.0 | 6.2 | 12.3 | 0.7 | 0.5 | 0.3 | 407 | | IIc | IIc | IIc | 40 | 41 | 37 |
| Romania /h | 4.4 | 3.1 | | 32.9 | 31.9 | 18.1 | 18.2 | 26.5 | | 0.0 | 14.6 | | 2.5 | 1.3 | 0.4 | 502 | | IIc | IIIa | IIIa | 78 | 63 | 57 |
| Syria | 1.9 | 1.6 | 1.5 | 9.0 | 5.2 | 2.9 | 11.7 | 7.3 | 2.7 | 0.2 | 0.0 | | 0.5 | 0.4 | 0.4 | 435 | | IIIb | IIIb | IIIb | 77 | 78 | 78 |
| Tunisia | 5.1 | 5.6 | 5.0 | 16.2 | 19.9 | 24.5 | 19.6 | 16.8 | 28.7 | 0.2 | 1.4 | 23.2 | 1.2 | 1.5 | 1.4 | 1247 | | IIb | IIc | IIc | 42 | 46 | 47 |
| Turkey | 5.6 | 5.9 | 5.5 | 25.2 | 27.8 | 25.6 | 19.9 | 21.2 | 23.8 | 0.1 | 11.5 | | 7.1 | 7.2 | 6.8 | 5553 | | IIIa | IIc | IIIa | 73 | 56 | 51 |
| Yemen, AR | 0.0 | 0.1 | 0.7 | 0.0 | 1.0 | 7.7 | 0.0 | 0.4 | 2.0 | 1.4 | 2.2 | | 0.0 | 0.0 | 0.1 | 100 | 149 | IIIa | IIIa | IIIa | .. | .. | .. |
| Yugoslavia /h | 2.9 | 2.2 | 1.2 | 13.8 | 12.4 | 10.3 | 13.2 | 11.0 | 9.5 | 0.0 | 13.7 | 30.7 | 3.9 | 2.6 | 1.6 | 1478 | | IIIa | IIIa | IIIa | 66 | 62 | 58 |
| **LAC** | | | | | | | | | | | | | | | | | | | | | | | |
| Argentina | 2.9 | 3.5 | 4.4 | 3.0 | 4.7 | 7.2 | 5.4 | 6.0 | 9.0 | 0.0 | 12.5 | 21.6 | 1.6 | 2.5 | 3.4 | 3610 | | IIIa | IIIa | IIIa | 71 | 75 | 71 |
| Bahamas | 0.2 | 0.2 | 0.2 | 8.0 | 18.8 | | 6.3 | 12.1 | | 0.0 | 0.0 | 10.0 | 0.0 | 0.0 | 0.0 | 21 | | IIa | IIa | IIa | .. | .. | .. |
| Barbados | 1.1 | 1.2 | 1.0 | 10.2 | 15.6 | | 9.3 | 10.3 | | 0.0 | 19.0 | 39.9 | 0.1 | 0.0 | 0.0 | 48 | | IIc | IIc | IIa | .. | 60 | 56 |
| Belize | 0.8 | 1.1 | 1.8 | 7.2 | 9.6 | 13.6 | 6.6 | 7.5 | 14.1 | 0.0 | 17.6 | 53.7 | 0.0 | 0.0 | 0.0 | 19 | | IIc | IIc | IIc | .. | .. | .. |
| Bolivia | 5.7 | 4.0 | 1.9 | 5.4 | 3.0 | 0.8 | 11.2 | 6.6 | 2.6 | 0.8 | 9.7 | 43.8 | 0.3 | 0.2 | 0.1 | | 300 | IIIc | IIIc | IIIc | 94 | 103 | 102 |
| Brazil | 4.4 | 4.0 | 3.2 | 9.5 | 10.2 | 12.2 | 6.9 | 9.0 | 13.8 | 0.0 | 5.7 | 12.5 | 10.4 | 10.0 | 8.9 | 9489 | | IIIa | IIIa | IIIa | 51 | 61 | 55 |
| Chile | 2.3 | 3.2 | 4.9 | 7.1 | 7.5 | 8.0 | 7.3 | 6.6 | 10.0 | 0.0 | 21.3 | 38.8 | 1.5 | 1.9 | 1.8 | 1556 | | IIIb | IIIb | IIIb | 62 | 72 | 70 |
| Colombia | 3.3 | 7.4 | 5.1 | 27.4 | 24.2 | 18.1 | 27.6 | 25.7 | 21.4 | 0.0 | 0.0 | 33.6 | 4.7 | 4.2 | 3.4 | 2571 | | IIc | IIc | IIc | 19 | 50 | 48 |
| Costa Rica | 1.9 | 3.6 | 2.1 | 9.8 | 8.8 | 7.2 | 10.3 | 12.7 | 10.0 | 0.0 | 12.3 | | 0.6 | 0.4 | 0.3 | 164 | | IIIb | IIIb | IIIb | 90 | 86 | 84 |
| Dominican Rep. | 1.9 | 2.0 | 1.9 | 5.6 | 6.1 | 7.5 | 6.1 | 7.7 | 8.8 | 0.1 | 10.7 | 22.0 | 0.3 | 0.2 | 0.2 | 176 | | IIIb | IIIb | IIIb | 86 | 91 | 89 |
| Ecuador | 2.9 | 2.7 | | 5.1 | 6.4 | | 7.9 | 8.7 | | 0.1 | 13.0 | 31.2 | 0.6 | 0.7 | 0.6 | 561 | | IIIa | IIIa | IIIb | [illegible] | 70 | 69 |
| El Salvador | 1.3 | 1.5 | 1.5 | 7.3 | 8.4 | | 7.4 | 13.9 | | 0.2 | 13.2 | 32.5 | 0.2 | 0.2 | 0.2 | 134 | | IIIc | IIIb | IIIb | 103 | 106 | 104 |
| Guatemala | 3.0 | 3.6 | 3.3 | 11.6 | 16.8 | 21.6 | 11.3 | 14.5 | 17.0 | 0.0 | 5.5 | 33.2 | 0.4 | 0.5 | 0.4 | 183 | | IIIb | IIIb | IIIb | 88 | 82 | 82 |
| Guyana | | | | | | | | | | | | | 0.1 | 0.1 | 0.0 | | 7 | IIIc | IIIc | IIIc | .. | .. | .. |
| Honduras | 5.7 | 4.4 | 3.2 | 17.0 | 13.0 | 13.2 | 22.8 | 25.4 | 22.8 | 0.3 | 16.6 | | 0.6 | 0.5 | 0.4 | 238 | | IIIb | IIIb | IIIb | 93 | 97 | 93 |
| Jamaica | 6.0 | | | 14.2 | | | 12.1 | | | 0.0 | 30.9 | 45.9 | 0.8 | 0.5 | 0.3 | 151 | | IIIb | IIIb | IIIb | 85 | 89 | 88 |
| Mexico | 4.5 | 4.4 | | 7.1 | 7.5 | | 7.8 | 7.8 | | 0.0 | 3.7 | | 8.3 | 8.2 | 8.1 | 8750 | | IIIa | IIIb | IIIb | 50 | 48 | 62 |
| Nicaragua | | | | | | | | | | | | | 0.2 | 0.1 | 0.0 | | | IIIc | IIIc | IIIc | 105 | 109 | 108 |
| Panama | 1.8 | 1.8 | | 13.3 | 20.5 | | 13.1 | 21.9 | | 0.0 | 14.9 | 51.8 | 0.6 | 0.6 | 0.3 | 330 | | IIIa | IIIa | IIIa | 54 | 59 | 59 |
| Paraguay | 7.6/i | | | 16.5 | 9.4 | | 25.8 | | | | | | 0.5 | 0.3 | 0.1 | | | IIc | IIc | IIIb | 50 | 57 | 60 |
| Peru /j | 5.8 | 7.1 | | 7.4 | 5.4 | | 64.8 | 69.2 | | 0.0 | 0.0 | 92.4 | 1.4 | 1.0 | 0.4 | 21 | | IIIb | IIIc | IIIc | 69 | 32 | 37 |
| Uruguay | 3.5 | 3.5 | 3.1 | 7.6 | 9.3 | 13.1 | 10.7 | 9.8 | 11.8 | 0.0 | 23.1 | 37.3 | 0.3 | 0.3 | 0.3 | 411 | | IIIa | IIIa | IIIa | 64 | 67 | 56 |
| **EAST ASIA & PACIFIC** | | | | | | | | | | | | | | | | | | | | | | | |
| China | 0.4 | 0.8 | 1.6 | 6.3 | 12.2 | 23.9 | 4.8 | 7.7 | 20.1 | 0.5 | 0.0 | 6.3 | 1.6 | 3.5 | 8.2 | 9457 | 2616 | IIb | IIa | IIa | 24 | 21 | 22 |
| Fiji | 1.8 | 2.0 | 1.3 | 24.7 | 20.7 | 11.3 | 18.4 | 29.9 | 21.8 | 0.0 | 5.0 | 49.2 | 0.1 | 0.1 | 0.0 | 29 | | IIb | IIb | IIa | 59 | .. | .. |
| Indonesia | 4.4 | 5.0 | 5.1 | 17.9 | 19.6 | 26.4 | 17.1 | 19.3 | 24.1 | 0.2 | 0.0 | 17.5 | 7.8 | 7.8 | 8.5 | 6538 | | IIc | IIc | IIc | 37 | 42 | 43 |
| Korea | 1.9 | 1.5 | 0.8 | 12.5 | 10.3 | 5.9 | 13.3 | 11.0 | 8.9 | 0.0 | 7.3 | | 6.1 | 4.3 | 2.2 | 1925 | | IIa | I | I | 31 | 29 | 29 |
| Malaysia | 1.1 | 1.0 | 0.8 | 5.3 | 5.7 | 7.7 | 8.1 | 7.5 | 9.5 | 0.0 | 0.0 | 11.0 | 1.2 | 1.2 | 1.2 | 1440 | | IIb | IIb | IIb | 20 | 25 | 27 |
| PNG | 1.3 | 1.9 | 2.9 | 7.1 | 13.9 | | 7.6 | 9.4 | | 0.5 | 2.1 | 27.9 | 0.1 | 0.2 | 0.4 | 400 | | IIc | IIIa | IIIa | 48 | 47 | 49 |
| Philippines | 5.6 | 5.4 | 4.2 | 18.0 | 15.8 | | 16.2 | 16.9 | | 0.0 | 7.1 | 27.6 | 4.4 | 3.9 | 3.4 | 2307 | | IIIb | IIIb | IIIb | 63 | 80 | 77 |
| Thailand | 3.4 | 2.5 | 2.3 | 22.7 | 18.6 | 9.6 | 22.3 | 15.5 | 10.1 | 0.1 | 16.6 | 47.0 | 3.9 | 2.9 | 1.8 | 785 | | IIa | IIa | IIa | 36 | 36 | 33 |
| **SOUTH ASIA** | | | | | | | | | | | | | | | | | | | | | | | |
| India | 3.7 | 4.5 | 4.7 | 11.1 | 16.9 | 16.3 | 16.4 | 26.7 | 17.5 | 4.3 | 30.5 | 51.6 | 4.9 | 9.1 | 11.0 | [illegible] | 1189 | [illegible] | [illegible] | [illegible] | [illegible] | [illegible] | [illegible] |
| Pakistan | 1.8 | 2.6 | 3.6 | 7.4 | 13.6 | 15.0 | 7.9 | 17.1 | 21.7 | 1.9 | 25.7 | 43.8 | 1.1 | 1.9 | 2.4 | 1870 | 950 | IIIa | IIIa | IIIa | 76 | [illegible] | [illegible] |
| Sri Lanka | 0.7 | 0.7 | 0.7 | 1.9 | 1.7 | 1.4 | 3.0 | 4.8 | 4.0 | 1.7 | 22.8 | | 0.1 | 0.1 | 0.1 | 62 | 186 | IIIb | IIIb | IIIb | [illegible] | [illegible] | [illegible] |

/a Ratio of IBRD debt outstanding and disbursed (DOD) to public and publicly guaranteed MLT debt (including IMF). PBD projections of IBRD DOD.
Regional projections of total public and publicly guaranteed MLT debt.

/b Ratio of IBRD debt service to debt service on all public and publicly guaranteed MLT debt (including IMF). PBD projections of IBRD debt service.
Regional projections of total public and publicly guaranteed MLT debt service.

/c Ratio of IDA, IMF, and preferred creditors to debt service on all public and publicly guaranteed MLT debt service (including IMF). PBD projections of IDA debt service.
Regional projections of IMF, preferred creditors, and total public and publicly guaranteed MLT debt service.

/d By convention, preferred creditor status is accorded to the BIS, IMF, World Bank and other multilateral development banks. Regional estimates; where blank, no consistent data.

/e PBD base case projections of loan portfolio, January, 1987.

/f Country lending allocations as of November 1986.

/g A total of 109 countries are ranked from 1 (least risky) to 109 (most risky) based on commercial bank responses.

/h Includes private non-guaranteed debt of the socially owned enterprises.

/i 1986 data.

/j Peru debt service projections reflect current announced repayment plans.

TABLE 3: EXTERNAL DEBT OUTSTANDING, END-1985/a
(US$ Million)

| | Public Debt | | Private Non-Guaranteed Debt/b | Total | % Share of Total Private to Total MLT | Short-term Debt | Total MLT & Short-term Debt |
|---|---|---|---|---|---|---|---|
| | Official Sources | Private Sources | | | | | |
| **E. AFRICA** | | | | | | | |
| Botswana | 299.4 | 34.9 | 0.0 | 334.3 | 10.4 | 2.0 | 336.3 |
| Kenya | 2437.0 | 420.3 | 405.7 | 3263.0 | 25.3 | 470.0 | 3733.0 |
| Lesotho | 164.5 | 7.8 | 0.0 | 172.3 | 4.5 | 4.0 | 176.3 |
| Malawi | 676.5 | 98.4 | 0.0 | 774.9 | 12.7 | 79.0 | 853.9 |
| Mauritius | 316.6 | 87.5 | 14.8 | 418.9 | 24.4 | 51.0 | 469.9 |
| Seychelles | 45.5 | 8.5 | 0.0 | 54.0 | 15.7 | 24.0 | 78.0 |
| Sudan | 4171.6 | 914.3 | 0.0 | 5085.9 | 18.0 | 581.0 | 5666.9 |
| Swaziland | 172.8 | 8.9 | 0.0 | 181.7 | 4.9 | 15.0 | 196.7 |
| Tanzania | 2411.6 | 570.1 | 6.3 | 2988.0 | 19.3 | 600.0 | 3588.0 |
| Zaire | 4058.9 | 762.1 | 0.0 | 4821.0 | 15.8 | 309.0 | 5130.0 |
| Zambia | 2520.3 | 693.6 | 0.0 | 3213.9 | 21.6 | 507.0 | 3720.9 |
| Zimbabwe | 651.3 | 874.8 | 45.1 | 1571.2 | 58.5 | 308.0 | 1879.2 |
| **W. AFRICA** | | | | | | | |
| Cameroon | 1569.6 | 405.0 | 381.1 | 2355.7 | 33.4 | 515.0 | 2870.7 |
| Congo | 943.5 | 816.9 | 0.0 | 1760.4 | 46.4 | 660.0 | 2420.4 |
| Cote d'Ivoire | 2618.3 | 3081.3 | 1400.0 | 7099.6 | 63.1 | 725.0 | 7824.6 |
| Ghana | 1026.4 | 143.7 | 0.0 | 1170.1 | 12.3 | 302.0 | 1472.1 |
| Guinea | 1076.3 | 215.9 | 0.0 | 1292.2 | 16.7 | 76.0 | 1368.2 |
| Liberia | 708.0 | 171.2 | 0.0 | 879.2 | 19.5 | 50.0 | 929.2 |
| Mauritania | 1228.2 | 134.8 | 0.0 | 1363.0 | 9.9 | 84.0 | 1447.0 |
| Nigeria | 2295.7 | 10719.9 | 416.0 | 13431.6 | 82.9 | 4916.0 | 18347.6 |
| Senegal | 1737.3 | 251.9 | 12.6 | 2001.8 | 13.2 | 211.0 | 2212.8 |
| **EMENA** | | | | | | | |
| Algeria | 2684.0 | 10980.0 | 0.0 | 13664.0 | 80.4 | 1862.0 | 15526.0 |
| Cyprus | 448.6 | 474.6 | 0.0 | 923.2 | 51.4 | 409.0 | 1332.2 |
| Egypt | 14803.4 | 2947.8 | 750.0 | 18501.2 | 20.0 | 5800.0 | 24301.2 |
| Hungary | 1297.4 | 8840.4 | 0.0 | 10137.8 | 87.2 | 1881.0 | 12018.8 |
| Jordan | 1840.2 | 852.7 | 0.0 | 2692.9 | 31.7 | 917.0 | 3609.9 |
| Morocco | 7179.2 | 4051.3 | 200.0 | 11430.5 | 37.2 | 1664.0 | 13094.5 |
| Oman | 366.3 | 1579.2 | 0.0 | 1945.5 | 81.2 | 422.0 | 2367.5 |
| Poland | — | — | — | — | — | — | — |
| Portugal | 2552.5 | 8250.3 | 519.0 | 11321.8 | 77.5 | 2610.0 | 13931.8 |
| Romania | 2732.5 | 3068.4 | 0.0 | 5800.9 | 52.9 | 516.0 | 6316.9 |
| Syria | 2607.7 | 143.2 | 0.0 | 2750.9 | 5.2 | 815.0 | 3565.9 |
| Tunisia | 3118.5 | 1323.5 | 246.0 | 4688.0 | 33.5 | 562.0 | 5250.0 |
| Turkey | 12370.5 | 5450.6 | 358.9 | 18180.0 | 32.0 | 6617.0 | 24797.0 |
| Yemen AR | 1854.7 | 13.1 | 0.0 | 1867.8 | 0.7 | 160.0 | 2027.8 |
| Yugoslavia | 4466.8 | 5452.4 | 6383.0 | 16302.2 | 72.6 | 972.0 | 17274.2 |
| **LAC** | | | | | | | |
| Argentina | 4145.8 | 31458.2 | 4575.1 | 40179.1 | 89.7 | 5953.0 | 46132.1 |
| Bahamas | 22.8 | 167.4 | 0.0 | 190.2 | 88.0 | 29.0 | 219.2 |
| Barbados | 175.6 | 176.3 | 0.0 | 351.9 | 50.1 | 48.0 | 399.9 |
| Belize | 78.5 | 15.6 | 0.0 | 94.1 | 16.6 | 13.0 | 107.1 |
| Bolivia | 2347.2 | 912.1 | 314.2 | 3573.5 | 34.3 | 347.0 | 3920.5 |
| Brazil | 14034.4 | 59859.2 | 17200.0 | 91093.6 | 84.6 | 11017.0 | 102110.6 |
| Chile | 2195.0 | 10539.5 | 4730.6 | 17465.1 | 87.4 | 1668.0 | 19133.1 |
| Colombia | 5160.7 | 4216.2 | 1568.3 | 10945.2 | 52.8 | 3099.0 | 14044.2 |
| Costa Rica | 1745.4 | 1919.8 | 296.6 | 3961.8 | 55.9 | 40.4 | 4002.2 |
| Dominican Rep. | 1751.9 | 768.9 | 150.6 | 2671.4 | 34.4 | 325.0 | 2996.4 |
| Ecuador | 1963.2 | 5157.9 | 69.8 | 7190.9 | 72.7 | 1683.0 | 8873.9 |
| El Salvador | 1310.0 | 150.4 | 104.2 | 1564.6 | 16.3 | 82.0 | 1646.6 |
| Guatemala | 1355.2 | 792.9 | 106.0 | 2254.1 | 39.9 | 225.8 | 2479.9 |
| Guyana | 571.7 | 171.0 | 0.0 | 742.7 | 23.0 | 155.0 | 897.7 |
| Honduras | 1716.9 | 461.5 | 141.4 | 2319.8 | 26.0 | 259.0 | 2578.8 |
| Jamaica | 2369.5 | 453.2 | 90.0 | 2912.7 | 18.6 | 169.0 | 3081.7 |
| Mexico | 8398.8 | 64111.1 | 16500.0 | 89009.9 | 90.6 | 5450.0 | 94459.9 |
| Nicaragua | 3411.2 | 1341.6 | 0.0 | 4752.8 | 28.2 | 862.0 | 5614.8 |
| Panama | 1144.3 | 2131.3 | 0.0 | 3275.6 | 65.1 | 1123.0 | 4398.6 |
| Paraguay | 1030.6 | 494.3 | 103.8 | 1628.7 | 36.7 | 151.0 | 1779.7 |
| Peru | 4762.4 | 5764.4 | 1342.0 | 11868.8 | 59.9 | 1117.0 | 12985.8 |
| Uruguay | 436.7 | 2249.3 | 60.4 | 2746.4 | 84.1 | 814.0 | 3560.4 |
| Venezuela | 140.6 | 16509.2 | 5150.0 | 21799.8 | 99.4 | 10279.0 | 32078.8 |
| **E. ASIA & PACIFIC** | | | | | | | |
| China | 4419.0 | 2601.2 | 0.0 | 7020.2 | 37.1 | 0.0 | 7020.2 |
| Fiji | 229.0 | 73.2 | 108.0 | 410.2 | 44.2 | 19.0 | 429.2 |
| Indonesia | 14956.7 | 11667.9 | 3810.0 | 30434.6 | 50.9 | 5280.0 | 35714.6 |
| Korea | 10158.6 | 18967.3 | 6630.1 | 35756.0 | 71.6 | 10732.0 | 46488.0 |
| Malaysia | 3269.7 | 10564.4 | 4131.7 | 17965.8 | 81.8 | 1658.0 | 19623.8 |
| Papua New Guinea | 495.7 | 565.3 | 1020.4 | 2081.4 | 76.2 | 146.0 | 2227.4 |
| Philippines | 6882.3 | 6679.1 | 2998.0 | 16559.4 | 58.4 | 8573.0 | 25132.4 |
| Thailand | 5745.2 | 4153.2 | 3369.9 | 13268.3 | 56.7 | 3200.0 | 16468.3 |
| **S. ASIA** | | | | | | | |
| India | 23200.6 | 3448.8 | 3093.0 | 29742.4 | 22.0 | 1516.0 | 31258.4 |
| Pakistan | 9945.1 | 736.4 | 25.6 | 10707.1 | 7.1 | 722.0 | 11429.1 |
| Sri Lanka | 2167.9 | 647.3 | 98.5 | 2913.7 | 25.6 | 299.0 | 3212.7 |

— Data not available in Debtor Reporting System.
/a World Debt Tables, 1986-87; short-term debt estimates are based on data supplied by the BIS.
/b For some [illegible] estimated by EPD.

Table 4: EXTERNAL DEBT OUTSTANDING AND FINANCIAL FLOWS OF DEVELOPING COUNTRIES, 1975-85/a
(US $ Billion)

| | Debt Outstanding and Disbursed | | | Amortization | | | Interest | | | Net Transfer | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 1975 | 1980 | 1985 | 1975 | 1980 | 1985 | 1975 | 1980 | 1985 | 1975 | 1980 | 1985 |
| All Developing Countries/b | 162.5 | 429.2 | 730.9 | 14.7 | 41.9 | 53.5 | 8.3 | 31.1 | 54.4 | 21.3 | 28.8 | -26.3 |
| Private Sources | 90.9 | 267.6 | 462.8 | 11.7 | 34.7 | 40.0 | 6.2 | 26.0 | 43.0 | 11.5 | 13.9 | -31.0 |
| Official Sources | 71.6 | 161.6 | 268.1 | 3.0 | 7.2 | 13.5 | 2.1 | 5.1 | 11.4 | 9.8 | 14.9 | 4.7 |
| Major Borrowers/c | 97.9 | 240.3 | 430.4 | 8.6 | 24.3 | 27.4 | 5.5 | 20.0 | 36.3 | 11.5 | 10.2 | -22.9 |
| Private Sources | 57.4 | 162.3 | 311.5 | 7.0 | 20.9 | 21.3 | 4.3 | 16.9 | 30.5 | 6.4 | 5.8 | -22.5 |
| Official Sources | 40.5 | 78.0 | 118.9 | 1.6 | 3.4 | 6.1 | 1.2 | 3.1 | 5.8 | 5.1 | 4.4 | -0.4 |
| Low Income Africa | 10.4 | 26.3 | 37.3 | 0.6 | 1.2 | 1.3 | 0.3 | 0.9 | 0.9 | 1.9 | 3.3 | 0.8 |
| Private Sources | 4.0 | 8.0 | 6.5 | 0.4 | 0.8 | 0.5 | 0.2 | 0.5 | 0.3 | 0.7 | 0.8 | -0.4 |
| Official Sources | 6.4 | 18.3 | 30.8 | 0.2 | 0.4 | 0.8 | 0.1 | 0.4 | 0.6 | 1.2 | 2.5 | 1.2 |
| Low Income Asia | 20.1 | 34.1 | 60.0 | 0.9 | 1.2 | 3.2 | 0.5 | 0.9 | 2.0 | 2.3 | 3.9 | 3.5 |
| Private Sources | 1.1 | 2.4 | 11.2 | 0.3 | 0.3 | 1.8 | 0.1 | 0.2 | 0.9 | 0.0 | 0.9 | 0.4 |
| Official Sources | 19.0 | 31.7 | 48.8 | 0.6 | 0.9 | 1.4 | 0.4 | 0.7 | 1.1 | 2.3 | 3.0 | 3.1 |
| Middle Income Oil Importers | 90.7 | 248.8 | 428.9 | 9.5 | 24.7 | 30.4 | 5.5 | 20.0 | 34.0 | 9.2 | 16.6 | -14.6 |
| Private Sources | 59.7 | 171.8 | 291.6 | 7.8 | 20.4 | 22.7 | 4.3 | 16.2 | 26.6 | 6.0 | 9.8 | -14.6 |
| Official Sources | 31.0 | 77.0 | 137.3 | 1.7 | 4.3 | 7.7 | 1.2 | 3.8 | 7.4 | 3.2 | 6.8 | 0.1 |
| Oil Exporters | 41.4 | 120.0 | 204.8 | 4.0 | 14.7 | 18.5 | 2.1 | 10.4 | 17.6 | 7.9 | 5.0 | -15.9 |
| Private Sources | 26.2 | 85.4 | 153.6 | 3.4 | 13.1 | 14.8 | 1.7 | 9.1 | 15.3 | 4.8 | 2.4 | -16.3 |
| Official Sources | 15.2 | 34.6 | 51.2 | 0.6 | 1.6 | 3.7 | 0.4 | 1.3 | 2.3 | 3.1 | 2.6 | 0.4 |
| Highly Indebted Countries /d | 76.7 | 203.6 | 367.5 | 8.9 | 24.6 | 17.1 | 5.2 | 19.7 | 33.0 | 7.6 | 8.8 | -27.7 |
| Private Sources | 57.1 | 166.4 | 296.4 | 7.7 | 22.0 | 12.3 | 4.3 | 17.5 | 29.1 | 5.8 | 6.3 | -27.7 |
| Official Sources | 19.6 | 37.2 | 71.1 | 1.2 | 2.6 | 4.8 | 0.9 | 2.2 | 3.9 | 1.8 | 2.5 | 0.0 |

Source: World Debt Tables, 1986-87 (forthcoming).
/a Covers public, publicly guaranteed and private non-guaranteed MLT debt.
/b Covers all countries included in the World Debt Tables, 1986-87 (forthcoming).
/c Namely Argentina, Brazil, Chile, Egypt, India, Indonesia, Israel, Korea, Malaysia, Mexico, Turkey and Venezuela.
/d Namely, Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Cote d'Ivoire, Ecuador, Jamaica, Mexico, Morocco, Nigeria, Peru, Philippines, Uruguay, Venezuela, Yugoslavia.

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Table 5: AVERAGE TERMS OF BORROWING (COMMITMENTS OF PUBLIC AND PUBLICLY GUARANTEED DEBT), 1975-85

| | 1975 | 1980 | 1982 | 1983 | 1984 | 1985 |
|---|---|---|---|---|---|---|
| All Developing Countries/a | | | | | | |
| Interest Rate (%) | 7.0 | 9.3 | 10.5 | 9.1 | 9.2 | 8.0 |
| Maturity (Years) | 16.3 | 15.9 | 14.1 | 14.0 | 15.5 | 16.1 |
| Grace Period (Years) | 5.3 | 4.9 | 4.4 | 4.3 | 5.0 | 5.6 |
| Grant Element (%)/c | 19.4 | 8.5 | 1.3 | 7.3 | 7.7 | 13.2 |
| Major Borrowers/b | | | | | | |
| Interest Rate (%) | 7.5 | 10.1 | 11.9 | 10.0 | 10.2 | 8.6 |
| Maturity (Years) | 15.6 | 16.1 | 12.4 | 12.9 | 14.8 | 15.7 |
| Grace Period (Years) | 5.7 | 5.3 | 4.3 | 4.4 | 5.5 | 5.9 |
| Grant Element (%)/c | 15.7 | 4.4 | -6.8 | 1.7 | 0.7 | 9.1 |
| Low Income Africa | | | | | | |
| Interest Rate (%) | 5.0 | 5.0 | 4.5 | 3.5 | 4.1 | 3.0 |
| Maturity (Years) | 22.1 | 21.5 | 27.6 | 27.9 | 29.9 | 32.9 |
| Grace Period (Years) | 6.0 | 5.6 | 6.8 | 6.6 | 6.7 | 7.6 |
| Grant Element (%)/c | 35.5 | 36.0 | 42.4 | 48.6 | 46.3 | 56.6 |
| Low Income Asia | | | | | | |
| Interest Rate (%) | 2.5 | 4.6 | 5.8 | 5.4 | 5.8 | 5.3 |
| Maturity (Years) | 31.8 | 28.1 | 27.7 | 26.5 | 26.8 | 29.0 |
| Grace Period (Years) | 8.1 | 6.5 | 6.9 | 6.4 | 6.7 | 7.1 |
| Grant Element (%)/c | 59.5 | 44.4 | 36.3 | 37.8 | 34.8 | 38.4 |
| Middle Income Oil Importers | | | | | | |
| Interest Rate (%) | 8.0 | 10.8 | 11.0 | 9.6 | 10.1 | 8.7 |
| Maturity (Years) | 14.5 | 13.6 | 12.5 | 12.7 | 12.5 | 13.0 |
| Grace Period (Years) | 4.3 | 4.5 | 3.9 | 4.1 | 4.5 | 5.4 |
| Grant Element (%)/c | 10.5 | -1.4 | -3.9 | 3.0 | 0.6 | 7.2 |
| Oil Exporters | | | | | | |
| Interest Rate (%) | 7.2 | 9.6 | 11.8 | 10.1 | 9.8 | 8.4 |
| Maturity (Years) | 13.7 | 13.7 | 11.0 | 10.8 | 14.0 | 14.4 |
| Grace Period (Years) | 5.7 | 4.9 | 4.3 | 3.8 | 4.9 | 4.9 |
| Grant Element (%)/c | 17.1 | 5.5 | -5.2 | 0.5 | 2.1 | 7.8 |
| Highly Indebted Countries /d | | | | | | |
| Interest Rate (%) | 8.3 | 11.8 | 12.6 | 10.6 | 11.3 | 9.4 |
| Maturity (Years) | 10.5 | 10.6 | 9.9 | 10.0 | 11.5 | 12.3 |
| Grace Period (Years) | 3.2 | 4.0 | 3.6 | 3.1 | 4.2 | 3.4 |
| Grant Element (%)/c | 8.0 | -7.5 | -10.2 | -1.7 | -6.1 | 2.8 |

Source: World Debt Tables, 1986-87 (forthcoming).

/a Covers all countries included in the World Debt Tables, 1986-87.

/b Namely, Argentina, Brazil, Chile, Egypt, India, Indonesia, Israel, Korea, Malaysia, Mexico, Turkey and Venezuela.

/c Refers to concessionality of loans using a discount rate of 10%.

/d Namely Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Cote d'Ivoire, Ecuador, Jamaica, Mexico, Morocco, Nigeria, Peru, Philippines, Uruguay, Venezuela, Yugoslavia.

Table 6: CURRENT BANK GROUP BORROWERS WITH IMF STANDBY AND EFF ARRANGEMENTS IN EFFECT AS OF DECEMBER 31, 1986

| COUNTRY | Standby | | | | | CFF | Remarks |
|---|---|---|---|---|---|---|---|
| | Date of Arrangement | Expiration Date | Amount (SDRm) | % of Quota | Balance (SDRm) | 1986 Amount (SDRm) | |
| E. AFRICA | | | | | | | |
| Burundi | 08/08/86 | 03/31/88 | 21.0 | 49 | 21.0 | | Standby review completed, revised targets are being negotiated. |
| Ethiopia | | | | | | 35.3 | |
| Madagascar | 09/17/86 | 02/16/88 | 30.0 | 45 | 25.0 | 16.1 | Standby review completed in December, satisfactory performance. |
| Tanzania | 08/28/86 | 02/27/88 | 64.2 | 60 | 31.2 | | Program is on track. |
| Zaire | 05/28/86 | 03/27/88 | 214.2 | 74 | 166.6 | | Program suspended, arrears have developed, but a new program is being negotiated. |
| Zambia | 02/21/86 | 02/28/88 | 229.8 | 85 | 194.8 | 68.8 | Arrears have developed and a revised program is being considered. |
| W. AFRICA | | | | | | | |
| C.A.R. | 09/23/85 | 03/22/87 | 15.0 | 49 | 7.5 | | Standby suspended December 1986 due to non-compliance. New standby under discussion. SAF credit to be approved shortly. |
| Congo | 08/29/86 | 08/28/88 | 22.4 | 60 | 12.9 | | Out of compliance at December 1986 review. Discussions under way. |
| Cote d'Ivoire | 06/23/86 | 06/22/88 | 100.0 | 60 | 76.0 | | Slippages in implementation in 1986. 1987 program not yet agreed. |
| Gabon | 12/22/86 | 12/31/88 | 98.7 | 135 | 71.3 | | Standby just approved. |
| Gambia | 09/17/86 | 10/16/87 | 5.1 | 30 | 4.1 | 4.7 | Technical slip in performance prevented release of December 1986 tranche. Waiver expected in March 1987. |
| Ghana | 10/15/86 | 10/14/87 | 81.8 | 40 | 49.1 | | Policy and monitoring slippages in 1986. February 1987 drawing delayed pending new discussions. |
| Guinea | 02/03/86 | 03/02/87 | 33.0 | 57 | 18.0 | | 1986 program confronted with major difficulties in policy area, currently being resolved. New standby and SAF to be discussed shortly. |
| Mali | 11/08/85 | 03/31/87 | 22.9 | 45 | 6.6 | | Out of compliance on credit ceilings in last two quarters. New standby under negotiation. |
| Mauritania | 04/26/86 | 04/25/87 | 12.0 | 35 | 2.7 | | In good standing. New standby being prepared. |
| Niger | 12/05/86 | 12/04/87 | 10.1 | 30 | 8.1 | | New standby. |
| Nigeria | 01/30/87 | 01/30/88 | 650.0 | 77 | | | Standby just approved. Nigeria doesn't intend to draw on it. |
| Senegal | 11/10/86 | 11/09/87 | 34.0 | 40 | 22.6 | | New standby. |
| Sierra Leone | 11/14/86 | 11/13/87 | 23.2 | 40 | 15.2 | | New standby. |
| Togo | 06/09/86 | 04/08/88 | 23.0 | 60 | 14.4 | | December 1986 review incomplete. Targets to be renegotiated. |
| EMENA | | | | | | | |
| Morocco | 12/16/86 | 03/31/87 | 230.0 | 75 | 200.0 | | In compliance. |
| Tunisia | 11/04/86 | 05/03/88 | 103.7 | 75 | 68.7 | 114.7 | In compliance. |
| LAC | | | | | | | |
| Argentina | Feb.1987 | 12/31/87 | 1200.0 | 108 | | | Agreement on Letter of Development Policy reached in Jan. 1987. Standby expected in February. |
| Bolivia | 06/19/86 | 06/18/86 | 50.0 | 55 | 17.3 | 64.1 | OK. |
| Chile /a | 08/15/85 | 08/14/88 | 750.0 | 170 | 375.0 | | |
| Ecuador | 08/15/86 | 08/14/87 | 75.4 | 50 | 60.3 | 39.7 | |
| Mexico | 11/19/86 | 04/01/88 | 1400.0 | 120 | 950.0 | | |
| Panama | 07/15/85 | 03/31/87 | 90.0 | 88 | 11.0 | | |
| Uruguay | 09/27/85 | 03/26/87 | 122.9 | 75 | 35.1 | | OK. |
| E.ASIA & PACIFIC | | | | | | | |
| China | 11/12/86 | 11/11/87 | 597.7 | 25 | | | Progressing well; an informal review by the IMF is scheduled for March 1987. |
| Korea | 07/12/85 | 03/10/87 | 280.0 | 61 | 120.0 | | In full compliance with IMF targets; there is no intention to renegotiate another agreement. |
| Philippines | 10/24/86 | 04/23/88 | 198.0 | 45 | 193.0 | 224.1 | An IMF review is due shortly; indications are that the arrangement has progressed well thus far. |
| S.ASIA | | | | | | | |
| Bangladesh | 12/02/85 | 06/30/87 | 180.0 | 63 | 48.0 | | |
| Nepal | 12/23/85 | 04/22/87 | 18.7 | 50 | 6.3 | | |
| **SAF ARRANGEMENTS** | | | | | | | |
| E. AFRICA | | | | | | | |
| Burundi | 08/08/86 | 08/07/89 | 20.1 | 47 | 11.5 | | |
| W. AFRICA | | | | | | | |
| Gambia | 09/17/86 | 09/16/89 | 8.0 | 47 | 4.6 | | |
| Mauritania | 09/22/86 | 09/21/89 | 15.9 | 47 | 9.2 | | |
| Niger | 11/17/86 | 11/16/89 | 15.8 | 47 | 9.1 | | |
| Senegal | 11/10/86 | 10/31/89 | 40.0 | 47 | 23.0 | | |
| Sierra Leone | 11/14/86 | 11/13/89 | 27.2 | 47 | 15.6 | | |
| LAC | | | | | | | |
| Bolivia | 12/15/86 | 12/14/89 | 42.6 | 47 | 24.5 | | |
| Dominica | 11/26/86 | 11/25/89 | 1.9 | 48 | 1.1 | | |
| Haiti | 12/17/86 | 12/16/89 | 20.7 | 31 | 11.9 | | |

Source: IMF.

/a EFF

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Table 7: MULTILATERAL DEBT RENEGOTIATIONS, 1982-DECEMBER 31, 1986/a
(US $ Million)

| Type of Creditor /Country | 1982 | | 1983 | | 1984 | | 1985 | | 1986 | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Official Creditor | Commercial Bank | Official Creditor | Commercial Bank | Official Creditor | Commercial Bank | Official Creditor | Commercial Bank | Official Creditor | Commercial 1986 |
| Argentina | | | | 1300 | | | 2123 | 13400 | | |
| Bolivia | | | | | | | | | 100 | |
| Brazil | | | 3478 | 20252 | | 19946 | | | | 15971 |
| Central African Rep. | | | 13 | | | | 14 | | | |
| Chile | | | | 2169 | | 1160 | 176 | 6007 | | |
| Congo | | | | | | | | | 580 | 221 |
| Costa Rica | | | 97 | 709 | | | 166 | 440 | | |
| Cote d'Ivoire | | | | | 218 | | 229 | 501 | 370 | 691 |
| Cuba | | | | 128 | | | | 85 | | |
| Dominican Republic | | | | | | | 296 | | | 787 |
| Ecuador | | | 200 | 1835 | | | 400 | 4260 | | |
| Eq. Guinea | | | | | | | 29 | | | |
| Gambia | | | | | | | | | 25 | |
| Guinea | | | | | | | | | 196 | |
| Guyana | | 14 | | 41 | | 72 | | 57 | | |
| Honduras | | | | 120 | | 368 | | | | |
| Jamaica | | | | | 106 | 164 | 70 | 195 | | |
| Liberia | | 27 | 18 | | 17 | | | | | |
| Madagascar | 103 | | | | 146 | 195 | 135 | | 135 | |
| Malawi | 24 | | 30 | 57 | | | | | | |
| Mauritania | | | | | | | 77 | | 27 | |
| Mexico | | | 1550 | 20167 | | | | 49650 | 1000 | 43700 |
| Morocco | | | 1225 | | | | 1000 | | | 1738 |
| Mozambique | | | | | 200 | | | | | |
| Nicaragua | | 100 | | | | 145 | | | | |
| Niger | | | 33 | | 39 | 27 | 32 | | 39 | |
| Nigeria | | | | 1935 | | | | | 3300 | 3700 |
| Panama | | | | | | | 15 | 602 | | |
| Peru | | | 450 | 580 | 1000 | 1425 | | | | |
| Philippines | | | | | 936 | | | 5885 | | |
| Poland | | 4182 | | 1192 | | 1390 | 10300 | | 1400 | 2000 |
| Romania | 234 | 1598 | 195 | 567 | | | | | | 800 |
| Senegal | 84 | | 64 | | | 78 | 105 | 20 | 86 | |
| Sierra Leone | | | | | 88 | 20 | | | 50 | |
| Somalia | | | | | | | 142 | | | |
| Sudan | 174 | 55 | 502 | 790 | 179 | 838 | | 920 | | |
| Tanzania | | | | | | | | | 40 | |
| Togo | | | 114 | 84 | 51 | | 22 | | | |
| Turkey | | 2269 | | | | | | | | |
| Uganda | 22 | | | | | | | | | |
| Uruguay | | | | 575 | | | | | | 1958 |
| Venezuela | | | | | | | | | | 21203 |
| Yugoslavia | | | | 1750 | 750 | 1250 | 625 | 3600 | 401 | |
| Zaire | | | 1317 | 58 | | 64 | 423 | 61 | 429 | 65 |
| Zambia | | | 285 | | 164 | 74 | | | 371 | |
| Total | 641 | 8245 | 9571 | 54309 | 3894 | 27216 | 16379 | 85683 | 8549 | 92834 |

/a Amounts shown exclude new money.
Source: World Debt Tables 1986-87.

11-Feb-87

Table 8: PROJECTED NET DISBURSEMENTS AND NET TRANSFERS
(BASE CASE)
(US $ million)

| | | NET DISBURSEMENTS | | | | | | | | | NET TRANSFERS | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | Bank | | | IDA | | | Total | | | Bank | | | IDA | | | Total | | |
| | Risk Category | FY87 | FY90 | FY93 | FY87 | FY90 | FY93 | FY87 | FY90 | FY93 | FY87 | FY90 | FY93 | FY87 | FY90 | FY93 | FY87 | FY90 | FY93 |
| **EAST AFRICA** | | | | | | | | | | | | | | | | | | | |
| Botswana | IIb | -4 | 2 | -1 | 0 | 0 | 0 | -4 | 2 | -1 | -17 | -10 | -13 | 0 | 0 | 0 | -17 | -10 | -13 |
| Ethiopia | IIIa | -9 | -6 | -4 | 47 | 72 | 81 | 38 | 66 | 77 | -12 | -7 | -5 | 42 | 64 | 71 | 30 | 57 | 66 |
| Kenya | IIIb | -4 | -50 | -50 | 32 | 48 | 65 | 28 | -2 | 15 | -81 | -122 | -108 | 27 | 42 | 56 | -54 | -80 | -52 |
| Lesotho | IIIa | 0 | 3 | 10 | 4 | 6 | 5 | 4 | 9 | 15 | 0 | 2 | 8 | 4 | 5 | 4 | 4 | 7 | 12 |
| Malawi | IIIb | 0 | 1 | -8 | 69 | 56 | 62 | 69 | 57 | 54 | -7 | -6 | -14 | 66 | 52 | 56 | 59 | 46 | 42 |
| Mauritius | IIb | 6 | 7 | 12 | 0 | 0 | 0 | 6 | 7 | 12 | -7 | -7 | -5 | 0 | 0 | -1 | -7 | -7 | -6 |
| Seychelles | IIc | 1 | 0 | -1 | 0 | 0 | 0 | 1 | 0 | -1 | 0 | -1 | -1 | 0 | 0 | 0 | 0 | -1 | -1 |
| Sudan | IIIc | -5 | -8 | -4 | 48 | 50 | 66 | 43 | 42 | 62 | -7 | -9 | -4 | 42 | 43 | 57 | 35 | 34 | 53 |
| Swaziland | IIc | -1 | -3 | 5 | 0 | 0 | 0 | -1 | -3 | 5 | -6 | -7 | 1 | 0 | 0 | 0 | -6 | -7 | 1 |
| Tanzania | IIIc | -23 | -25 | -25 | 52 | 65 | 70 | 29 | 40 | 45 | -43 | -40 | -34 | 47 | 58 | 61 | 4 | 18 | 27 |
| Zaire | IIIc | -8 | 6 | -4 | 97 | 141 | 164 | 89 | 147 | 160 | -13 | 1 | -9 | 91 | 132 | 151 | 78 | 133 | 142 |
| Zambia | IIIc | -4 | -37 | -43 | 123 | 89 | 97 | 119 | 52 | 54 | -39 | -65 | -62 | 121 | 86 | 91 | 82 | 21 | 29 |
| Zimbabwe | IIIa | 38 | 33 | 64 | 5 | 1 | 0 | 43 | 34 | 64 | 10 | -10 | 12 | 5 | 1 | 0 | 15 | -9 | 12 |
| **WESTERN AFRICA** | | | | | | | | | | | | | | | | | | | |
| Cameroon | IIc | 16 | 37 | 15 | 1 | -2 | -3 | 17 | 35 | 12 | -20 | -5 | -32 | 0 | -3 | -4 | -20 | -8 | -36 |
| Congo | IIIb | 3 | 13 | 41 | 1 | 0 | -1 | 4 | 13 | 40 | -4 | -2 | 16 | 1 | 0 | -1 | -3 | -2 | 15 |
| Cote d'Ivoire | IIIb | 190 | 89 | 29 | 0 | 0 | 0 | 190 | 89 | 29 | 69 | -75 | -132 | 0 | 0 | 0 | 69 | -75 | -132 |
| Ghana | IIIc | -13 | -9 | -10 | 121 | 135 | 128 | 108 | 126 | 118 | -23 | -17 | -16 | 117 | 128 | 119 | 94 | 111 | 103 |
| Guinea | IIIc | -8 | -10 | -6 | 43 | 54 | 70 | 35 | 44 | 64 | -12 | -12 | -6 | 42 | 51 | 65 | 30 | 39 | 59 |
| Liberia | IIIc | -6 | -12 | -10 | 9 | 11 | 8 | 3 | -1 | -2 | -16 | -19 | -15 | 8 | 10 | 7 | -8 | -9 | -8 |
| Mauritania | IIIc | 7 | -9 | -9 | 9 | 10 | 13 | 16 | 1 | 4 | 2 | -14 | -11 | 8 | 8 | 12 | 10 | -6 | 1 |
| Nigeria | IIIb | 220 | 609 | 592 | -1 | -1 | -1 | 219 | 608 | 591 | 49 | 326 | 173 | -1 | -1 | -1 | 48 | 325 | 172 |
| Senegal | IIIc | -1 | -9 | -10 | 87 | 43 | 67 | 86 | 34 | 57 | -10 | -16 | -15 | 84 | 40 | 62 | 74 | 24 | 47 |
| **EMENA** | | | | | | | | | | | | | | | | | | | |
| Algeria | IIc | 25 | 32 | 68 | 0 | 0 | 0 | 25 | 32 | 68 | -29 | -31 | -6 | 0 | 0 | 0 | -29 | -31 | -6 |
| Cyprus | IIa | -7 | -1 | -8 | 0 | 0 | 0 | -7 | -1 | -8 | -15 | -8 | -13 | 0 | 0 | 0 | -15 | -8 | -13 |
| Egypt | IIIb | 155 | 195 | 104 | 25 | 3 | -7 | 180 | 198 | 97 | 22 | 2 | -110 | 20 | -2 | -12 | 42 | 0 | -122 |
| Hungary | IIc | 196 | 174 | 5 | 0 | 0 | 0 | 196 | 174 | 5 | 147 | 82 | -96 | 0 | 0 | 0 | 147 | 82 | -96 |
| Iran | IIIc | -66 | -56 | -12 | 0 | 0 | 0 | -66 | -56 | -12 | -90 | -65 | -13 | 0 | 0 | 0 | -90 | -65 | -13 |
| Iraq | IIIc | -6 | -7 | -4 | 0 | 0 | 0 | -6 | -7 | -4 | -10 | -10 | -6 | 0 | 0 | 0 | -10 | -10 | -6 |
| Jordan | IIb | 36 | 15 | 21 | -1 | -1 | -2 | 35 | 14 | 19 | 9 | -14 | -11 | -1 | -2 | -2 | 8 | -16 | -13 |
| Lebanon | IIIc | -3 | 10 | 61 | 0 | 0 | 0 | -3 | 10 | 61 | -6 | 5 | 48 | 0 | 0 | 0 | -6 | 5 | 48 |
| Morocco | IIIb | 248 | 108 | 152 | -1 | -1 | -1 | 247 | 107 | 151 | 92 | -104 | -97 | -1 | -1 | -1 | 91 | -105 | -98 |
| Oman | IIc | 3 | -1 | -4 | 0 | 0 | 0 | 3 | -1 | -4 | -2 | -6 | -8 | 0 | 0 | 0 | -2 | -6 | -8 |
| Poland | IIIb | 0 | 201 | 184 | 0 | 0 | 0 | 0 | 201 | 184 | 0 | 180 | 116 | 0 | 0 | 0 | 0 | 180 | 116 |
| Portugal | IIc | 6 | -22 | -43 | 0 | 0 | 0 | 6 | -22 | -43 | -34 | -58 | -74 | 0 | 0 | 0 | -34 | -58 | -74 |
| Romania | IIIa | -222 | -178 | -131 | 0 | 0 | 0 | -222 | -178 | -131 | -378 | -284 | -197 | 0 | 0 | 0 | -378 | -284 | -197 |
| Syria | IIIb | -14 | 9 | 30 | -1 | -1 | -1 | -15 | 8 | 29 | -45 | -22 | -6 | -1 | -1 | -1 | -46 | -23 | -7 |
| Tunisia | IIc | 133 | 145 | 43 | -1 | -1 | -2 | 132 | 144 | 41 | 61 | 41 | -72 | -1 | -2 | -2 | 60 | 39 | -74 |
| Turkey | IIIa | 505 | 480 | 281 | -4 | -4 | -6 | 501 | 476 | 275 | 78 | -29 | -285 | -5 | -5 | -6 | 73 | -34 | -291 |
| Yemen A R | IIIa | 0 | 9 | 19 | 24 | 25 | 22 | 24 | 34 | 41 | 0 | 8 | 14 | 22 | 22 | 18 | 22 | 30 | 32 |
| Yugoslavia | IIIa | -120 | -112 | -129 | 0 | 0 | 0 | -120 | -112 | -129 | -349 | -304 | -287 | 0 | 0 | 0 | -349 | -304 | -287 |
| **LAC** | | | | | | | | | | | | | | | | | | | |
| Argentina | IIIa | 271 | 324 | 280 | 0 | 0 | 0 | 271 | 324 | 280 | 172 | 154 | 30 | 0 | 0 | 0 | 172 | 154 | 30 |
| Bahamas | IIa | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | -2 | -1 | -1 | 0 | 0 | 0 | -2 | -1 | -1 |
| Barbados | IIa | -1 | -1 | 1 | 0 | 0 | 0 | -1 | -1 | 1 | -4 | -5 | -2 | 0 | 0 | 0 | -4 | -5 | -2 |
| Belize | IIc | 0 | 1 | 1 | 0 | 0 | 0 | 0 | 1 | 1 | 0 | 1 | 0 | 0 | 0 | 0 | 0 | 1 | 0 |
| Bolivia | IIIc | -16 | -20 | -18 | 14 | 34 | 39 | -2 | 14 | 21 | -35 | -34 | -28 | 13 | 31 | 36 | -22 | -3 | 8 |
| Brazil | IIIa | 629 | 463 | 259 | 0 | 0 | 0 | 629 | 463 | 259 | -6 | -264 | -501 | 0 | 0 | 0 | -6 | -264 | -501 |
| Chile | IIIb | 334 | 44 | 102 | -1 | -1 | -1 | 333 | 43 | 101 | 260 | -71 | -25 | -1 | -1 | -1 | 259 | -72 | -26 |
| Colombia | IIc | 113 | 55 | 12 | -1 | -1 | -1 | 112 | 54 | 11 | -166 | -250 | -302 | -1 | -1 | -1 | -167 | -251 | -303 |
| Costa Rica | IIIb | -16 | 18 | -16 | 0 | 0 | 0 | -16 | 18 | -16 | -49 | -12 | -42 | 0 | 0 | 0 | -49 | -12 | -42 |
| Dominican Rep. | IIIb | -1 | 6 | 10 | 0 | 0 | -1 | -1 | 6 | 9 | -16 | -11 | -9 | 0 | 0 | -1 | -16 | -11 | -10 |
| Ecuador | IIIb | 48 | 41 | 35 | -1 | -1 | -1 | 47 | 40 | 34 | 8 | -10 | -21 | -1 | -1 | -1 | 7 | -11 | -22 |
| El Salvador | IIIb | -7 | 12 | 5 | 0 | 0 | -1 | -7 | 12 | 4 | -17 | 1 | -9 | -1 | -1 | -1 | -18 | 0 | -10 |
| Guatemala | IIIb | 2 | 78 | 5 | 0 | 0 | 0 | 2 | 78 | 5 | -20 | 46 | -31 | 0 | 0 | 0 | -20 | 46 | -31 |
| Guyana | IIIc | -5 | -7 | -5 | 2 | 1 | 0 | -3 | -6 | -5 | -10 | -11 | -8 | 2 | 1 | 0 | -8 | -10 | -8 |
| Honduras | IIIb | -11 | -9 | 4 | -1 | -1 | -1 | -12 | -10 | 3 | -48 | -44 | -32 | -1 | -1 | -2 | -49 | -45 | -34 |
| Jamaica | IIIb | -9 | -31 | -27 | 0 | 0 | 0 | -9 | -31 | -27 | -60 | -74 | -63 | 0 | 0 | 0 | -60 | -74 | -63 |
| Mexico | IIIb | 715 | 518 | 312 | 0 | 0 | 0 | 715 | 518 | 312 | 255 | -55 | -357 | 0 | 0 | 0 | 255 | -55 | -357 |
| Nicaragua | IIIc | -13 | -14 | -14 | 0 | 0 | -1 | -13 | -14 | -15 | -28 | -25 | -22 | -1 | -1 | -1 | -29 | -26 | -23 |
| Panama | IIIa | 15 | 22 | -20 | 0 | 0 | 0 | 15 | 22 | -20 | -18 | -16 | -52 | 0 | 0 | 0 | -18 | -16 | -52 |
| Paraguay | IIIb | 5 | -23 | -33 | -1 | -1 | -1 | 4 | -24 | -34 | -23 | -46 | -49 | -1 | -1 | -1 | -24 | -47 | -50 |
| Peru | IIIc | 74 | -74 | -97 | 0 | 0 | 0 | 74 | -74 | -97 | -13 | -157 | -154 | 0 | 0 | 0 | -13 | -157 | -154 |
| St. Lucia | IIIb | 0 | 1 | 0 | 0 | 0 | 0 | 0 | 1 | 0 | 0 | 1 | 0 | 0 | 0 | 0 | 0 | 1 | 0 |
| St. Vincent | IIIb | 0 | 0 | 1 | 1 | 0 | 0 | 1 | 0 | 1 | 0 | 0 | 1 | 1 | 0 | 0 | 1 | 0 | 1 |
| Uruguay | IIIa | 7 | 1 | 10 | 0 | 0 | 0 | 7 | 1 | 10 | -11 | -24 | -16 | 0 | 0 | 0 | -11 | -24 | -16 |
| Venezuela | IIIa | -23 | 0 | 0 | 0 | 0 | 0 | -23 | 0 | 0 | -24 | 0 | 0 | 0 | 0 | 0 | -24 | 0 | 0 |
| **E.ASIA & PACIFIC** | | | | | | | | | | | | | | | | | | | |
| China | IIa | 317 | 795 | 1287 | 295 | 401 | 403 | 612 | 1196 | 1690 | 214 | 551 | 794 | 282 | 379 | 372 | 496 | 930 | 1166 |
| Fiji | IIa | -3 | -5 | -6 | 0 | 0 | 0 | -3 | -5 | -6 | -9 | -9 | -9 | 0 | 0 | 0 | -9 | -9 | -9 |
| Indonesia | IIc | 709 | 340 | 582 | 3 | -8 | -17 | 712 | 332 | 565 | 223 | -253 | -103 | -2 | -13 | -21 | 221 | -266 | -124 |
| Korea | I | -134 | -223 | -255 | -2 | -2 | -3 | -136 | -225 | -258 | -505 | -541 | -507 | -2 | -3 | -4 | -507 | -544 | -511 |
| Malaysia | IIb | -18 | 27 | 77 | 0 | 0 | 0 | -18 | 27 | 77 | -93 | -61 | -20 | 0 | 0 | 0 | -93 | -61 | -20 |
| PNG | IIIa | 17 | 45 | 49 | 0 | -1 | -2 | 17 | 44 | 47 | 8 | 29 | 21 | -1 | -1 | -2 | 7 | 28 | 19 |
| Philippines | IIIb | 108 | -31 | 90 | 8 | 2 | 0 | 116 | -29 | 90 | -151 | -314 | -204 | 7 | 1 | -1 | -144 | -313 | -205 |
| Thailand | IIa | 27 | -126 | -94 | 2 | 0 | -1 | 29 | -126 | -95 | -216 | -349 | -286 | 1 | -1 | -2 | -215 | -350 | -288 |
| **SOUTH ASIA** | | | | | | | | | | | | | | | | | | | |
| India | IIb | 593 | 1333 | 1054 | 805 | 602 | 429 | 1398 | 1935 | 1483 | 252 | 741 | 215 | 724 | 513 | 332 | 976 | 1254 | 547 |
| Pakistan | IIIa | 191 | 247 | 195 | 120 | 132 | 119 | 311 | 379 | 314 | 129 | 118 | 18 | 105 | 114 | 98 | 234 | 232 | 116 |
| Sri Lanka | IIIb | 0 | 7 | 5 | 80 | 69 | 62 | 80 | 76 | 67 | -8 | -1 | -4 | 75 | 63 | 54 | 67 | 62 | 50 |
| **SUM OF THE ABOVE** | | 5182 | 5437 | 5011 | 2111 | 2022 | 1916 | 7293 | 7459 | 6927 | -747 | -1728 | -3153 | 1931 | 1802 | 1651 | 1184 | 74 | -1502 |
| **PAST BANK BORROWERS** | | -175 | -142 | -36 | 952 | 1139 | 1260 | 777 | 997 | 1224 | -233 | -168 | -47 | 879 | 1048 | 1138 | 646 | 880 | 1091 |
| **BANKWIDE TOTAL** | | 5007 | 5295 | 4975 | 3063 | 3161 | 3176 | 8070 | 8456 | 8151 | -980 | -1896 | -3200 | 2810 | 2850 | 2789 | 1830 | 954 | -411 |

Source: Projections of net disbursements and net transfers are based on the Country lending programs as of November 30,1986.

02-Mar-87

**Table 9**: PORTFOLIO DISTRIBUTION BY REGION, FY86-98
(in percent of total IBRD loans outstanding)

| Region | Actual FY86 | Base Case FY88 | Base Case FY93 | Base Case FY98 |
|---|---|---|---|---|
| Eastern Africa | 3.8 | 3.4 | 2.2 | 1.7 |
| Western Africa | 6.2 | 6.8 | 8.4 | 9.3 |
| EMENA | 24.7 | 23.7 | 20.6 | 18.6 |
| Eastern Europe | 8.0 | 6.6 | 3.9 | 2.9 |
| Middle East | 1.2 | 1.1 | 1.1 | 1.0 |
| North Africa | 6.6 | 7.7 | 8.2 | 7.8 |
| Other Europe | 6.6 | 8.3 | 7.4 | 6.9 |
| LAC | 33.2 | 33.5 | 30.5 | 28.5 |
| Caribbean | 1.5 | 1.2 | 0.8 | 0.5 |
| Central Amercia | 2.9 | 2.4 | 1.8 | 1.5 |
| Mexico | 7.8 | 8.2 | 8.2 | 8.1 |
| Brazil | 10.3 | 10.2 | 9.1 | 8.8 |
| Other S. America | 10.7 | 11.5 | 10.6 | 9.5 |
| East Asia & Pacific | 26.7 | 25.3 | 25.6 | 28.0 |
| South Asia | 5.4 | 7.4 | 12.7 | 13.9 |
| TOTAL | 100.0 | 100.0 | 100.0 | 100.0 |
| Portfolio ($ billion) | 60.0 | 75.0 | 101.1 | 133.4 |

Note: Individual items may not add due to rounding.

Record: April 3, 1987

# FINANCIAL POLICY COMMITTEE

## MINUTES OF MEETING OF THURSDAY, MARCH 19, 1987

Members Present: Messrs. Qureshi (Chairman), Asser, Gue, Hasan, Inakage, Paijmans, Rotberg and Wood.

Also Present: Ms. Hadler and Messrs. Asanuma, Baneth, Baudon, Jansen, Lysy, McPheeters, Mistry and Talvadkar.

### I. 1987 Review of Country Creditworthiness and Bank Loan Portfolio Issues, FPC/87-4.

1. The Chairman opened the meeting by asking for a summary of the OVP discussions on the same subject held on March 18, so as to brief the FPC members on the essential reactions of the Operations Complex to the report. A member then reported that the key views expressed during the OVP meeting in reaction to the deteriorating trends pointed out in the report, were:

(a) That the Bank should not consider retrenchment as a viable option;

(b) That the trade-off between the financial strengthening of the institution and the "optimal" use of Bank funds would be difficult;

(c) That the increase in Bank exposure in selected countries should not be viewed in a static sense; a number of countries especially in Latin America were making good adjustment efforts and that the high exposure had been accompanied by increased Bank involvement in policy dialogue on macro and sector management issues. In specific cases, there had been deliberate decisions to increase Bank exposure beyond "norms";

(d) That while increased burden-sharing could be explored, there were real constraints imposed by our limited leverage with commercial banks and inability to use guarantees; and

(e) The option of using quick disbursing assistance to manage debt service profile is already being used to limit in many cases; further increases will lead to severe volatility in future disbursements.

The same member noted that the OVP meeting had concluded that the country ratings in the report were generally appropriate, and that the overwhelming concerns expressed by the OPC members were for the fast deteriorating global environment and the increasing risk which the institution confronted.

2. At the Chairman's request, another member summarized the purpose and broad conclusions of the paper. He first stated that the report had a "stock-taking" objective for the institution as a whole. From that point of view, the central message is very sobering: the Bank has now a very high risk portfolio and is becoming increasingly vulnerable to protracted arrears in the servicing of its loans. He illustrated this by mentioning that the ratio of Bank debt service to exports has increased three or fourfold in many countries over the recent past. He then said that the second objective of the report was to point out that the Bank does have some capacity to manage its rising exposure. This could in particular be achieved through: (a) increases in the share of fast-disbursing operations in the lending program, whenever possible and desirable; (b) a liberalization of repayment terms; and (c) changes in the loan charge structure to better withstand increased risk of non-accruals from small borrowers. However, the same member noted that the first action can reduce our exposure risk in the short-run only (by temporarily raising the level of net transfers), but would then lead to higher exposure levels in the future. In that sense, restored growth and improved fiscal/current account balances in borrowing countries will be crucial to avoid unmanageable Bank risk in the medium-term. He then concluded by saying that despite the "exposure management" tools it can develop, the Bank is in an increasingly difficult situation. The need for a General Capital Increase thus becomes paramount to avoid severe impairment of the Bank's capacity to absorb potential shocks in the future.

3. Before opening the discussions, the Chairman stated that in his opinion, the paper served several essential purposes in the present difficult environment: first, it triggered a Bank-wide debate and highlighted the riskiness of the situation; second, it put things in perspective by demonstrating that, contrary to what a purely static analysis would indicate, an increase in Bank's exposure in the short-run could ultimately reduce the overall risk to the institution if adjustment programs in borrowing countries are carefully designed and implemented; third, it showed that the problem of burden-sharing was real and; fourth, it provided additional evidence that a GCI will be a necessary part of the answer, even though it would not reduce the risk factor itself, but rather allow the Bank to withstand it better.

4. The Committee then focused its discussion on the following points:

(a) The lack of a fully satisfactory solution in the present world economic environment to deal with the deteriorating situation of the portfolio and the extent to which a GCI would be instrumental in giving the Bank additional strength and leverage to adjust to the increased risk factor; and

(b) The specific proposals made in the report with respect to the management of Bank exposure (country-specific limitations in lending and total exposure; the use of policy-based, fast-disbursing operations to manage the debt service profile; optional new Bank lending terms; and improved burden-sharing with other creditors).

5. *The need for a broader response to an increasing risk and the potential contribution of a GCI.* One member stressed that the main conclusion he drew from the report was the absence of a satisfactory solution at hand to deal with the increasingly difficult situation faced by the Bank. He felt that a GCI, though desirable, would not by itself be an adequate answer, and that a conflict situation is gradually arising between the Bank's need to protect its financial situation and the need to meet its basic mandate by assisting its member countries. Another member supported this by adding that the world economic environment was difficult and could deteriorate further, and that retrenchment by the Bank at this point could increase the likelihood of defaults rather than reduce it; he agreed that a GCI would not be sufficient, although it would definitely have the two major advantages of increasing financial flows to developing countries and allowing the adjustment process to continue. The same member pointed out that in his view the real issue was the debt problem, and how we could tackle it. He felt that the Bank should fully acknowledge the variability of situations among debtor countries and not put excessive hope in a quick resumption of voluntary lending by the commercial banks. The Chairman then stated that a GCI was absolutely essential and would greatly contribute to restoring the Bank's ability to cope with the deteriorating situation. It would bring back the Bank's financial ratios to more satisfactory levels and allow the institution to continue to meet its normal obligations by offsetting the constraints that sharp exchange rate movements will soon impose on our aggregate borrowing and lending capacity.

6. A member then said the situation had become so serious that the Bank should refuse to participate in any new concerted lending package unless it receives assurances by the major shareholders that a GCI will be implemented soon. In his opinion, the combination of slow growth prospects of the world economy with deteriorating Bank financial ratios and "headroom" was unprecedented and justified such a strong stance regarding a GCI. The Chairman replied that these were certainly valid causes for concern but that he did not see a drastic deterioration in either the situation of borrowing countries or the Bank portfolio itself over the last year. He noted that none of the underlying trends were new, but rather that we were one year farther along the path that we have been on for some time. He reiterated that the recent deterioration in financial ratios stemmed almost exclusively from exchange rate movements, i.e., the decline of the US dollar vis-a-vis other major currencies. A member emphasized, however, that what was new was the convergence at one time of several key adverse trends.

7. Several members expressed the view that the past year had been the fifth consecutive one of declining creditworthiness for our borrowers, despite the adjustment measures undertaken by a number of them. The cumulative effect of this steady degradation, which is likely to continue given the expected evolution of the terms of trade during the coming year, will ultimately take its toll if nothing is done to alleviate the excessive burden that debt service puts on several countries. They thought that the Bank should: (a) increase its reserves as quickly as possible; and (b) seriously consider a broad new approach to the global

problem of LDC debt and debt service. The Chairman also noted that the issue of net transfers is indeed a real one, and that the Bank should be very concerned about it.

8. Specific proposals with respect to management of Bank exposure. The discussion then turned to the specific recommendations made in the report to improve the management of Bank exposure. A broad consensus emerged in the Committee on the following points:

(a) The Bank should maintain a degree of flexibility in managing exposure limits and not be excessively bound by formal ratios; this would be justified in particular if a country is pursuing a high quality adjustment program. Retrenchment in lending, especially to the highly indebted countries, could prove to be a more risky proposition than continued support through increased capital flows, provided sound economic policies are being implemented; the risks associated with this proposition were fully acknowledged by Committee members, who agreed, nevertheless, that the Bank should preserve the option to pull out or retrench in certain specific cases;

(b) The liberalization of lending terms is a sound proposition which could benefit both the borrowers and the Bank, but further detailed work needs to be done before a fully operational proposal can be presented. In addition, the Bank should be sensitive to the timing of this proposal in relation to the discussions on the GCI; premature adoption of a liberalization policy could undermine the GCI process itself. A member pointed out that this liberalization would not have much effect in the short run; it was noted, however, that even modest positive effects are worth considering, particularly during the interim period preceding the implementation of the GCI; and

(c) Portfolio concentration in high risk countries could be alleviated in part, should the Bank decide to offer more attractive terms or better tailored products to its most creditworthy borrowers. This would increase their interest in borrowing from the Bank.

9. With respect to the Bank's vulnerability to arrears and the possible measures the Bank could take to avoid a significant deterioration in net income, the Chairman asked that reference to a contingent charge be dropped for the time being, pending conclusion of the on-going discussions on the structure of loan charges.

10. In conclusion, the Chairman stated that the discussion had highlighted the urgency of a GCI and increased the Bank-wide awareness of the high risk profile the Bank is increasingly taking. He hoped that this awareness would be reflected in our policies and approaches: (a) on the operational side, our criteria for lending should remain as strict as possible since the quality of the programs we support is the key to restoring a viable situation; and (b) on the financial side, the Bank should be more sensitive than ever to the evolution of the financial ratios, and be adequately prepared to deal with crisis situations should they arise.

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# 1987 REVIEW OF COUNTRY CREDITWORTHINESS AND BANK LOAN PORTFOLIO ISSUES

VOLUME I

March 9, 1987

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Country Program Review Division
Planning and Budgeting Department

## 1987 REVIEW OF COUNTRY CREDITWORTHINESS AND BANK LOAN PORTFOLIO ISSUES

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## I. INTRODUCTION

1.1 This is the fifth annual review of country creditworthiness and IBRD loan portfolio issues in the current series which began in 1982.[1/] This report reviews the creditworthiness prospects of current and prospective borrowers, and assesses the consequences of these changes for the Bank's loan portfolio. It also identifies aspects of country and portfolio risk which need to be considered in the formulation of country assistance plans and financial policies.

1.2 The previous review, considered by Senior Management in June 1986, concluded that the continued, albeit slow, turnaround in the global economy in 1985 and the efforts of many developing countries to stabilize and restructure their economy had resulted in some improvement in creditworthiness and in marginal strengthening of the portfolio. Particular factors influencing this assessment included a continued decline in interest rates and the resumption of an orderly realignment of exchange rates following the Plaza Hotel agreement. Moreover, the decline in oil prices which began late in 1985 was expected to improve the outlook for the oil importing countries, which account for more than 70% of the Bank's portfolio. As a result of these and related developments, the risk ratings of several major borrowers, including China, India, Korea, and Turkey, were upgraded and there was some overall strengthening of the portfolio. In particular, for the first time since 1982, there was a measurable decline in the aggregate portfolio share of high-risk Category III borrowers. The 1986 review also noted, however, that within Category III there was further deterioration, continuing a trend which had already been identified in earlier reviews as a source of concern. Specifically, declining oil prices contributed to the downgrading of ratings for three major oil exporters (Egypt, Mexico and Nigeria), as a result of which the portfolio share of Category IIIb countries again increased sharply. Finally, the review concluded that given the global outlook there appeared to be only limited prospects for early improvement in the classification of most countries in the highest risk categories (IIIb and IIIc), and that the partial debt service moratoria imposed by Nigeria and Peru had raised new concerns over the possibility of preferred creditors being drawn into debt restructuring.

1.3 The conclusions of the current report appear to bear out some of the concerns raised in the 1986 review and to point toward new warning signals for the future. The slowdown in industrial country growth and world trade noted last year has continued, amid increasing uncertainty about LDC terms of trade, capital flows and interest rates. In spite of strong efforts and continued austerity in many countries, the adjustment process is taking longer than had been hoped. Although the risk ratings of a few relatively minor borrowers have been upgraded, the downgrading of

1/ Comprehensive earlier reviews were conducted in 1975 and 1978.

Turkey in particular has once again pushed the share of Category III countries above 60% of the portfolio. Further, if, as seems likely, there is some expansion of lending beyond current plans to borrowers in Category III -- and particularly if lending to Venezuela, graded IIIa, is resumed without too much delay, then the share of Category III could continue to grow. In addition, even on current lending plans the share of IIIb countries in the portfolio is likely to continue to expand steadily for the foreseeable future. Finally, it should also be noted that the unilateral debt service moratoria first mentioned in the 1986 review as a source of potential concern appear to be spreading, particularly as a result of recent developments in Brazil.

1.4 This report is based on the risk classification system which has been used in previous reviews. At the conclusion of the 1986 creditworthiness review, it was suggested that a summary of the risk rating system and Bank policies related to risk assessment be prepared and circulated for information and guidance on this aspect of country economic analysis and programming. The summary was circulated in January 1987, and a copy is reproduced as Annex III to this report. A more detailed description of the risk rating system is attached as Annex I, while Annex II contains a description of the portfolio projection methodology and a sensitivity analysis of the impact of alternative portfolio assumptions.

1.5 Supporting the individual ratings assigned in this report, detailed country notes have been prepared for 33 higher-risk borrowers, with special emphasis on major borrowers in Category IIIb. These notes are presented separately in Volume II of this report. While these notes have been cleared in substance with Regional Office Programs Division Chiefs, the assessments and specific risk ratings are those of PBD alone.

1.6 Chapter II of this report provides a brief overview of recent developments in and prospects for the global environment, and their effect on the outlook for the developing countries. Emphasis is placed, in particular, on the downside risks associated with longer-term trends emerging in the global economy. Chapter III reviews the risk ratings derived from the current assessment of country creditworthiness, reviews recent and projected changes in the risk structure of the portfolio, and summarizes recent developments and the outlook for stabilization and adjustment in the highly indebted countries. Risks to the Bank's balance sheet are discussed in Chapter IV, which reviews trends in exposure, net transfers, portfolio concentration and the risk of arrears, and discusses the implications of these trends for operational and financial management.

## II. THE GLOBAL ENVIRONMENT

2.1 The outlook for the creditworthiness of the Bank's borrowers is heavily dependent on global developments and prospects. Developments over the past year have not been promising. While the likelihood of a "hard landing" or a similar precipitous plunge into global recession still seems rather remote, there has been further deterioration in current conditions and longer-term trends. In particular, it has become increasingly clear that cooperation among the industrial countries to correct the major imbalances in their relations is likely to take place under conditions permitting only limited growth. This is crucial for the developing countries, and reduces the hope for a speedy resolution of the debt crisis.

2.2 The evolution of the global economy since 1982 is illustrated by the data shown in Table 2.1, below. Among the principal elements in this picture the following are particularly noteworthy:

- Industrial country growth. OECD growth rates have continued to drift downward since the short-lived boomlet in 1983-84. Further, near-term growth projections, especially for Japan and the U.S., have been progressively reduced over the past few months, so that the current outlook is substantially below recent WDR central case assumptions. Barring major changes, these trends will eventually translate into reduced export demand and growth prospects for the LDCs.

- Commodity prices and LDC terms of trade. The Bank's overall index of non-oil commodity prices was stagnant in 1986, and with a few exceptions current projections point toward little improvement over the depressed levels of 1984-85. In constant dollar terms, all of the major commodity group averages are either flat or declining over the medium term, with the non-oil aggregate index projected to remain 25% below the level of 1980 into the early 1990s. The decline in the non-oil developing countries' terms of trade is therefore likely to continue. A major question mark in this scenario is, of course, the price of oil. If the current OPEC target of $18 per barrel is unsustainable, then the problems facing a number of highly indebted oil exporters could mount rapidly.

- Capital flows and debt. The explosive growth of debt and debt service of the late 1970s and early 1980s has virtually come to halt. However, this aggregate evolution masks disturbing trends at the component level of the debt accounting system. The stabilization of total debt service is a function not only of a slowdown in the growth of debt outstanding, but also of two specific factors. First, the massive wave of rescheduling and refinancing triggered by the debt crisis in 1982 has had the effect of holding amortization on

Table 2.1: THE GLOBAL ENVIRONMENT—SELECTED INDICATORS, 1982-87
(Units as indicated)

| | 1982 | 1983 | 1984 | 1985 | Estimated 1986 | Projected 1987 |
|---|---|---|---|---|---|---|
| Real Growth of GDP (%/yr) | | | | | | |
| Developing Countries, of which: | 2.1 | 2.0 | 5.2 | 4.1 | 3.4 | 3.9 |
| Oil importers | 2.7 | 3.4 | 6.1 | 5.4 | 5.5 | 4.9 |
| Oil exporters | 0.4 | -2.3 | 2.3 | 2.1 | -1.6 | 2.2 |
| Exporters of manufactures | 4.2 | 4.8 | 7.8 | 7.6 | 6.4 | 5.5 |
| Highly indebted countries | -0.5 | -3.3 | 1.9 | 3.2 | 2.5 | 3.8 |
| Sub-Saharan Africa /a | -0.2 | -2.5 | -1.8 | 2.3 | 0.9 | 2.9 |
| Industrial countries | -0.6 | 2.6 | 4.7 | 2.3 | 2.4 | 2.3 |
| United States | -2.5 | 3.4 | 6.6 | 2.9 | 2.6 | 2.0 |
| Japan | 2.8 | 3.2 | 5.0 | 4.5 | 2.2 | 2.7 |
| OECD Europe | 0.6 | 1.6 | 2.4 | 2.5 | 2.3 | 2.5 |
| Developing Country Trade (%/yr) | | | | | | |
| Real Growth of Exports | -0.5 | 4.1 | 12.5 | 1.3 | 4.3 | 4.1 |
| Oil importers | 0.7 | 4.7 | 13.4 | 2.4 | 4.1 | 4.8 |
| Oil exporters | -3.7 | 2.4 | 9.9 | -1.9 | 4.9 | 1.8 |
| Real Growth of Imports | -4.9 | -5.0 | 5.0 | 2.8 | 2.4 | 3.3 |
| Oil importers | -3.8 | -1.2 | 6.1 | 3.0 | 7.8 | 2.7 |
| Oil exporters | -8.6 | -18.0 | 0.3 | 1.7 | -21.8 | 6.8 |
| Terms of Trade (1980=100) | 97 | 97 | 98 | 97 | 92 | 93 |
| Oil importers | 95 | 97 | 98 | 97 | 104 | 103 |
| Oil exporters | 103 | 98 | 98 | 96 | 55 | 61 |
| LDC External Debt (DOD, US$b) /b | | | | | | |
| Official MLT | 217 | 238 | 256 | 291 | 314 | 340 |
| Private MLT | 394 | 459 | 486 | 514 | 538 | 560 |
| Short-Term Debt | 193 | 162 | 153 | 149 | 143 | 145 |
| Use of IMF Credit | 21 | 31 | 34 | 38 | 40 | 40 |
| Total Outstanding | 824 | 890 | 929 | 992 | 1035 | 1085 |
| Capital Flows to LDCs (US$b) /c | | | | | | |
| Gross Disbursements | 137 | 119 | 94 | 94 | 80 | 80 |
| Total Debt Service | 132 | 124 | 127 | 138 | 132 | 137 |
| Amortization | 51 | 49 | 49 | 60 | 61 | 63 |
| Interest | 81 | 75 | 78 | 78 | 71 | 74 |
| Net Disbursements | 86 | 70 | 45 | 34 | 19 | 17 |
| Net Transfer | 5 | -5 | -33 | -44 | -52 | -57 |
| Multilateral Debt Relief (US$b) /d | | | | | | |
| Commercial Banks | 8.2 | 54.3 | 27.2 | 85.7 | 92.8 | n.a. |
| Official Creditors | 0.6 | 9.6 | 3.9 | 16.4 | 8.5 | n.a. |
| New Money Disbursed | 0.0 | 13.0 | 10.4 | 5.3 | 2.6 | n.a. |
| Int'l Capital Markets (US$b) | | | | | | |
| Total Funds Raised | 179.1 | 153.8 | 195.6 | 265.5 | 298.3 | n.a. |
| Of which, Non-OPEC LDCs: | | | | | | |
| Total borrowing | 37.4 | 27.5 | 28.6 | 23.6 | 14.6 | n.a. |
| MLT bank loans | 32.3 | 24.9 | 19.8 | 13.1 | 5.6 | n.a. |
| International Prices (1979/81=100) /e | | | | | | |
| Petroleum | 112 | 101 | 99 | 96 | 49 | 58 |
| Food and Agriculture | 83 | 89 | 92 | 80 | 83 | 76 |
| Metals and Minerals | 85 | 88 | 83 | 78 | 72 | 72 |
| Manufactures (MUV index) | 99 | 97 | 95 | 96 | 114 | 115 |
| International Interest Rates (%) | | | | | | |
| Six-month U.S.$ LIBOR | 13.60 | 9.93 | 11.29 | 8.64 | 6.88 | 7.00 |
| Average Spread (non-OPEC LDCs) | 1.14 | 1.70 | 1.44 | 0.99 | 0.71 /f | 0.70 |
| Total Nominal Rate | 14.74 | 11.63 | 12.73 | 9.63 | 7.59 | 7.70 |
| Real Rate, Including Spread | 7.74 | 7.54 | 8.50 | 6.13 | 4.86 | 3.56 |
| Value of the U.S. Dollar (1980=100) /g | | | | | | |
| Against the SDR | 118 | 122 | 127 | 128 | 107 | 100 |
| Against Other SDR Currencies | 132 | 142 | 157 | 161 | 125 | 111 |
| Effective Rate (IMF-MERM) | 126 | 133 | 144 | 150 | 122 | 109 |

Note: Value data expressed in current prices and exchange rates. Data for 1986 are preliminary estimates; 1987 projections from sources indicated below. LDC data exclude high-income oil exporters; totals may not add due to rounding.

/a Excluding South Africa.

/b Debt disbursed and outstanding. Composition reflects roll-over of about $45 billion short-term debt into long-term debt in 1983-86.

/c Including net year-to-year changes in and interest on short-term debt, and FBD estimates for non-DRS reporting countries and the use of IMF credit.

/d Total restructuring recorded in the year of agreement in principle (commercial banks), or year in which agreed minute is signed (Paris Club). Due to revisions in recording practices, data are not comparable to previous estimates.

/e In current U.S.$ terms; MUV index based on 1980=100.

/f Annual rate based on data for January-October 1986.

/g Period average rates; index against other SDR currencies uses 1985 SDR weights.

Sources: LDC growth and trade from 1987 IBRD WDR data base; 1987 data central case projections; trade data on balance of payments basis. Industrial country growth from OECD Economic Outlook, December 1986, with revisions for 1986 and 1987 by IBRD (ERS) staff.
Debt, capital flows and debt relief from of IBRD 1987 World Debt Tables.
Capital market data and spreads from OECD Financial Market Trends, November 1986. Commodity prices from IBRD, "Half-Yearly Revisions of Commodity Price Forecasts" (SecM87-135), February 1987. Historical data on interest and exchange rates from IMF/IFS; projections from IBRD Planning Assumptions Committee.

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MLT debt far below originally scheduled levels. Second, the current dollar value of total LDC interest payments has been virtually unchanged at the 1982-83 level for several years because nominal interest rates have been declining generally since 1981, more than offsetting the effect of the increase in DOD over the same period. However, unlike the rolling rescheduling of amortization, the decline in interest rates is not likely to continue indefinitely, and may in fact already be over. It should, of course, also be noted that real interest rates have remained at historically high levels--a major factor in the heavy weight of the debt burden.

2.3 In sum then, the global outlook is not encouraging. Against this background it is important to remember that average per capita income has been declining steadily in many of the developing countries for much of the past decade, particularly in Africa and Latin America but also in oil-exporting countries in other parts of the world. It seems highly unlikely that all of them will be willing, or even politically able, to proceed indefinitely under a regime of strenuous austerity. The current outbreak of unilateral interest moratoria may amount to little more than isolated attempts to bargain for better terms. It could also, however, have more serious long-term implications; clearly it adds to uncertainty in the global outlook and increases the risk of failure in the search for a solution to the debt crisis and a generalized resumption of LDC growth.

## III. COUNTRY RISK RATINGS, PORTFOLIO TRENDS AND ADJUSTMENT IN THE HIGHLY INDEBTED COUNTRIES

### Country Risk Ratings

3.1 Changes in country risk ratings in the present report concern mostly smaller borrowers.[1/] The four countries which have been upgraded account for only 0.8% of the FY86 portfolio. The share of the five countries which have been downgraded is much larger, 7.8% of the portfolio. This is largely due to the downgrading of Turkey which has a 6.6% portfolio share. In the 1986 report most of the changes took place among the major borrowers; in that report the risk ratings of six countries accounting for 19% of the FY85 portfolio were upgraded and the ratings of ten countries accounting for 21% of the portfolio downgraded. The country risk ratings are based on the methodology outlined in Annex I; the resulting country classification is shown in Table 3.1 below.

3.2 The recent developments which underlie the changes in creditworthiness ratings are discussed in the country notes in Volume II. This volume also contains notes on developments in a number of other countries with significant debt problems.

### Portfolio Trends

3.3 For the purpose of analyzing trends in the risk composition of the Bank's loan portfolio, we have linked historical data for the recent past with projections out to the late 1990s.[2/]

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1/ The analysis has been undertaken for all countries for which lending was proposed in the FY87-91 Regional lending programs submitted in November 1986, including those countries which remain in the graduation phase, namely the Bahamas, Barbados, Cyprus and Oman. In total, this includes 58 borrowers (including the Caribbean Development Bank), which accounted for 94.2% of the Bank's loan portfolio at the end of FY86 and, on the basis of current lending plans would account for over 94.5% by FY91. The balance of the portfolio is held by past Bank borrowers and former blend countries. The only borrower not covered is the International Finance Corporation, which is excluded from all portfolio estimates in this report. For further detail, see Annex I, para. 2. Although not included in the November 1986 lending programs, Venezuela and Paraguay have been reviewed in the expectation that lending will occur in these countries in the near future.

2/ The lending and technical assumptions for the base case portfolio projection are shown in Annex II, together with a brief assessment of two alternate scenarios. The projected Regional distribution of the portfolio is presented in Table 9 of the Statistical Appendix.

Table 3.1: RISK CLASSIFICATION OF CURRENT BORROWERS

| Risk Category | East Africa | West Africa | East Asia | South Asia | EMENA | LAC |
|---|---|---|---|---|---|---|
| I. Minimal Risk of Debt Servicing Difficulties | | | Korea | | | |
| II. Some Risk of Debt Servicing Difficulties | | | | | | |
| (a) | | | China<br>Fiji ↑<br>Thailand | | Cyprus ↑ | Bahamas<br>Barbados ↑ |
| (b) | Botswana<br>Mauritius | | Malaysia | India | Jordan | |
| (c) | Swaziland | Cameroon | Indonesia | | Algeria<br>Hungary<br>Oman ↓<br>Portugal<br>Tunisia | Belize<br>Colombia |
| III. High Risk of Debt Servicing Difficulties | | | | | | |
| (a) | Zimbabwe ↑ | | PN Guinea | Pakistan | Romania<br>Turkey ↓<br>Yemen A.R.<br>Yugoslavia | Argentina<br>Brazil<br>Panama<br>Uruguay<br>Venezuela ↓/c |
| (b) | Kenya | Congo<br>Cote d'Ivoire<br>Nigeria | Philippines | Sri Lanka | Egypt<br>Morocco<br>Poland /a<br>Syria | Chile<br>Costa Rica<br>Dominican Rep.<br>Ecuador ↓<br>El Salvador<br>↑ Guatemala<br>Honduras<br>Jamaica<br>Paraguay ↓ /b<br>↑ Mexico |
| (c) | | | | | Lebanon | Peru |

/a Rated for the first time; rating is based on incomplete data.
/b No operations currently scheduled for the FY87-91 period.
/c Venezuela has been declared eligible again for Bank borrowing (SecM86-1335) and is included here following Government's request for Bank borrowing.

The table excludes the Caribbean Development Bank, and enclave borrowers, namely Lesotho, St. Lucia and St. Vincent. Arrows indicate improvement (↑) or deterioration (↓) in a country risk rating since the 1986 Creditworthiness Review.

3.4 The main development, shown in Table 3.2 below, is the drastic, once-for-all shift at the beginning of the present debt crisis to the high risk category (category III) which from then on has been fairly stable, around 60% of the portfolio. Within category III, however, there has been a marked deterioration as shown by the increased share of category IIIb.

Table 3.2: EVOLUTION OF THE IBRD PORTFOLIO RISK STRUCTURE, FY82-86, FY91, FY96
(Percent of loans outstanding)

| | Actual /a | | | | | Projected /b | |
|---|---|---|---|---|---|---|---|
| | FY82 | FY83 | FY84 | FY85 | FY86 | FY91 | FY96 |
| Category I - Minimal Risk | 2.3 | 1.1 | 0.9 | 8.1 | 7.4 | 3.8 | 1.9 |
| Category II - Some Risk | 58.5 | 36.3 | 38.5 | 35.2 | 29.9 | 35.1 | 39.9 |
| IIa | 15.6 | 13.0 | 12.7 | 5.8 | 6.6 | 7.2 | 10.7 |
| IIb | 9.3 | 10.6 | 5.8 | 7.1 | 6.7 | 10.9 | 13.0 |
| IIc | 33.6 | 12.7 | 20.0 | 22.3 | 16.6 | 17.0 | 16.2 |
| Category III - High Risk | 39.2 | 62.6 | 60.5 | 56.7 | 62.7 | 61.1 | 58.2 |
| IIIa | 29.2 | 48.2 | 36.7 | 22.5 | 28.0 | 26.7 | 25.2 |
| IIIb | 3.2 | 8.1 | 17.7 | 28.2 | 29.4 | 32.0 | 32.1 |
| IIIc | 6.8 | 6.3 | 6.2 | 2.0 | 5.3 | 2.4 | 0.9 |
| Memo: Total Loans Outstanding Excluding IFC (billion US$) | 28.7 | 33.2 | 37.3 | 40.7 | 60.0 | (91.5) | (119.9) |

/a Actual loans outstanding at end of each fiscal year, with risk structure based on country creditworthiness ratings in place at that time or approved during the subsequent fiscal year.
/b Based on FY87 risk ratings and base case portfolio projections.

3.5 In FY85, the share of category III declined moderately (to 56.7%) but since then it has risen once more. The increase is concentrated in category IIIa and reflects primarily the downgrading of Turkey. For the first time since 1982, the portfolio share of category IIIb has remained constant. However, with close to 30% of the portfolio, this category remains one of the most worrisome aspects of the portfolio. This is especially so since most of the countries in this category are primary commodities producers and/or oil exporters. Given the poor market prospects for these commodities, the countries in this category are generally not expected to realize any significant improvement in their credit standing in the near term. There are also concerns that should

financial packages unravel, one or more of the current IIIa countries could be downgraded.

3.6 The future risk composition of the portfolio shows a modest improvement. Based on current country ratings, the portfolio share of category III as a whole is projected to decline (from 62.7% in FY86 to 58.2% in FY96). The share of category IIIa declines slightly, primarily as a result of the declining portfolio share of several higher income borrowers (for instance, Romania and Yugoslavia). The share of category IIIb increases slightly through FY96 reflecting the increased portfolio shares of countries that are assumed to have adopted stabilization and/or adjustment programs (for instance, Chile, Côte d'Ivoire, Egypt, Morocco, Nigeria). The share of category IIIc, however, declines rapidly because of the assumptions made in the projections that (i) lending to former blend countries does not resume; (ii) lending to countries with uncertain political prospects (for instance, Lebanon and Nicaragua) remains virtually nil; and (iii) there will be no lending to IIIc countries after FY91.

3.7 Portfolio Vulnerability to Global Trends and Developments. Another way to look at the portfolio is to categorize borrowers into groups that facilitate analysis of certain risks arising from changes in the global environment. A view of the portfolio from this angle is shown in Table 3.3, below. In this table, two specific characteristics are used to aggregate the portfolio shares of the Bank's borrowers into more or less homogeneous subgroups, namely (a) the commodity orientation of the country's exports, and (b) the country's status as a debtor. The table

Table 3.3: LENDING AND PORTFOLIO COMPOSITION BY SELECTED MACROECONOMIC CHARACTERISTICS, FY82-98
(Percent of lending or portfolio)

| | Lending Program | | Loan Portfolio | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Actual | Projected/a | Actual | | | Projected/a | | |
| | FY82-86 | FY87-91 | FY82 | FY83 | FY86 | FY88 | FY93 | FY98 |
| I. Active Borrowers, Total /b | 99.6 | 99.9 | 93.5 | 95.1 | 97.8 | 98.8 | 99.8 | 100.0 |
| A. Oil Exporters /c | 24.5 | 30.0 | 22.0 | 21.6 | 24.1 | 26.1 | 28.8 | 29.9 |
| B. Oil Importers, of which: | 75.1 | 69.8 | 71.5 | 73.5 | 73.7 | 72.7 | 71.0 | 70.1 |
| Major exporters of manufactures | 39.9 | 37.6 | 25.4 | 26.0 | 28.5 | 28.7 | 33.0 | 36.0 |
| Largely primary producers | 35.2 | 32.2 | 46.0 | 47.5 | 45.3 | 44.0 | 38.0 | 34.0 |
| II. High Debt/High Risk Borrowers | 52.3 | 56.2 | 55.0 | 55.1 | 58.2 | 59.4 | 56.8 | 54.9 |
| A. "Highly Indebted" Countries/d | 41.2 | 45.8 | 43.7 | 43.4 | 45.9 | 46.9 | 44.3 | 43.2 |
| B. Other High Debt/ Risk Borrowers/e | 11.1 | 10.4 | 11.3 | 11.7 | 12.3 | 12.5 | 12.5 | 11.7 |

/a Based on 1987 central case assumptions.
/b I.e., excluding graduated Part I borrowers and other countries in graduation status.
/c Export classification based on current WDR structure.
/d The 15 "Baker" countries plus Costa Rica and Jamaica.
/e Defined as other Category III countries which have (a) debt to exports ratio of around 200% or more and (b) current or projected share of the IBRD portfolio of 0.5% or more.

also summarizes actual lending to the same groups of countries during FY82-86 and projected lending for FY87-91. Table 3.3 reveals certain trends which merit attention:

- Portfolio shares of oil exporting countries and major exporters of manufactured goods increased steadily since 1982 and are projected to increase further over the next decade. As a result, the portfolio is becoming more vulnerable to the world economic outlook, particularly the outlook for oil prices and protectionism. The marked increase in the aggregate portfolio share of the oil exporters (from 24.1% in FY86 to 28.8% in FY93) is linked to the sharp increase in lending, particularly of policy-based lending, to several countries in this group. This is particularly true for Mexico and Nigeria, which together account for more than half of projected lending to this group over the next five years. The converse, of course, is the case for the manufactured goods exporters. In this group, portfolio evolution is heavily weighted by the projected expansion of project lending and sector investment in China and India, in neither of which is policy-based lending a factor in current lending plans.

- Policy-based lending is also a dominant consideration in the near-term expansion of lending to and portfolio shares of the countries designated in Table 3.3 as high debt/high risk borrowers. On the pattern of lending currently foreseen, however, there will be little increase, if any, in the riskiness of the portfolio arising from this group of countries. Over the next few years, expansion of lending and rapid disbursements to these countries will hold the portfolio share of this group at close to 60% of the total. For the 1990s, however, a gradual reversal of this trend is indicated. This, in turn, is a function of current assumptions for an eventual tapering off of the share of fast-disbursing loans from the relatively high levels reached in programs for these countries in the mid-1980s.

3.8 Using the same way to categorize the portfolio, Table 3.4 illustrates recent and projected changes in portfolio quality. In this table, the weighted average risk rating of the portfolio as a whole in FY82 is used as a benchmark against which to measure both the average ratings of major groups of borrowers at that time as well as actual and projected changes since then. Among other things, these data reveal:

- The impact of the initial downgrading of risk ratings of many borrowers following the eruption of the debt crisis in 1982.

- The steady deterioration (which is projected to continue) of average ratings of the oil exporters and at the same time, the improvement in the ratings of the oil importers as a whole and the manufactured goods exporters in particular.

Table 3.4: PORTFOLIO RISK STRUCTURE BY SELECTED MACROECONOMIC CHARACTERICS, FY82-98
(Index, FY82 average risk rating for all active borrowers = 100)

| | Actual /a | | | Projected/b | | |
|---|---|---|---|---|---|---|
| | FY82 | FY83 | FY86 | FY88 | FY93 | FY98 |
| I. Active Borrowers, Total | 100 | 89 | 86 | 82 | 86 | 89 |
| A. Oil Exporters | 96 | 89 | 68 | 64 | 64 | 61 |
| B. Oil Importers, of which: | 103 | 89 | 93 | 89 | 96 | 100 |
| Major exporters of manufactures | 128 | 107 | 125 | 121 | 128 | 128 |
| Largely primary producers | 89 | 79 | 75 | 68 | 68 | 68 |
| II. High Debt/High Risk Borrowers | 96 | 75 | 61 | 54 | 54 | 54 |
| A. "Highly-Indebted" Countries | 100 | 75 | 54 | 54 | 54 | 54 |
| B. Other High Debt/High Risk Borrowers | 71 | 68 | 75 | 54 | 54 | 57 |

/a Actual portfolio shares and risk ratings in place in fiscal year indicated.
/b Based on 1987 risk ratings and central case portfolio projections.

Note: For portfolio coverage and classification, see footnotes to Table 3.3. In this table, country risk ratings are weighted by portfolio share to obtain group averages, with results rescaled from 100 (Category I) to zero (Category IIIc), and then indexed to the FY82 portfolio average = 100.

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- The effect on the creditworthiness of the primary producing countries of the secular decline in their terms of trade and related debt and payments problems. The creditworthiness rating of this group of countries remains far below the average of all countries.

- The deterioration since 1982 of the risk ratings of the "highly indebted" and other high risk borrowers. In FY82, ratings for the countries now classified as "highly indebted" were at approximately the same level as the average rating of all active borrowers. By FY86, the average of "highly indebted" had fallen to only 54% of the FY82 level. On the basis of current ratings and lending plans, the average rating is projected to remain at that level while the average rating for all active borrowers is projected to make a modest recovery to 89% of the FY82 level.

3.9 Taken together, the data in these two tables provide at least a partial measure of the challenge facing the Bank's portfolio management. In spite of the projected increase in portfolio shares of a few major low-risk borrowers such as China and India, for the foreseeable future well over half the portfolio will continue to be concentrated in a large number of relatively higher-risk countries. Much of the portfolio will continue to be highly susceptible to adverse changes in the global environment, and a susbstantial share of the IBRD lending program should continue to be linked to borrower success in developing and sustaining effective programs of adjustment and reform.

Adjustment in the Highly-Indebted Countries

3.10 The riskiness of the Bank's loan portfolio depends to a very large extent on developments in the highly-indebted countries. Almost a year and a half since U.S. Treasury Secretary Baker proposed a concerted effort to resolve the continuing debt servicing problems of these countries, it is of interest to review briefly how the adjustment process has proceeded so far. The main lesson of this brief review seems to be that despite initial progress in adjustment--and strong efforts by governments and international institutions--most primary product and oil exporters will have to face a period of slow growth and that optimistic scenarios for these countries should generally be viewed with scepticism. This is important for the Bank's portfolio management. In determining its lending posture in these high risk countries, the Bank should carefully associate itself only with realistic scenarios for growth and external financing.

3.11 To examine this issue, it is useful first to describe the manner in which a "typical" economy adjusted to the shock of being suddenly cut off from external sources of finance. This description would of course not necessarily provide the outline an optimal process of adjustment. Individual countries, moreover, will have deviated in some respect from the average path, with each economy having its own particular story to tell. However, establishing a typical or average path does provide a framework as well as a basis for comparison, to which the experience of the individual countries can be related.

3.12 The basic story of the reaction of the highly-indebted economies to the debt crisis could be as follows. Up to the crisis point (1982 for most of the countries) GDP growth had been relatively fast and import growth even faster. In a number of cases imports were extremely high in the period around 1979-81 as a consequence of poorly designed "liberalization" attempts (Chile, Argentina, Uruguay). The result was a high trade deficit and, because of interest on the external debt, an even higher current account deficit. This in turn meant that external debt was growing at a high rate. Debt to export ratios rose, as the growth in debt exceeded the growth in exports. This was eventually seen to be unsustainable, with perceptions changed particularly in August 1982 when Mexico declared it could no longer service its debt on schedule.

3.13 Although the 1982 Mexico crisis was important, other factors also entered.[3/] The downward shift in the market's perception of the level of the debt to exports ratio that debtor countries would be able to service also followed from the rise in real interest rates of the period, from negative levels in the 1970s to a positive 8-10% in the 1980s (using U.S. inflation to deflate). The major recession in the U.S. and Europe also reduced prospects. Whatever the reason, the downward shift in the

3/ It should also be noted that several of the key countries (Brazil, Argentina, Morocco) had already gone into recession in 1981, and that lending to Eastern Europe had been cut back even earlier.

perceived serviceable debt to exports ratio led to a sharp cut-back in voluntary commercial lending. Borrowing countries reacted by instituting a variety of import controls, as well as contractionary macro policies to reduce import demand, and the economies fell into a recession as a result.

3.14 Exports generally continued to grow, however, and with imports sharply reduced the trade deficit fell. The current account deficit therefore fell and borrowing requirements were less. The initial causative factor, of course, was the reduced willingness of creditors to lend. In any case, the growth in outstanding debt slowed, and with continued export growth the debt to export ratio reached a peak and then fell. Eventually, if sustained, the debt to export ratio would reach a lower, serviceable level, and voluntary lending would resume.

3.15 The basic questions are how well the data fit this pattern, and at what point we are in the cycle. Since voluntary lending has not resumed, we are certainly not at the end, and therefore a more crucial question (but one on which less can be said) is what is the likelihood that the process will be seen through to the end.

3.16 Tables 3.5 and 3.6 show the basic indicators, with coverage of those Baker countries (plus Jamaica and Turkey) included in the set of 30 for which EPD gathers data for the SAVEM set. The cycle followed appears to be broadly similar to the one described above. The discussion here will focus first on the non-oil exporters, with the peculiarities of the oil exporters added later.

3.17 GDP, real imports and real exports all grew relatively fast in the period 1973-80, with export growth (5.2%) even more rapid than import growth (4.6%). However, the trade deficit was high at 3.8% of GDP on average, because the countries started with an initial trade deficit and because of terms of trade changes (especially petroleum prices). The current account deficit averaged an additional percentage point of GDP, reaching almost 5% of GDP, because of interest on the external debt. Starting from a relatively low base, external debt grew at an annual rate of 29% in nominal terms, and the debt to export ratio rose from 160% in 1975 to 229% in 1980. This growth continued into 1981-82.

3.18 . It had become clear by this time that the process was unsustainable. Imports were sharply curtailed and GDP growth fell to only 1.2% in 1981 and was negative in 1982. Export growth continued, and in 1983-85 the trade deficit fell steadily and then turned into a surplus. One should note, however, that in terms of the aggregate savings/investment balance, the reduction in the trade deficit came not from an increase in savings (which were steady, at 18-19% of GDP throughout 1981-85) but from a reduction in investment (which fell from 24% of GDP in 1981 and in the 1970s, to only 18% of GDP in 1985). This does not bode well for the future. GDP growth was slow throughout 1983-85, falling in per capita terms, and import growth was negative on average.

3.19 With the trade deficit reduced, the current account deficit fell as well, from 8.4% of GDP in 1981 to 2.0% in 1985. This 6.4% point reduction

Table 3.5: ADJUSTMENT IN THE HIGHLY-INDEBTED COUNTRIES: GROWTH RATES AND GDP SHARES

| | 1973-80 | 1981 | 1982 | 1983 | 1984 | 1985 | 1986 | 1987 |
|---|---|---|---|---|---|---|---|---|
| GDP Growth (%) | | | | | | | | |
| Non-Oil Exporters | 4.5 | 1.2 | -0.4 | 0.4 | 1.6 | 1.8 | 4.3 | 3.7 |
| Oil Exporters | 4.3 | 2.3 | -0.8 | -8.0 | 0.5 | 2.1 | 0.2 | 3.6 |
| Import (GNFS) Growth (%) | | | | | | | | |
| Non-Oil Exporters | 4.6 | 0.7 | -7.7 | -5.4 | 3.3 | -4.7 | 7.0 | 6.2 |
| Oil Exporters | 7.8 | 22.9 | -19.3 | -31.3 | -7.5 | -6.6 | -14.7 | 2.4 |
| Export (GNFS) Growth (%) | | | | | | | | |
| Non-Oil Exporters | 5.2 | 10.7 | 3.0 | 2.2 | 9.0 | 4.1 | 4.5 | 5.3 |
| Oil Exporters | 7.1 | -15.1 | -3.6 | -0.1 | 11.4 | 2.8 | -2.1 | 2.7 |
| Investment Share of GDP (%) | | | | | | | | |
| Non-Oil Exporters | 24.2 | 24.4 | 22.2 | 20.8 | 19.1 | 18.0 | | |
| Oil Exporters | 25.8 | 29.7 | 24.9 | 19.7 | 18.5 | 17.0 | | |
| Domestic Savings Share of GDP (%) | | | | | | | | |
| Non-Oil Exporters | 20.4 | 18.7 | 18.1 | 18.3 | 18.9 | 18.4 | | |
| Oil Exporters | 26.7 | 24.9 | 22.6 | 21.4 | 23.0 | 22.9 | | |
| Savings Minus Investment Share of GDP (= Trade Surplus) (%) | | | | | | | | |
| Non-Oil Exporters | -3.8 | -5.7 | -4.1 | -2.5 | -0.2 | 0.4 | | |
| Oil Exporters | 0.9 | -4.8 | -2.3 | 1.7 | 4.5 | 5.0 | | |
| Current Account Balance Share of GDP (%) | | | | | | | | |
| Non-Oil Exporters | -4.9 | -8.4 | -7.7 | -6.3 | -4.7 | -2.0 | -1.7 | -2.4 |
| Oil Exporters | -1.9 | -6.9 | -6.5 | -2.1 | 0.5 | 0.8 | -2.2 | -4.1 |
| Rate of Growth of Total Nominal Debt (%) | | | | | | | | |
| Non-Oil Exporters | 28.6 /a | 17.4 | 12.9 | 3.9 | 4.8 | 6.6 | 3.1 | 3.8 |
| Oil Exporters | 31.7 /a | 25.1 | 10.1 | 17.6 | 3.6 | 1.6 | 8.8 | 5.4 |

/a 1975-80.

Notes: Growth Rates are in real terms.
Shares of GDP are in current prices.
Non-Oil Exporters = Argentina, Brazil, Chile, Colombia, Cote d'Ivoire, Jamaica, Morocco, Philippines, Turkey, Yugoslavia.
Oil Exporters = Mexico, Nigeria, Peru.
Averages are computed with each country given equal weight.

Source: Computed from fourth edition of SAVEM Tables, issued December 22, 1986.

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Table 3.6: ADJUSTMENT IN THE HIGHLY INDEBTED COUNTRIES: RATIOS TO EXPORTS

| | 1975 | 1980 | 1981 | 1982 | 1983 | 1984 | 1985 | 1986 | 1987 |
|---|---|---|---|---|---|---|---|---|---|
| Total Debt to Exports (%) | | | | | | | | | |
| Non-Oil Exporters | 160 | 229 | 247 | 297 | 316 | 293 | 302 | 294 | 280 |
| Oil Exporters | 127 | 133 | 185 | 245 | 280 | 257 | 271 | 428 | 421 |
| Total Interest to Exports (%) | | | | | | | | | |
| Non-Oil Exporters | 11.0 | 21.4 | 26.5 | 31.7 | 30.8 | 26.7 | 26.7 | 23.0 | 23.0 |
| Oil Exporters | 8.1 | 13.8 | 22.3 | 30.4 | 28.2 | 28.0 | 26.2 | 31.0 | 31.3 |

Notes: Total Debt includes short-term and private non-guaranteed MLT, but excludes IMF.
Total Interest is interest on total debt as defined above.
Country coverage and source same as Table 3.5.
Ratios shown are for total debt, interest and exports in each category, not averages across countries.

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is about the same as the reduction over the same period in the trade deficit. With the current account reduced, the growth rate of total nominal debt also fell[4/]. In 1983-85 nominal debt grew at a rate comparable to international inflation, meaning real debt was about constant. With real export growth quite respectable (averaging 5.1%), the debt to export ratio should have fallen at a fairly fast rate. The ratio did in fact fall, but by a disappointing amount, i.e., from 316% in 1983 to 302% in 1985. The cause was disappointing performance of export prices of the non-oil exporters, which fell slightly over the period. If export prices had kept pace with international inflation, the ratio would have dropped to approximately 240%. That would have indicated a very significant improvement in the debt situation.

3.20 In 1986-87, GDP and import growth resumed. However, the GDP growth, at a rate of about 4% per year, mostly reflected a recovery from the previous recession. With investment reduced to 18% of GDP, capacity limits may soon be reached (Brazil). The current account deficit appears to have leveled off at about 2% of GDP and the growth in nominal debt is slow, so the debt to exports ratio has continued its decline, albeit slowly. The slow fall in this ratio is in contrast to its rapid build-up

4/ Although the current account must all be financed, other factors (such as changes in reserves, drawings from or repayment to the IMF, official grants, and capital flight) will mean the relationship between the current account and the change in debt is not always one-to-one.

in 1980-83. The nominal interest to export ratio has fallen by more, reflecting the decline in international interest rates, and has almost reached the level of 1980. However, when adjusted for the inflation component of nominal interest, the 1987 level is still far above the level in 1980. It is in any case clear that with these ratios we are still far from the point at which a resumption of voluntary lending could be expected.

3.21 The adjustment process has therefore been slow. Furthermore, it is not clear whether capacity limits will soon be reached in more countries (as in Brazil) and whether the population of these countries will continue to accept the constraint on consumption which is implied by the modest size of the recovery in output accompanied by strong efforts to maintain a positive trade surplus.

3.22 For the oil exporters, the large swings in oil prices dominated events. In 1979-81 the OPEC average oil price more than doubled in real terms, but in 1986 it fell back to the real levels of 1975-78. The highly indebted oil exporters (Mexico, Nigeria and Peru) maintained a modest trade surplus in the 1970s, as they found it took time to spend their windfall, but by 1981 imports were blossoming (growing by 23% in that one year). A trade deficit was produced, and an even larger current account deficit, and the cutback in imports in 1982-83 was extremely sharp. By 1984-85 a current account surplus was being generated, and the growth in debt had slowed sharply. However, the 1986 oil price decline dealt a severe setback to these countries, and the debt to export ratio jumped from 271% in 1985 to 428% in 1986.

3.23 It appears therefore, that most of the highly-indebted countries are past the initial import contraction phase of the debt adjustment cycle. However, it cannot be said they are yet on a sustainable path which will eventually lead to a resumption of voluntary lending. The debt to export ratio has declined only slowly for the non-oil exporters, and jumped in 1986 for the oil exporters. The macro adjustment, for the period through which we have data, has occurred through a decline in investment rather than through an increase in savings. Capacity limits are therefore likely to be reached soon for countries that try to resume earlier growth rates of GDP. How much longer this slow process will be politically acceptable is not clear.

3.24 Meanwhile, governments, multilateral institutions and commercial banks did take of number of steps in response to the debt crisis. Some of these were well underway before the Baker initiative.

- Most countries have entered into stabilization agreements with the IMF or benefit from frequent discussions (enhanced surveillance) with the IMF on their stabilization efforts.

- Most countries are carrying out adjustment efforts, supported by substantially increased Bank lending. See Table 3.7 below.

- o Commercial banks have entered into or are discussing rescheduling agreements which permit rolling over MLT maturities and, where necessary, consolidation of short-term debt and arrears, and, in some cases, conversion of some debt into equity. The bankers have supplied only relatively small amounts of new funds.

- o The Paris Club has rescheduled bilateral debt for most of these countries.

Table 3.7: BANK COMMITMENTS TO BAKER COUNTRIES
($ millions)

| | 1982 | | | FY85 | | | FY86-88 | | |
|---|---|---|---|---|---|---|---|---|---|
| | Total | Adj. /a Lending | As % of Total | Total | Adj. /a Lending | As % of Total | Total | Adj. /a Lending | As % of Total |
| Argentina | 400.0 | 0.0 | 0.0 | 180.0 | 0.0 | 0.0 | 1629.5 | 850.0 | 52.2 |
| Bolivia /b | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 207.0 | 134.0 | 64.7 |
| Brazil | 722.1 | 0.0 | 0.0 | 1523.0 | 0.0 | 0.0 | 4473.0 | 500.0 | 11.2 |
| Chile | 0.0 | 0.0 | 0.0 | 287.0 | 0.0 | 0.0 | 1089.2 | 750.0 | 68.9 |
| Colombia | 291.3 | 0.0 | 0.0 | 707.5 | 300.0 | 42.0 | 1580.3 | 400.0 | 25.3 |
| Cote d'Ivoire | 374.5 | 150.0 | 40.1 | 141.3 | 0.0 | 0.0 | 1024.0 | 774.5 | 75.6 |
| Ecuador | 228.7 | 0.0 | 0.0 | 6.0 | 0.0 | 0.0 | 537.5 | 150.0 | 27.9 |
| Mexico | 657.3 | 0.0 | 0.0 | 598.0 | 0.0 | 0.0 | 4027.0 | 1000.0 | 24.8 |
| Morocco | 276.0 | 0.0 | 0.0 | 207.6 | 100.0 | 48.2 | 1664.3 | 1050.0 | 63.1 |
| Nigeria | 314.0 | 0.0 | 0.0 | 119.0 | 0.0 | 0.0 | 2316.7 | 952.0 | 41.1 |
| Peru | 286.7 | 0.0 | 0.0 | 31.0 | 0.0 | 0.0 | 13.5 /c | 0.0 | 0.0 |
| Philippines | 452.9 | 0.0 | 0.0 | 254.0 | 150.0 | 59.0 | 1024.5 | 530.0 | 51.7 |
| Uruguay | 40.0 | 0.0 | 0.0 | 64.0 | 60.0 | 93.8 | 269.2 | 80.0 | 29.7 |
| Yugoslavia | 256.6 | 0.0 | 0.0 | 292.5 | 0.0 | 0.0 | 773.0 | 0.0 | 0.0 |
| Total | 4300.1 | 150.0 | 3.5 | 4410.9 | 610.0 | 13.8 | 20628.7 | 7170.5 | 34.8 |

/a Fast and medium-fast disbursing.
/b IDA commitments.
/c FY86 only.

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3.25 In spite of these efforts, the debt problem is proving to have a very stubborn character. In view of the poor price and demand prospects, there can be little optimism about export growth. Interest rates meanwhile appear to have stopped declining, and may start increasing once more. Thus, the interest to export ratio is likely to remain at a level which does not permit rapid further growth of the debt, even if the funds

were readily available. For both social and political reasons, the prospects for further compression of consumption are poor. Consequently, it is not clear that there will be sufficient resources to sustain rapid growth and to work off the debt overhang in the medium term. These considerations should lead the Bank to be generally wary of associating itself with country scenarios permitting high GDP, import, and consumption growth in spite of a heavy debt burden. While a few countries, particularly newly industrialized ones, have indeed been successful in increasing their exports rapidly, most of the primary commodities and oil exporters will find it difficult to do this, unless they are very successful in their diversification efforts. Given the prospects for interest rates, developing country exports, and continued compression of consumption, resources to sustain economic growth will be very scarce. Most of the economic growth therefore will have to be eked out from whatever domestic efficiency measures are feasible, and from the utilization of all possibilities to encourage non-debt creating flows such as direct foreign investment, debt-into-equity conversion and the return of flight capital. More than in the case of other countries, the Bank should for the sake of the quality of its loan portfolio be careful to lend only in support of realistic plans for future growth.

## IV: THE MANAGEMENT OF COUNTRY CREDIT RISK

### Introduction

4.1 The Bank has become increasingly vulnerable to country credit risk. Aside from increased risk of extended arrears due to deterioration in conditions in specific countries, other trends--in Bank exposure, in Bank net transfers, in the basic financial ratios of the Bank, and in the Bank's portfolio concentration--also indicate an increased level of vulnerability. Some of these trends are long-term and to be expected given the maturation of the Bank as a lending institution. Others are an outcome of the Bank's responsibility to lend in what are often high risk country situations, a role the Bank has increasingly been called upon to perform in recent years. This chapter examines one by one these trends in credit risk and discusses in each case the instruments the Bank has or might develop to manage this risk. Obviously, these instruments must be used with maximum efficiency to allow the Bank to operate as safely as possible in the given conditions. Ultimately, however, the Bank cannot get away from having to operate in a high risk environment and, as the chapter shows, this is happening at a time when the Bank's basic financial ratios have deteriorated significantly. Losses arising from arrears on more than a quite small portion of the Bank's loan portfolio would seriously harm the Bank's financial standing. The chapter therefore argues that a General Capital Increase will not merely serve to support an expansion in the volume of Bank operations, but is also needed to increase the Bank's ultimate ability to withstand country credit risk. [Strengthening the Bank] ?

4.2 Several of the adverse trends have also been accelerated by the sharp depreciation of the US dollar since February 1985. Before starting on this chapter's examination of trends in credit risk, we briefly examine the important effect of this depreciation on the Bank's financial condition. Currently, about 90% of the Bank's outstanding loan portfolio is denominated in currencies other than the U.S. dollar, with all but a small fraction of this accounted for by deutsche mark, yen, guilders and Swiss francs. Each of these four currencies has appreciated sharply against the dollar. As a result, obligations of borrowers in dollar terms have gone up. The dollar depreciation in 1986 by itself added more than 20% to the average outstanding loan balances of Bank borrowers. The depreciation has had three effects of interest here. First, net transfers will be reduced, becoming less positive or more negative. The reason is that gross disbursements will be largely unaffected as commitments are fixed in U.S. dollar terms.[1/] However, amortization payments (which are in the

1/ They might increase slightly in the short term, as disbursements under contracts written in deutsche mark or yen, for example, would rise. However, total project disbursements, which must not exceed the commitment level that has been set in dollar terms, cannot rise.

currencies that were originally disbursed) and interest payments (which are a fixed percentage of each of the currencies that were disbursed) will rise in dollar terms as the dollar depreciates. Therefore net transfers, which equal gross disbursements minus amortization and interest, will fall. Second, the dollar depreciation will increase Bank exposure in most of its borrowers. Export values in dollar terms have not risen in proportion to the dollar depreciation; many commodity prices have in fact fallen. Therefore the debt service owed the Bank, which has risen in dollar terms with the dollar depreciation, will rise as a ratio to the exports of the Bank's borrowers. Third, the Bank's reserves to loans and capital to loans ratios will fall with the dollar depreciation as the share of dollars in the Bank's reserves and in the Bank's capital[2/] is greater than the share of dollars in the Bank's outstanding loans.

4.3 The effect of the trends noted above is greater risk to the Bank's balance sheet and projected net income. With increasingly negative net transfers, there is greater risk that borrowers will suspend debt service payments to the Bank in cases of financial crisis. The Bank's exposure in the client countries is also higher, while its financial strength as measured by the reserves to loans and capital to loans ratios has fallen with the dollar depreciation. Although a reversal of the dollar depreciation is always possible, this is not currently expected, and plans should not be made assuming that there will be such a reversal.

Bank Lending Posture and Country Creditworthiness Standing

4.4 The first line of defense in managing country risk is and will remain the Bank's lending posture in high-risk countries. The Bank's policies in this respect have evolved into the formal set of creditworthiness ratings discussed in Annexex I and III. The higher risk ratings are defined operationally, where Management has agreed that there should be no new IBRD commitments to countries in the IIIc category, that further lending to IIIb countries is justified only in those cases where an adequate adjustment program is in place, and that lending to IIIa countries, although unconstrained as to scale on creditworthiness grounds, should nonetheless be oriented to operations designed to improve the state of creditworthiness in those economies.

4.5 The rationale for lending to IIIb countries follows from the Bank's role and importance as a development institution. These countries are in such a weak state of creditworthiness that they would normally not be

2/ Given the way the Bank's share capital is valued by the capped SDR standard of value. Note that the weight of dollars in the SDR, at 42%, is greater than the 10% weight in the Bank's outstanding loans, and that in any case the value of each share is capped at an SDR rate of 1.20635.

considered creditworthy for commercial lending, and such lending therefore has normally arisen only through concerted lending packages. However, the World Bank's role as a development institution, as well as its size and its ability to mobilize resources, justify its lending to these countries provided they are pursuing a program of adjustment which is judged to have a reasonable chance of success. Based on current conditions, we would judge that an adequate adjustment program is not in place in Syria, Sri Lanka, Costa Rica and Honduras. As long as these conditions persist, we recommend that the Bank not make loans to these countries. There are a number of other IIIb countries which also lack an adequate adjustment program, but where the Government is actively exploring an adjustment course, usually in consultation with the Bank and the Fund. In varying degrees, this is happening in Kenya, Egypt, Guatemala, Congo, the Dominican Republic, El Salvador and Paraguay. Resumption of a full scale lending program to these countries would be premature. To maintain and strengthen the dialogue, however, it may be useful to maintain small programs, e.g., through loans for technical assistance in public sector management, which are relatively small in size but which can have a major direct impact on the dialogue.

The Rise in Bank Exposure

4.6 Apart from developments in the creditworthiness of any given country, the risk borne by the Bank is affected by the extent of its exposure in that country's export earnings and debt or debt service. A high degree of Bank exposure in the country's debt or its debt servicing capacity increases the probability that the Bank's preferred creditor status could be at risk should the country encounter difficulties. The Bank has, therefore, developed exposure guidelines. Specifically, Senior Management has agreed that: (a) the debt service due the Bank should not exceed 5% of the country's exports of goods and services, and (b) the debt or debt service due the Bank should not exceed 20% of the country's total public and publicly-guaranteed medium and long-term debt or debt service, or 15% in those cases where the preferred creditors' share[3/] exceeds 33%.

4.7 These guidelines are applied flexibly. It has specifically been recognized that they should be considered only as part of the effort to develop a broad picture of the safety of the exposure position. Other considerations which enter include the Bank's net disbursement and net transfer position vis-a-vis the borrower, the overall creditworthiness level of the borrower, perhaps the state of public sector finances, and perhaps other country-specific factors.[4/]

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3/ Preferred creditors are defined as the IBRD, IDA, the regional multilateral development banks (IDB, ADB, AfDB and EIB), the IMF and the BIS.

4/ The rationale for the guidelines and other considerations were discussed in the 1986 Creditworthiness Review and are summarized in Annex III below.

4.8 Trends in Bank Exposure. Bank exposure has developed into a significant problem in the 1980s. The reasons are several. First, the Bank's lending program has been steadily growing in relative importance. Second, while export growth (in dollar terms) was high in the 1970s, it has been disappointly low in the 1980s. Depressed commodity prices account for much of this.[5/] Third, the Bank has accounted for an increased share of the total lending to developing countries in the 1980s, as other sources (particularly lending from commercial banks) declined with the onset of the debt crisis. This is projected to continue to at least 1995 under current financing scenarios being used by the Regions, although not at the pace recorded between 1980 and 1987. And fourth, a sharp jump between 1985 and currently is due in part to the depreciation of the dollar, which is increasing (in dollar terms) the debt service due the Bank, while exports in dollar terms and the dollar-denominated debt and debt service due others are largely unchanged.

4.9 The countries where Bank exposure is high are shown in Table 4.1, with the list broken into those countries where the exposure should be of immediate concern and a second, more marginal, group where the situation warrants close monitoring. The table also presents data on the trends in exposure in the list of high exposure countries, the Baker-list countries, and all developing countries as a group.[6/] The speed with which exposure has risen deserves particular attention. In the Baker countries, Bank exposure in exports, stable in the 1970s, almost quadrupled in the 1980s. For all developing countries as a group, Bank exposure in exports tripled between 1980 and 1987. In terms of debt service, Bank exposure rose at a slower but still very high pace, by over 100% in all developing countries and by 50% in the Baker countries. Projections indicate that these ratios may now level off and that certain ones may in fact decline, but these projections may well be optimistic.

4.10 The countries identified in the top part of Table 4.1 as those where exposure is of concern are the same as those in the similar list of the 1986 Creditworthiness Review, with the addition of Turkey, Paraguay and Tunisia, but with the deletion of all IIIc countries. The seven IIIb countries on the list are the most worrisome: Kenya, Côte d'Ivoire, Morocco, Honduras, Jamaica, Paraguay and the Philippines. Net transfers are already negative to all of them except Côte d'Ivoire and Morocco (where net transfers are projected to turn negative in FY90). Reform

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5/ Using figures underlying those in Table 3.5 of Chapter III above, the real export growth rate of the non-oil Baker Countries was 5.5% in 1981-87, slightly higher than the 5.2% real rate recorded in 1973-80. However, in 1981-87 their export prices fell by 1.9% per year on average, while in the 1970s they had risen by over 13% a year.

6/ Category IIIc countries are excluded, even though exposure is high in several of them, since with no further IBRD lending anticipated there is, operationally, little that can be done about the exposure.

Table 4.1: IBRD EXPOSURE

| PBD Risk Rating | Country | Debt Service Due IBRD as % of Exports 1975 | 1980 | 1985 | 1987 | 1990 | 1995 | Debt Service Due IBRD As % of Total Public and Publicly-Guaranteed MLT Debt Service 1980 | 1987 | 1990 | 1995 | Debt Due IBRD As % of Total Public and Publicly-Guaranteed MLT Debt 1980 | 1987 | 1990 | 1995 | Debt Service Due Preferred Creditors as % of Total Public and Publicly-Guaranteed MLT Debt Service 1987 | Year IBRD+IDA Net Transfers Turn Negative |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Countries Where IBRD Exposure is of Concern | | | | | | | | | | | | | | | | | |
| IIIb | Kenya | 0.6 | 2.0 | 5.8 | 7.4 | 7.3 | | 15.2 | 27.3 | 29.1 | | 12.7 | 24.1 | 18.5 | | 45.6 | Already |
| IIIb | Cote d'Ivoire | 0.4 | 0.8 | 3.9 | 6.0 | 7.0 | 7.4 | 3.4 | 13.1 | 18.6 | | 7.1 | 24.1 | 36.2 | | | FY90 |
| IIIb | Morocco | 1.6 | 2.4 | 5.5 | 5.9 | 5.2 | 4.5 | 6.0 | 18.1 | 12.1 | 39.5 | 7.3 | 15.5 | 24.9 | 44.8 | 46.6 | FY90 |
| IIIb | Honduras | 1.7 | 1.7 | 3.6 | 5.7 | 4.4 | 3.2 | 16.8 | 22.8 | 25.4 | 22.8 | 15.1 | 17.0 | 13.0 | 13.2 | 35.3 | Already |
| IIIb | Jamaica | 0.5 | 1.3 | 4.9 | 6.0 | | | 7.1 | 12.1 | | | 10.1 | 14.2 | | | 45.9 | Already |
| IIIb | Paraguay | 0.8 | 1.0 | 4.8 | 7.6 /b | | | 8.9 | 25.8 | | | 12.6 | 16.5 | | | | Already |
| IIIb | Philippines | 0.8 | 1.3 | 3.8 | 5.6 | 5.4 | 4.2 | 13.2 | 16.2 | 16.9 | 11.1 | 12.4 | 18.0 | 15.8 | | 27.6 | Already |
| IIIa | Romania /a | | 0.7 | 2.2 | 4.4 | 3.1 | | 6.3 | 18.2 | 26.5 | | 10.8 | 32.9 | 31.9 | | | Already |
| IIIa | Turkey | 1.5 | 3.6 | 3.6 | 5.6 | 5.9 | 5.5 | 12.1 | 19.9 | 21.2 | 23.8 | 7.0 | 25.2 | 27.8 | 25.6 | | FY88 |
| IIc | Tunisia | 1.0 | 1.1 | 3.4 | 5.1 | 5.6 | 5.0 | 7.9 | 19.6 | 16.8 | 28.7 | 8.3 | 16.2 | 19.9 | 24.5 | 23.2 | FY91 |
| IIc | Colombia | 3.6 | 2.5 | 6.7 | 8.3 | 7.4 | 5.1 | 27.2 | 27.6 | 25.7 | 21.4 | 24.3 | 27.4 | 24.2 | 18.1 | 33.6 | Already |
| Other Countries With Significant Levels of IBRD Exposure | | | | | | | | | | | | | | | | | |
| IIIb | Malawi | 0.0 | 0.4 | 2.5 | 4.0 | 3.5 | 2.3 | 1.8 | 11.3 | 16.0 | 13.9 | 3.6 | 7.3 | 6.7 | 3.4 | 49.3 | After FY96 |
| IIIb | Mexico | 1.8 | 1.0 | 2.1 | 4.5 | 4.4 | | 3.2 | 7.8 | 7.8 | | 6.1 | 7.1 | 7.5 | | 8.7 | FY88 |
| IIIb | Nigeria | 0.4 | 0.2 | 1.0 | 4.7 | 4.6 | 5.7 | 13.7 | 16.7 | | | 12.2 | 10.7 | | | | After FY96 |
| IIIa | Brazil | 1.0 | 1.2 | 2.8 | 4.4 | 4.0 | 3.2 | 3.5 | 6.9 | 9.0 | 13.8 | 5.2 | 9.5 | 10.2 | 12.2 | 12.5 | Already |
| IIc | Indonesia | | 0.5 | 2.0 | 4.4 | 5.0 | 5.1 | 6.8 | 17.1 | 19.3 | 24.1 | 6.9 | 17.9 | 19.6 | 26.4 | | FY89 |
| IIc | Cameroon | 0.6 | 0.8 | 1.3 | 2.6 | 3.2 | 2.8 | 8.1 | 21.9 | 26.9 | 29.9 | 7.4 | 19.7 | 18.1 | 14.0 | 28.1 | Already |
| IIb | India | 1.6 | 1.1 | 2.3 | 3.7 | 4.5 | 4.7 | 13.6 | 16.4 | 26.7 | 37.5 | 4.6 | 11.1 | 13.6 | 15.0 | 51.6 | After FY96 |
| Average of Above | | 1.1 | 1.3 | 3.5 | 5.4 | 5.0 | 4.5 | 9.7 | 17.7 | 19.9 | 24.2 | 9.7 | 17.5 | 19.2 | 19.7 | 34.0 | |
| Average of Baker Countries /c | | 1.1 | 1.2 | 2.9 | 4.5 | 4.3 | 3.7 | 8.1 | 12.2 | 11.7 | 14.5 | 8.8 | 11.8 | 13.6 | 14.8 | | |
| Average for All Developing Countries /d | | | 0.7 | 1.4 | 2.1 | 2.1 | 2.0 | 4.5 | 9.7 | 10.1 | 12.6 | 6.1 | 9.2 | 10.8 | 11.4 | | |

/a For Romania, Private Non-Guaranteed MLT Debt is Included With Public and Publicly-Guaranteed MLT Debt.

/b 1986 data.

/c Includes individual Baker countries shown above, plus other countries on Baker's original list of 15, plus Costa Rica, Jamaica, and Turkey.

/d Total exports, debt and debt service taken from WDR Central Case Scenario, December 30, 1986. IMF debt and debt service not available.

Note: Averages for Baker countries and for high exposure countries are simple averages calculated with equal weight to each country. The Averages for All Developing Countries are calculated from totals across all countries.

Sources: Historical data from EPD Debt Data Files. Projections of IBRD DOD, debt service and net transfers done by PBD, while projections of exports, preferred creditors, and total public and publicly-guaranteed MLT debt service done by Regions.

programs of varying degrees of strength are, however, underway in all except Honduras and Paraguay. Paraguay has seen Bank exposure grow rapidly in recent years, in part a consequence of a decline in exports. However, IBRD debt service has also grown rapidly, despite the fact that there has been no lending since FY84, as the grace periods expire on loans which were rapidly built up in the late 1970s and early 1980s. IBRD debt service in 1986 was 6.9 times its level of 1980.

4.11 Bank exposure in Romania is high in part because the country has been reducing the total stock of its outstanding debt. However, Bank debt service is also moderately high at 4.4% of its exports, and the high level of exposure may account, in part, for the arrears of Romania to the Bank in 1986, when disbursements were suspended through much of the year. Bank exposure in Turkey was considered borderline last year, when it was anticipated that Bank debt service would account for about 4% of Turkey's exports. However, because of the dollar depreciation as well as disappointing export performance, the ratio for 1987 is anticipated to be 5.6%, and is projected to grow to 5.9% in 1990. The Bank also accounts for 25% of Turkey's public debt. Tunisia and Colombia are both rated IIc. Exposure is high, however, particularly in Colombia, and projected to remain so until at least 1990. Net transfers are also already negative in Colombia.

4.12 The countries shown in the bottom part of Table 4.1 are borderline cases where the situation should be monitored. Exposure grew rapidly in some of them (Mexico, Nigeria, and Indonesia) because of the 1986 collapse in oil export prices. IBRD debt service as a proportion of exports is expected to more than double in each between 1985 and 1987. In Brazil, as well as Mexico, IBRD debt or debt service as a proportion of the country's total debt or debt service is relatively small, but this is a consequence of the relatively high levels of debt in each of these countries. As a proportion of exports, IBRD debt service rose by a factor of four in both Brazil and Mexico between 1980 and 1985. In Malawi and India it is important to consider IDA debt service as well as IBRD. In both countries the combined IDA/IBRD exposure ratios are quite high, particularly in India. In both countries net transfers, with IDA included, do however remain positive throughout the projection period. It should also be noted that in Malawi, which is rated IIIb, no further IBRD lending is currently anticipated in the lending program.

4.13 Exposure Management. To mitigate exposure risks, the Bank should first of all give critical attention to its country lending strategies. For the countries shown in the top part of Table 4.1, the Bank's country strategies should give prominent attention to steps which will over time reduce Bank exposure, while for the other countries identified in the table, the exposure issue should be an explicit factor in determining the Bank's assistance strategy. The new Country Strategy Papers (CSPs) should address the issue directly, giving projections of what the exposure is anticipated to be, and discussing under what conditions that exposure could be at risk. The high level of exposure does not, of course, imply that new Bank lending should automatically cease. This would often, in any case, do more harm than good to the existing exposure. Rather, a

strategy should be formulated for managing that exposure over time, instead of leaving exposure as the residual outcome of a financing program that has been developed with other considerations in mind. An important part of the exposure strategy should be actions on the part of the Bank to improve burden sharing arrangements, both in overall financial packages and through more aggressive use of cofinancing.

4.14 The level of lending is obviously important in determining the path of Bank exposure. However, there are a number of other instruments through which exposure can be controlled. What is appropriate can of course only be decided on a case-by-case basis. Specifically, consideration should be given to: (i) the appropriate mix of fast, medium and slow disbursing loans, which can often have a powerful impact in the short term on the degree of exposure; (ii) the phasing of the lending program; (iii) the use of guarantees of less than 100% or of later maturities (when exposure is expected to be less); (iv) sales of some of the loans in the lower risk countries (India, Indonesia, Cameroon, and Colombia), although the sales would have to be structured differently than under the current program in order to reduce the Bank's de facto exposure; and (v) the orientation of Bank lending to operations which will directly promote exports. It is recognized that the impact on exposure of those measures which are available for a particular country is likely to be slow. This is all the more reason to develop an exposure management strategy early, before the situation has deteriorated to the point where options are extremely limited. It is also recognized that, as in high risk countries which are following an active adjustment program, the Bank as a development institution cannot avoid raising its exposure in certain countries where it is already high. Consideration must therefore be given to other risk management tools of the Bank to supplement the often limited possibilities here.

The Decline in Net Transfers

4.15 Trends in Net Transfers. The Bank's net transfers to its borrowing members are now undergoing an historic transition. They have been positive for borrowers as a whole from the beginning of the institution through FY86, but they are now projected to turn permanently negative in the aggregate starting in FY87. Many individual Bank members have already gone through this completely normal and expected cycle of net transfers being first positive and later negative, while for a number of others net transfers will remain positive for many years still to come. Still, this transition for the institution as a whole serves to point out that while net transfers to most Bank members (other than those graduating) were positive in the past during periods of crisis, this will not be true in the future.

4.16 There has been some confusion on why the state of net transfers is a factor in determining the safety of the Bank's outstanding exposure in a particular country. The Bank is a cooperative institution, with its borrowers also its members, and a country benefits over the long term from this relationship. However, debt service to the Bank does pose a financial burden, even if over the full life of the loan the net benefit is

positive. In a financial crisis, the country will place a high discount on the expected future net benefits of its relationship with the Bank, and a high premium on immediate cash flow. It may therefore suspend debt service to the Bank when there are short-term benefits to it to do so, which may be the case when net transfers are sufficiently negative.

4.17 It is also the case that net transfers will turn negative as the Bank matures as an institution unless the growth of the Bank is significantly higher than now anticipated. Net transfers thus differ from net disbursements, which can remain positive as long as the Bank has an expanding capital base. For net transfers to be positive, net disbursements must exceed the level of interest payments on the growing debt. This implies, with a current rate of Bank interest of about 8%, that net disbursements must equal 8% of the total debt outstanding each year, or that the total debt must grow by 8% a year. And to achieve this required level of net disbursements, gross disbursements will have to exceed net disbursements by the level of amortization payments. Amortization payments are currently roughly equal in size to total interest due. Although the Bank's gross disbursements have grown at this rate until this year (which is another way of saying net transfers have been positive in the aggregate until this year), it is currently anticipated the growth of the Bank's outstanding loans will fall short of this level from now on, given current lending plans.

4.18 Although given the currently anticipated growth of the Bank it is to be expected that net transfers will turn negative, there can be significant fluctuations in the short term. As of a year ago, it was projected that Bankwide net transfers would be positive, although quite small, until FY89 when they would turn permanently negative. The depreciation of the dollar has, however, brought this transition forward for reasons noted above. This is still subject to some uncertainty as the projected negative levels in FY87-89 are only $0.7 to $1.0 billion per year. Fluctuations in disbursements on a few policy-based loans could equal this. In the following paragraphs we discuss two ways in which net transfer can be increased, namely, through increasing the proportion of fast-disbursing operations and through the liberalization of lending terms.

4.19 Increasing Net Transfers: The Proportion of Fast-Disbursing Loans. Shifts in the share of fast-disbursing operations in the lending program can have a significant positive effect on net transfers, but only for a period of about seven years. Simulations are shown in Table 4.2 of the effects of assuming different proportions of fast-disbursing operations in the lending program in the 1990s. The results are shown separately for the Baker countries[7/] and for all other Bank borrowers. The base case,

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7/ Including Costa Rica, Jamaica and Turkey, but excluding Bolivia, Peru and Venezuela where no further IBRD lending is currently in the program.

Table 4.2: EFFECT ON NET TRANSFERS OF ALTERNATIVE SHARES OF FAST-DISBURSING LENDING

| | FY92-FY2000 Fast Disbursing Loans | Net Transfers ($ millions) | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | | FY91 | FY92 | FY93 | FY94 | FY95 | FY96 | FY97 | FY98 | FY99 | FY2000 |
| **A. Keep to FY91 Share of Fast-Disbursing Loans through FY2000.** | | | | | | | | | | | |
| Baker Countries | 18.2% | -1483 | -2043 | -2129 | -1883 | -1550 | -1521 | -1585 | -1784 | -2017 | -2339 |
| Other Borrowers | 7.0% | -859 | -1139 | -1076 | -928 | -967 | -1191 | -1452 | -1836 | -2248 | -2570 |
| Bank-Wide | 13.0% | -2343 | -3183 | -3205 | -2811 | -2517 | -2712 | -3037 | -3620 | -4265 | -4909 |
| **B. Return to FY87-91 Average Share of Fast Disbursing Loans.** | | | | | | | | | | | |
| Baker Countries | 31.1% | -1483 | -1767 | -1084 | -838 | -774 | -1016 | -1320 | -1715 | -2093 | -2511 |
| Other Borrowers | 11.9% | -859 | -1048 | -728 | -584 | -716 | -1030 | -1371 | -1818 | -2276 | -2626 |
| Bank-Wide | 22.0% | -2343 | -2815 | -1813 | -1421 | -1490 | -2046 | -2691 | -3532 | -4369 | -5137 |
| **C. Increase to 40% Average Share of Fast-Disbursing Loans.** | | | | | | | | | | | |
| Baker Countries | 56.1% | -1483 | -1187 | 1096 | 1272 | 722 | -136 | -956 | -1741 | -2369 | -2929 |
| Other Borrowers | 21.3% | -859 | -855 | -5 | 110 | -231 | -754 | -1262 | -1836 | -2372 | -2762 |
| Bank-Wide | 40.0% | -2343 | -2042 | 1091 | 1383 | 491 | -891 | -2219 | -3576 | -4740 | -5691 |

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panel A, assumes that fast-disbursing lending stays at the 13% level of FY91 through the 1990s; this is a scenario where the high proportion of fast-disbursing operations in the mid-1980s is viewed as a temporary phenomenon and, with adjustment completed, returns to a "normal" program of traditional loans. Panel B keeps the proportion of fast-disbursing operations after FY91 at 22%, which is the average of the FY87-91 program. Panel C sets the proportion even higher--at 40%. The effects on net transfers are significant; by FY93 net transfers Bankwide are $1.4 billion higher in the 22% case than in the 13% case, and $4.3 billion higher (and positive) in the 40% case than in the 13% case. However, the effect then begins to diminish as DOD and, hence, interest payments are higher with the acceleration in disbursements, and after eight years (i.e., by FY99) net transfers are in fact <u>less</u> in the 22% and 40% cases than in the 13% case. This occurs even though the scenarios assume that the Bank stays at the 22% or 40% proportions of fast-disbursing loans throughout. If the lending program had gone to the higher share of fast-disbursing operations only temporarily, net transfers would have dropped even further. There is therefore a ratchet-like effect: increasing the use of fast-disbursing loans raises net transfers only temporarily and unless the share is raised again net transfers will after a few years drop back to less than otherwise would have been the case.

4.20 Increasing Net Transfers: Liberalization of Lending Terms. Countries experiencing difficulties in servicing their Bank debt could be helped by a liberalization of lending terms, that is, by a lengthening of grace periods and/or maturities. This requires, however, an increase in Bank capital to finance the longer average terms, and it also raises the level of exposure of the Bank in the country's debt. Consideration is therefore being given to a scheme which would use bridge financing from third parties to offset the increase in capital requirements and exposure that would follow from a simple liberalization of terms. As currently discussed the scheme would lengthen grace periods to six years, during which financing would come from third parties. At the end of the sixth year, the Bank would then purchase the loan and would begin to receive repayments from the country as now. Since disbursements during the first six years would come from the third party rather than from the Bank, the average Bank capital requirement would be less. To neutralize the capital "freed up" by this process, it would be used to lengthen the maturities of the loans.[8/]

4.21 By lengthening the grace periods and the maturities, average annual amortization payments would be reduced. With interest due being paid to the third party during the grace period, the interest exposure of the Bank would be initially reduced.[9/] Total interest the country would have to pay would of course be unchanged if the interest rate on the bridge financing is the same as for World Bank financing.[10/] However, the Bank will have effectively reduced its risk somewhat, as the party providing the bridge financing would assume the interest risk during the grace period. Furthermore, provided the disbursements under such operations are viewed as Bank disbursements (which is appropriate even though the financing would be from a third party), Bank net transfers would be higher than they would otherwise be as interest and amortization payments to the Bank would be less. If introduced now, the effects would be particularly important during the early and mid-1990's, when many Bank borrowers would be in a large negative net transfer position vis-a-vis the Bank, but still in a relatively weak creditworthiness position under even optimistic scenarios.

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8/ The scheme is further described in the draft note of K. Jun and J. Wood, "Liberalization of IBRD Repayment Terms: Possible New Approach," February 16, 1987.

9/ In a long-run steady state, if the average maturities of the operations have been lengthened to keep the average capital requirements the same, then interest will be unchanged. However, during the transition period, which is what is relevant now, interest due the Bank would be reduced.

10/ It would, in fact, probably be less in the scheme now being discussed, as the general assumption is that the bridge financing would be in a low cost currency such as yen. The true realized cost will, of course, only be less provided exchange rates do not move adversely.

4.22 The quantitative effects of such a scheme are illustrated in Table 4.3. The impact on net transfers and on debt service due the Bank are shown for a simple terms liberalization (six years grace for all borrowers, and maturities lengthened to 23, 19 and 16 years for low, middle, and high income Bank borrowers), and terms liberalization with bridge financing for the grace period. It is assumed the scheme applies to 50% of all new loans to each country. The effect will vary by country, as it will depend on such factors as the share of fast-disbursing operations in the lending program and on the scale of new lending to the country relative to previous level. Even though the scheme would apply to only new loans from FY87 (and by assumption only to half), the effects are nonetheless significant by the early 1990's. Terms liberalization raises net transfers by $1.0 to $1.1 billion per year Bankwide in the mid-1990's above what it would otherwise be, while the addition of bridge financing raises net transfers by $2.1 to $2.2 billion above the base case. The effects begin to diminish after FY94, however. The effects are relatively more important for the Baker countries due to the major expansion of lending anticipated for these countries plus the high share of fast-disbursing operations in their programs. In terms of debt service, the amount due the Bank falls by 11% Bankwide in FY93, after which there is a steady decline in the impact of about 0.5% point a year. For the Baker countries, with their larger share of fast-disbursing operations, the peak reduction in debt service is 12.9% in FY93. Such a reduction in debt service due the Bank would reduce, for example, a Bank debt service to export ratio of 6% to a ratio of 5.2%. In a few individual countries, the reduction in debt service would be on the order of 20%.

Table 4.3: IMPACT ON NET TRANSFERS AND DEBT SERVICE OF TERMS LIBERALIZATION

| | FY87 | FY88 | FY89 | FY90 | FY91 | FY92 | FY93 | FY94 | FY95 | FY96 | FY97 | FY98 | FY99 | FY2000 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| I. Net Transfers | | | | | | | | | | | | | | |
| A. Base Case Levels (in $ millions) | | | | | | | | | | | | | | |
| Baker Countries | 192 | -131 | -407 | -1106 | -1483 | -2043 | -2129 | -1883 | -1550 | -1521 | -1585 | -1784 | -2017 | -2339 |
| Other Borrowers | -1173 | -566 | -434 | -794 | -859 | -1139 | -1076 | -928 | -967 | -1191 | -1452 | -1836 | -2248 | -2570 |
| Bankwide | -981 | -698 | -840 | -1900 | -2343 | -3183 | -3205 | -2811 | -2517 | -2712 | -3037 | -3620 | -4265 | -4909 |
| B. Terms Liberalization - Difference with Base (in $ millions) | | | | | | | | | | | | | | |
| Baker Countries | 0 | 0 | 0 | 55 | 222 | 494 | 683 | 686 | 642 | 612 | 563 | 497 | 431 | 363 |
| Other Borrowers | 0 | 0 | 0 | 24 | 85 | 244 | 390 | 413 | 426 | 418 | 391 | 361 | 329 | 300 |
| Bankwide | 0 | 0 | 0 | 79 | 307 | 739 | 1073 | 1099 | 1068 | 1030 | 954 | 858 | 760 | 663 |
| C. Terms Liberalization with Bridge Financing - Difference with BAse (in $ millions) | | | | | | | | | | | | | | |
| Baker Countries | 10 | 63 | 174 | 379 | 729 | 1115 | 1313 | 1309 | 1277 | 1266 | 1237 | 1195 | 1153 | 1110 |
| Other Borrowers | 6 | 34 | 96 | 218 | 411 | 654 | 816 | 855 | 383 | 891 | 878 | 860 | 841 | 824 |
| Bankwide | 16 | 97 | 270 | 597 | 1141 | 1769 | 2128 | 2164 | 2159 | 2157 | 2116 | 2055 | 1993 | 1934 |
| II. Impact on Debt Service Due IBRD of Terms Liberalization with Bridge Financing - Proportional Difference with Base (%) | | | | | | | | | | | | | | |
| Baker Countries | -0.2 | -0.9 | -2.3 | -4.7 | -8.2 | -11.7 | -12.9 | -12.1 | -11.1 | -10.4 | -9.6 | -8.7 | -8.0 | -7.3 |
| Other Borrowers | -0.1 | -0.5 | -1.4 | -2.9 | -5.2 | -7.7 | -8.9 | -8.8 | -8.5 | -8.0 | -7.5 | -6.9 | -6.4 | -6.0 |
| Bankwide | -0.1 | -0.7 | -1.9 | -3.8 | -6.8 | -9.8 | -11.0 | -10.5 | -9.9 | -9.3 | -8.6 | -7.3 | -7.2 | -6.7 |

Portfolio Concentration

4.23 For any financial institution, measures of internal concentration are an important indicator of the risk of its loan portfolio. Diversification is important. However, given the nature of the Bank, one cannot compare the diversification of its portfolio with that of a commercial institution. First, the Bank is a cooperative institution, with its borrowers also its members and also sovereign governments. The relevant universe over which the Bank can lend (a limited number of sovereign governments) is vastly more constrained than the universe of borrowers available to any major commercial institution. It is therefore difficult to determine what degree of portfolio concentration might be considered excessive for the Bank. One should, however, monitor the trends as well as relate the shares of the top borrowers to the Bank's reserves and/or equity of the institution. This section will examine these trends.

4.24 Trends in Portfolio Concentration. Trends in past and projected portfolio concentration as well as the portfolio shares of the major Bank borrowers are shown in Table 4.4 and Diagram 1. The history to FY85 was described in the last year's Creditworthiness Review. Briefly, concentration fell in the 1960s, as the Bank matured and broadened its base of borrowers, and then stabilized through the 1970s. Between FY80 and FY85 it increased sharply, however, reflecting increased shares of one percentage point of the portfolio or more in Brazil, Indonesia, Turkey, the Philippines, Thailand and India, all of whom were in the top ten for IBRD borrowings outstanding in FY85. Concentration is projected to continue to rise to FY95. This basically reflects the orientation in lending to a middle-tier group of highly-indebted countries; the countries in FY95 which would hold positions 5 through 10 in the ranking by portfolio share would be Mexico, Turkey, Nigeria, the Philippines, Argentina and Colombia, with Morocco as number 11.

4.25 The portfolio projections are based on lending plans as of November 1986. These may change for some of the significant borrowers. In particular, the projections for Brazil are based on assumed lending of $1.1 billion in FY87 without any fast-disbursing operations, and $2.0 billion per year in FY88-90 with one fast-disbursing operation in each year of $500 million ($250 million in FY90). With this lending program, the Brazil share of the portfolio would decline from 10.7% as of September 1986, to 10.0% in FY90 and to 8.9% in FY95. However, consideration is now being given to increased Bank lending to Brazil with an emphasis on fast-disbursing operations; the situation warrants continued close monitoring.

4.26 To judge the risk of the portfolio concentration in the top borrowers, one should go beyond purely internal measures of that concentration to consider also the trends in the shares of the top borrowers relative to Bank reserves and equity. These are shown in Table 4.5 and in Diagrams 2 and 3. The trends are clear, particularly in the diagrams, and were discussed for the period through FY85 in last year's Creditworthiness Review. Briefly, loans to the largest borrowers first fell as a proportion of reserves in the 1960s but then started growing at a faster pace

Table 4.4: PAST AND PROJECTED PORTFOLIO CONCENTRATION
(Percentage Shares)

| | FY60 | FY65 | FY70 | FY75 | FY80 | FY85 | FY90 | FY95 |
|---|---|---|---|---|---|---|---|---|
| Portfolio Shares Of: | | | | | | | | |
| Major Borrowers /a | | | | | | | | |
| Brazil | 5.8 | 4.6 | 3.8 | 9.1 | 9.1 | 10.4 | 10.0 | 8.9 |
| Mexico | 4.9 | 7.7 | 9.1 | 9.9 | 8.8 | 7.9 | 8.2 | 8.1 |
| Korea | 0.0 | 0.0 | 0.1 | 2.4 | 7.0 | 7.3 | 4.3 | 2.2 |
| Indonesia | 0.0 | 0.0 | 0.0 | 0.1 | 3.7 | 6.7 | 7.8 | 8.5 |
| Turkey | 1.8 | 0.9 | 0.7 | 2.3 | 4.3 | 6.6 | 7.2 | 6.8 |
| Philippines | 0.5 | 1.3 | 1.9 | 1.7 | 3.4 | 4.8 | 3.9 | 3.4 |
| Yugoslavia | 1.8 | 3.5 | 3.8 | 4.7 | 5.7 | 4.5 | 2.6 | 1.6 |
| Colombia | 2.6 | 5.4 | 5.5 | 5.9 | 4.1 | 4.4 | 4.2 | 3.4 |
| Thailand | 1.8 | 2.4 | 2.6 | 2.4 | 2.8 | 4.3 | 2.9 | 1.8 |
| India | 15.3 | 13.7 | 8.4 | 4.4 | 3.3 | 4.3 | 8.1 | 11.0 |
| Nigeria | 0.0 | 0.5 | 2.4 | 3.0 | 2.4 | 2.5 | 4.2 | 5.9 |
| China | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.6 | 3.5 | 8.2 |
| Largest Borrower | 15.3 | 13.7 | 9.1 | 9.9 | 9.1 | 10.4 | 10.0 | 11.0 |
| Top 4 | 40.7 | 37.7 | 30.9 | 29.6 | 30.6 | 32.4 | 34.2 | 36.7 |
| Top 6 | 51.8 | 46.9 | 40.1 | 38.5 | 39.0 | 43.7 | 45.6 | 51.5 |
| Top 10 | 68.1 | 60.3 | 52.9 | 51.9 | 52.4 | 61.3 | 61.3 | 67.6 |
| Nos. 2-4 | 25.4 | 24.0 | 21.9 | 19.7 | 21.6 | 21.9 | 24.1 | 25.7 |
| Nos.5-10 | 27.4 | 22.6 | 22.0 | 22.3 | 21.7 | 28.9 | 27.2 | 31.0 |

/a Major borrowers are shown ranked by portfolio share of FY85, and are defined as borrowers with a portfolio share in FY85, or share projected for FY90 or FY95, in excess of 4.0%.

Notes: The shares of the top 4, 6 and 10 borrowers are defined over the entire Bank portfolio of the period, and not simply over the individual borrowers shown above.

IBRD loans to IFC excluded throughout.

**Diagram 1:**
**Past and Projected Portfolio Concentration**
(percentage shares)

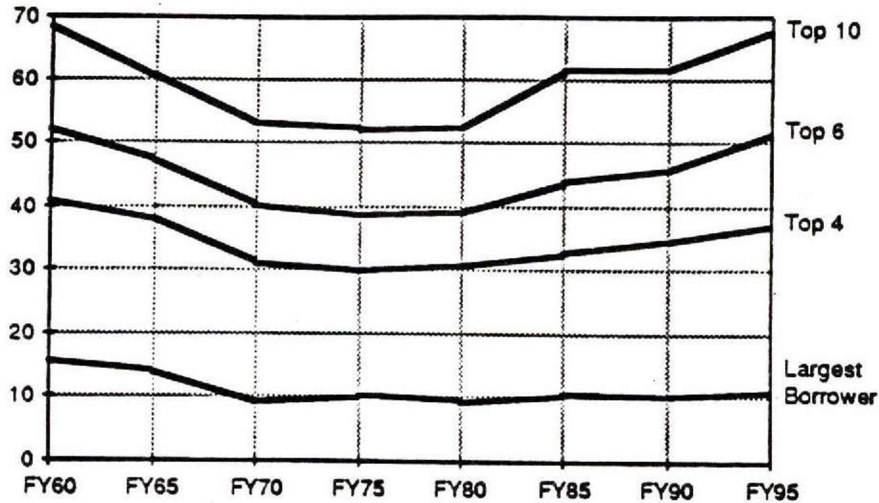



Table 4.5: LOANS OUTSTANDING AND DISBURSED AS A SHARE OF RESERVES AND EQUITY/a
(Percentage Shares)

| | FY60 | FY65 | FY70 | FY75 | FY80 | FY85 | Present System of Lending Rates Assumed FY90 | FY95 |
|---|---|---|---|---|---|---|---|---|
| Loans as percentage of Reserves /b | | | | | | | | |
| Largest Borrower | 84.6 | 58.8 | 40.1 | 61.4 | 82.4 | 105.8 | 95.8 | 74.3 |
| Top 4 | 225.5 | 161.3 | 136.8 | 183.3 | 278.3 | 327.5 | 326.5 | 247.4 |
| Top 10 | 377.4 | 257.9 | 234.0 | 321.7 | 475.6 | 620.4 | 586.2 | 456.3 |
| Total Loans | 554.2 | 428.1 | 442.2 | 619.7 | 908.4 | 1012.2 | 955.8 | 674.9 |
| Loans as percentage of Equity /c | | | | | | | | |
| Largest Borrower | 16.5 | 16.8 | 14.2 | 22.7 | 32.3 | 42.3 | 48.4 | 46.8 |
| Top 4 | 44.0 | 46.2 | 48.3 | 67.7 | 109.3 | 130.8 | 164.8 | 155.8 |
| Top 10 | 73.7 | 73.8 | 82.7 | 118.8 | 186.8 | 247.9 | 295.9 | 287.4 |
| Total Loans | 108.3 | 122.5 | 156.3 | 228.9 | 356.8 | 404.4 | 482.5 | 425.0 |

/a FY90 and FY95 projections of reserves and equity from FPA.
/b Reserves are defined as the Bank's Special plus General Reserves, plus (from FY86) Loan Loss Provisions, and excludes the current year's accumulation of Bank net income.
/c Equity is defined as reserves plus current year Bank net income net of any IDA allocation plus paid-in capital. The projections for FY90 and FY95 are from FPA, and are based on the assumption that while current authorized capital becomes fully subscribed, any future capital increase has a zero paid-in portion.

**Diagram 2:**
**Loans Outstanding as a Share of Reserves**
**Under Present System of Lending Rates**
(percentage shares)

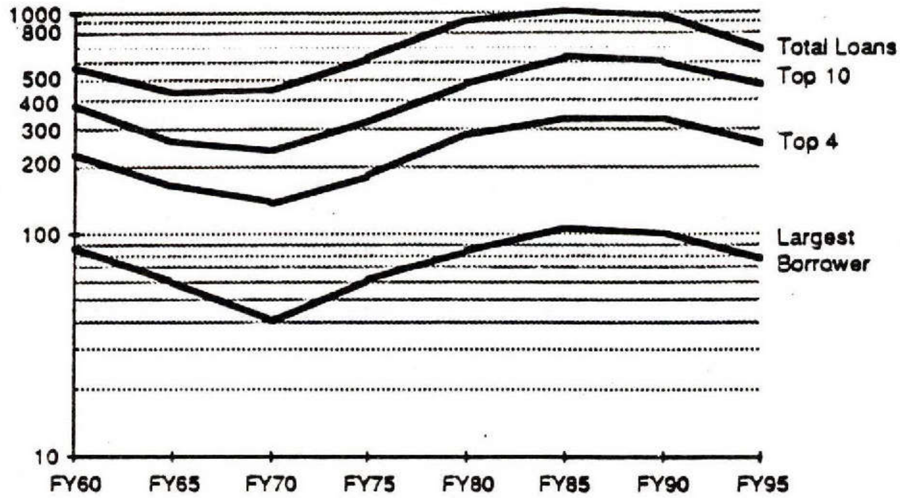
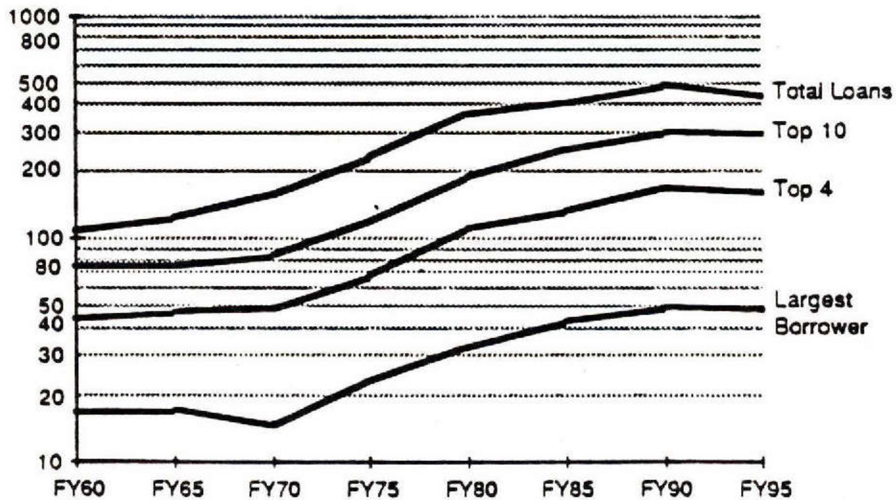



**Diagram 3:**
**Loans Outstanding as a Share of IBRD Equity**
**Under Present System of Lending Rates**
(percentage shares)



than reserves. This trend may now improve, however, because with the present system of loan charges, reserves should grow faster than loans.

4.27 The projected improvement in safety does not carry over when the focus is on equity rather than reserves. Here the ratios have grown steadily larger, particularly since FY70, and although there may be some leveling off and perhaps an improvement in the ratios from FY90, the ratios at end-FY95 would still be worse than at end-FY85.[11]

4.28 Portfolio concentration has therefore risen in the 1980s, and is projected to continue to rise until at least FY95 under current lending plans. Expressed as a ratio to reserves or of equity, there has been a steady increase for the top borrowers since FY70. However, loan charges are now such that barring such shocks as significant extended arrears, further adverse exchange rate changes, and/or a significant reduction in the lending margin, the key ratios should level off and begin to improve.

4.29 Bank Policy on Portfolio Concentration. In managing its loan portfolio, the Bank for some time followed two guidelines related to portfolio concentration:

- Limiting the combined share of the Bank's four largest borrowers, expressed in terms of the aggregate amount of loans disbursed and outstanding (DOD), to about one third of the total portfolio;

- Limiting the portfolio share of any individual borrower to about 10% of total DOD, recognizing that this limit may be exceeded for limited time periods if warranted by special circumstances.

In Board discussions during the course of 1985, it was agreed that the former guideline (the one-third total for the four largest borrowers) should be abandoned. However, the 10% guideline--to be applied flexibly--was reaffirmed, although primarily to ensure an equitable distribution of Bank resources across its borrowing members until the next GCI would clarify resources availabilities. For financial prudence concerns, it was agreed that a liberalization of the guideline to 12% or 12.5% would not be unwarranted if justified on country grounds, given the Bank's other tools for risk management.[12]

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11/ For lack of any decisions as yet on the timing of the next GCI or the level of the paid-in portion of that GCI, the projections assume that any future GCI would have a zero paid-in portion. To the extent there is any paid-in portion, the FY95 figures would improve.

12/ This is described in the Board Paper, "10% Exposure Guideline", SecM85-880, July 17, 1985.

The Risk of Arrears and the Bank's Financial Management

4.30 Despite Bank efforts to limit credit risk, countries may, at some point in the future, default on their debt service obligations. The question is whether the Bank will be able to absorb the attendant losses. In this section we will first examine the basic financial ratios as indicators of the Bank's financial strength, then examine the financial consequences of certain levels of default and finally review what, if anything, needs to be done to strengthen the Bank's financial condition.

4.31 Trends in the Bank's Financial Ratios. The basic financial ratios of any lending institution are important determinants of the continued ability to lend in the face of extended arrears or defaults on some of its loans. This is also true for the World Bank, although given its structure the critical levels of such ratios and their interpretation will differ from those of a commercial institution. Several of the key ratios are shown in Table 4.6, with data going back to FY60 to show the long-term trends.

Table 4.6: IBRD FINANCIAL RATIOS
(Percentage Shares)

| | FY60 | FY65 | FY70 | FY75 | FY80 | FY85 | FY86 |
|---|---|---|---|---|---|---|---|
| Ratios to Total Loans | | | | | | | |
| Reserves | 18.0 | 23.4 | 22.6 | 16.1 | 11.0 | 9.9 | 8.7 |
| Equity | 92.4 | 81.6 | 64.0 | 43.5 | 28.0 | 24.7 | 21.5 |
| Equity + Callable Capital of DAC Countries | 562.7 | 444.6 | 309.0 | 204.9 | 120.9 | 109.5 | 94.4 |
| Equity + Total Callable Capital | 708.1 | 590.9 | 418.7 | 279.1 | 164.9 | 156.7 | 139.1 |
| Ratio to Total Borrowings: | | | | | | | |
| Liquid Investments + Callable Capital of DAC Countries | 686.7 | 562.1 | 354.2 | 192.5 | 112.5 | 92.0 | 86.2 |

Definitions:
Total Loans: Outstanding loans to borrowing member countries, IFC excluded.
Reserves: Special plus General Reserves plus (from FY86) Loan Loss Provisions.
Equity: Reserves as defined above plus current year net IBRD income (net of any IDA allocation) plus total Paid-In Capital.
Callable Capital of DAC Countries: Callable capital as valued in current U.S. dollars of the 17 members of the Development Assistance Committee of the OECD who are also IBRD members.
Total Borrowings: Short and Long-Term Borrowings of the IBRD, including all payables under such borrowings (including net payables from currency swaps).
Liquid Investments: Cash plus other liquid investments, including all receivables from such investments.

Sources: IBRD Annual Reports and the Financial Statement of December 31, 1986.

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4.32 Reserves can be viewed as providing protection from an impairment of the Bank's capital should a country default. The Bank has managed its reserves in recent years with the aim of keeping them at about 10% of the portfolio, which would suffice to absorb a sudden default of any borrower, including the largest one.[13/] It is recognized, however, that the likelihood of a sudden and clear renunciation by a borrower of obligations to the Bank is remote, and thus as a rationale for reserve policy the argument is less than compelling. Should a country encounter difficulties, it is much more likely (as was the case with Nicaragua) that debt service will simply not be paid, and after six months the Bank will end accrual of interest and after two years begin to provision.[14/] The shock will therefore be absorbed over time, rather than all at once.[15/] Still, larger reserves in relation to the portfolio do provide a greater degree of protection, and trends in that ratio may be as important as its level in the perceptions of the financial markets in which the Bank must borrow. The argument that reserves afford a degree of protection to the Bank has also been extended by some to the Bank's equity.[16/] The argument would be that equity provides a similar cushion against the need to use callable capital in case of a severe adverse shock.

4.33 The depreciation of the dollar has affected the ratios of reserves to loans and equity to loans as the currency composition of loans differs from that of reserves and equity. The effect has been substantial. Comparing end-FY85 and end-FY86 positions, for example, the reserves to loans ratio fell from 9.9% to 8.7%[17/] despite a record level of net income. However, had exchange rates not changed, the ratio would have grown to 10.7% at end-FY86. The equity to loans ratio similarly fell from 24.7% at end-FY85 to 21.5% at end-FY86. Had exchange rates not changed, the ratio would have been 25.4% at end-FY86.

4.34 The reserves to loans ratio has now reached a level which current Bank policy views as a minimum below which it should not fall. Lending charges have therefore been set to generate net income adequate to raise

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13/ The policy is described in the Board Paper, "Review of IBRD Reserve Policy and Criteria for the Allocation of Net Income", R83-39, February 10, 1983.

14/ The policies on non-accrual are described in "Accounting Policy for Non-Accruing Bank Loans," SecM85-95, January 28, 1985, and for provisioning in "Provisions for Losses on Loans," R86-94, April 15, 1986.

15/ Simulations of how large a shock the Bank could absorb through its net income are presented later in this chapter.

16/ Equity is defined as the sum of paid-in capital, reserves and current year net income.

17/ Loans to IFC are excluded here and uniformly throughout this chapter.

this ratio. In the short run, exchange rate fluctuations will dominate, as noted in the previous paragraph. But it is currently projected that at current exchange rates, and provided extended arrears or defaults do not occur to reduce net income, the reserves to loans ratio should recover to 10.5% of the loan portfolio by FY90 and be on a growing path (assuming the current loan charges system is maintained) to reach a level of almost 15% by FY95. The projected level of the equity to loans ratio would also stabilize and then grow in the 1990s. The reason is that reserves, which now make up about half of equity and which would under this scenario make up 70% of equity by FY95, will bring up the overall equity ratio.

4.35 The ultimate security of the Bank's bondholders is the callable capital of the Bank's members. The Bank is required, by its Articles of Agreement, not to have loans outstanding in excess of its total capital (callable and paid-in) plus its accumulated reserves. For most of its history, outstanding loans have been far below this level; indeed, until 1969 the callable capital of the U.S. alone sufficed to cover all outstanding loans. This has, however, changed in recent years, as the Bank's lending program has continued to grow while decisions on a General Capital Increase have been postponed. As shown in Table 4.6, the Bank's total capital declined to a level of only 139% of its outstanding loans at the end of FY86; this ratio had been over 700% in FY60, about 420% in FY70, and 165% in FY80. As was the case for equity, exchange rate changes can have a significant effect on this ratio in the short term, as callable capital is also valued at the capped SDR rate. Had exchange rates not changed during FY86, the ratio of total capital to loans would have been 158% at the end of the year rather than 139%.

4.36 As the ratio of total capital to loans has declined to levels closer to 100%, some have argued that a more meaningful ratio would include the callable capital of only the wealthier, non-borrowing members of the Bank. In the event of default by a sizeable proportion of the Bank's borrowers, it would be unreasonable to assume that the callable capital of these same borrowers would be made available. Table 4.6 shows that the ratio of the Bank's equity plus the callable capital of the DAC countries to total loans outstanding fell below 100%, to a level of 94.4%, at end-FY86 for the first time in the Bank's history. Had exchange rates not changed during FY86, the ratio would have stood at 107% at end-FY86.

4.37 A different ratio that might be of more interest to the Bank's bondholders relates the Bank's liquid investments (including cash) plus callable capital of the DAC countries to the Bank's total borrowings. This ratio counts only those assets which are readily available in the event of a crisis, plus the callable capital of the major backers of the institution, and relates this directly to the Bank's obligations to its bondholders. As Table 4.6 shows, this ratio is also now below 100%, having reached a level of 86% at end-FY86.

4.38 The long-term downward trends of the key financial ratios shown in Table 4.6 are, of course, not any surprise, but rather the outcome of deliberate decisions on the system of loan charges and on the size and timing of capital increases for the Bank. It would, indeed, be wasteful

increasing risk

to continue to maintain the extremely high ratios necessary when the Bank was a young and untested institution. Nonetheless, these ratios have by now reached levels which current policy indicates should be viewed as close to minima, below which there could be dangers. Exchange rate changes can have significant short-term effects, and the sharp depreciation of the dollar since February 1985 has in particular led to a major downward shift in the ratios. Over the long term, the reserves ratio depends essentially on the system of loan charges, and the present charges are such that the ratio should now reverse its long-term decline and begin to rise unless there are significant problems with arrears or large further depreciation of the dollar. The future movement of the other ratios will depend on decisions made on the size, timing, and paid-in share of the next General Capital Increase.

4.39 The Bank's Vulnerability to Arrears. Despite Bank policies to control country credit risk, there is a risk that the Bank may have to absorb through its net income a suspension of service payments by one or more of its borrowers. Current procedures are that if a country has not produced a service payment, the Bank suspends after 75 days all Bank and IDA disbursements to the country for all projects; after six months it stops accruing interest income on the loans and reverses out of net income all previously accrued interest not received; and after two years it decides whether to set aside out of net income any provisions for losses on these now doubtful loans.

4.40 There are several trends which indicate that the Bank's excellent repayment record cannot be simply extrapolated into the future. First, arrears of a number of borrowers have grown in importance in recent years. Nicaragua was the first Bank borrower whose loans, in late 1984, were placed on non-accrual status and in June 1986 had to be provisioned against. Guyana was placed on non-accrual status in December 1986 and Syria in January 1987. Liberia was on non-accrual status between June and September 1986. Suspensions of disbursements are becoming more frequent, with difficulties arising for even some of the larger borrowers. Romania (2.9% of the portfolio) had disbursements suspended for much of 1986. Second, net transfers will become increasingly negative, which under certain conditions discussed in para. 4.16 may induce a country to renege on its repayment obligations to the Bank. Third, the rise in Bank exposure since 1980 shown in Table 4.1 is likely to continue. Most of the financing scenarios presented in the Medium-Term Growth Strategy Papers written for the Baker countries propose a Bank share of the incremental lending which is greater than the current 11.8% average share. More generally, the Bank is increasingly being asked to move boldly in a number of high risk cases, such as in Mexico, Jamaica, Chile, and Morocco.

4.41 Since history cannot provide a reasonable guide, the approach which will be used here will be to assume that a percentage of loans in particular categories of countries will cease being serviced. The purpose is to test the sensitivity of the net income projections to various default

scenarios, as well as to see trends over time. The methodology is described in the last year's Creditworthiness Review.[18]

4.42 The results, shown in Table 4.7 and in Diagrams 4 to 6, indicate that the deterioration in net income resulting from extended arrears on a given portion of the portfolio is much greater than projected last year. The 30% case in last year's report led to essentially zero levels of Bank net income for the period of provisioning; the same probabilities would now lead to negative net income of $200-300 million per year. The principal cause of this is that net transfers are now negative for more countries than was projected last year, mostly due to depreciation of the dollar. With the probability of default assumed to be higher when net transfers are negative, more loans are at risk.

4.43 The effects on Bank net income of arrears by individual countries, or small groups of countries, is shown in Table 4.8 and in Diagrams 7 to 9. While the countries are all high risk, the choice was abritrary and purely illustrative; inclusion is not meant to imply that a cessation of debt service to the Bank is anticipated. The basic result is that if a country, or a group of countries, with outstanding Bank loans equal to $4.4 billion (6.3% of the portfolio) or more go into default, the Bank net income would fall to a negative level in FY90. Default by Brazil, Mexico, Indonesia or Turkey individually would thus suffice to wipe out the entire Bank net income. Combinations such as Nigeria and the Philippines, or Nigeria, Peru and Romania, would also suffice.

4.44 There are, of course, likely to be indirect repercussions if one or more major borrowers ceases to service Bank debt, which have not been taken into account here. Financial markets are likely to react, for

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18/ Briefly, a specific probability of extended arrears for IIIc countries was chosen with three cases tried (30%, 20%, 10%). It was then assumed the probability of extended arrears of IIIb countries with negative net transfers was half of the IIIc rate, that for IIIa countries with negative net transfers it was half again, and for IIc countries with negative net transfers half again. A zero probability was assumed for countries in category IIb and above. For IIIb, IIIa and IIc countries with positive net transfers, a probability was assumed of half that in each category for the countries with negative net transfers. It is assumed the arrears all start in FY88 and provisioning to two years later in FY90, with the provisioning at a rate of 20% of the loan amount for each of five years. The scenarios are in a sense, thus, "worst case" scenarios in that they assume debt service is suspended by all the borrowers at exactly the same time, rather than being staggered over time. They also assume that after the five years of provisioning the bad loans have been "cleansed" from the portfolio, with no new loans going into arrears, so net income returns part way back to its base path.

Table 4.7: EFFECTS OF EXTENDED ARREARS ON IBRD NET INCOME

A. Total Loans Which Would Go Into Arrears

| Assumed Probabilities | In Dollars Millions End FY87 | In Dollars Millions End FY91 | As % of Total Loans End FY87 | As % of Total Loans End FY91 |
|---|---|---|---|---|
| 10% Anchor | 1693 | 2086 | 2.4% | 2.3% |
| 20% Anchor | 3385 | 4172 | 4.9% | 4.6% |
| 30% Anchor | 5077 | 6258 | 7.3% | 6.8% |
| 1986 Report 30% Anchor /a | 3564 | 4575 | 6.0% | 5.6% |

B. Effects on Projected Income and Reserves

| | FY88 | FY89 | FY90 | FY91 | FY92 | FY93 | FY94 | FY95 |
|---|---|---|---|---|---|---|---|---|
| 1. IBRD Net Income ($m) | | | | | | | | |
| No Arrears | 1086 | 1246 | 1417 | 1546 | 1645 | 1811 | 1917 | 2020 |
| 10% Anchor | 899 | 1039 | 835 | 969 | 1001 | 1138 | 1215 | 1631 |
| 20% Anchor | 752 | 871 | 293 | 392 | 356 | 464 | 513 | 1242 |
| 30% Anchor | 604 | 704 | -249 | -185 | -288 | -210 | -189 | 853 |
| 1986 Report 30% Anchor | 665 | 149 | 97 | 43 | 35 | 85 | 694 | 892 |
| 2. Return on Average Earning Assets (ROA) (%) | | | | | | | | |
| No Arrears | 1.25 | 1.36 | 1.46 | 1.48 | 1.46 | 1.48 | 1.46 | 1.42 |
| 10% Anchor | 1.03 | 1.13 | 0.86 | 0.93 | 0.89 | 0.93 | 0.92 | 1.15 |
| 20% Anchor | 0.86 | 0.95 | 0.30 | 0.38 | 0.32 | 0.38 | 0.39 | 0.87 |
| 30% Anchor | 0.70 | 0.77 | -0.26 | -0.18 | -0.25 | -0.17 | -0.14 | 0.60 |
| 1986 Report 30% Anchor | 0.82 | 0.17 | 0.10 | 0.04 | 0.03 | 0.07 | 0.55 | 0.65 |
| 3. Reserves/Loans Ratio (%) | | | | | | | | |
| No Arrears | 9.9 | 10.5 | 11.1 | 11.8 | 12.4 | 13.0 | 13.6 | 14.0 |
| 10% Anchor | 9.9 | 10.2 | 10.6 | 10.7 | 10.8 | 10.8 | 11.0 | 11.1 |
| 20% Anchor | 9.9 | 10.0 | 10.2 | 9.7 | 9.3 | 8.8 | 8.5 | 8.2 |
| 30% Anchor | 9.9 | 9.9 | 9.9 | 8.7 | 7.8 | 6.8 | 6.1 | 5.4 |
| 1986 Report 30% Anchor | 10.0 | 10.1 | 9.5 | 8.8 | 8.0 | 7.3 | 6.7 | 6.7 |

/a Figures as projected for 30% Anchor Case in 1986 Creditworthiness Report.

**Diagram 4:**
**Effects of Extended Arrears on IBRD Net Income**
**($ millions)**

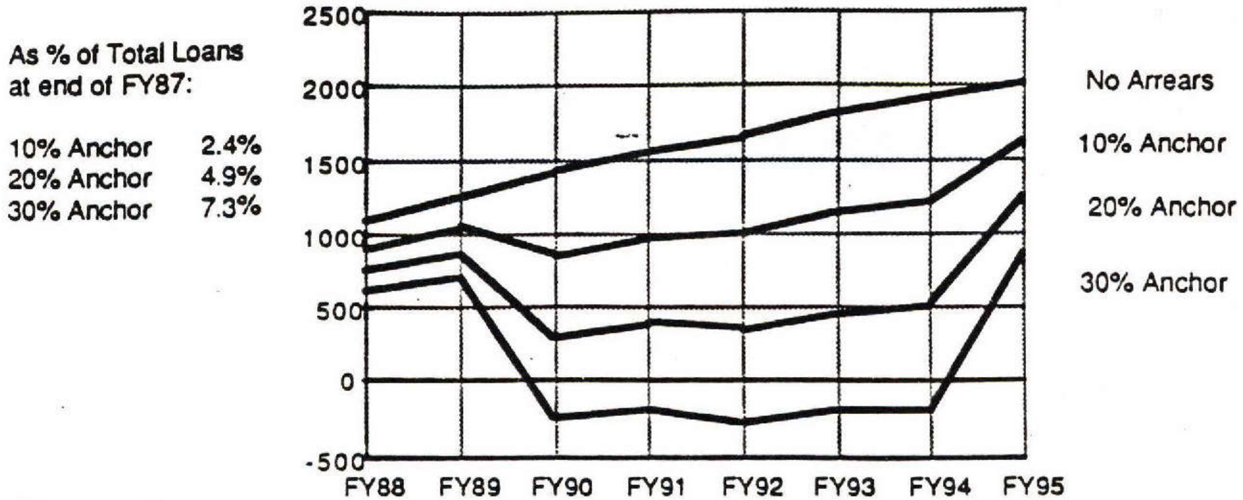


**Diagram 5:**
**Effects of Extended Arrears on IBRD ROA**

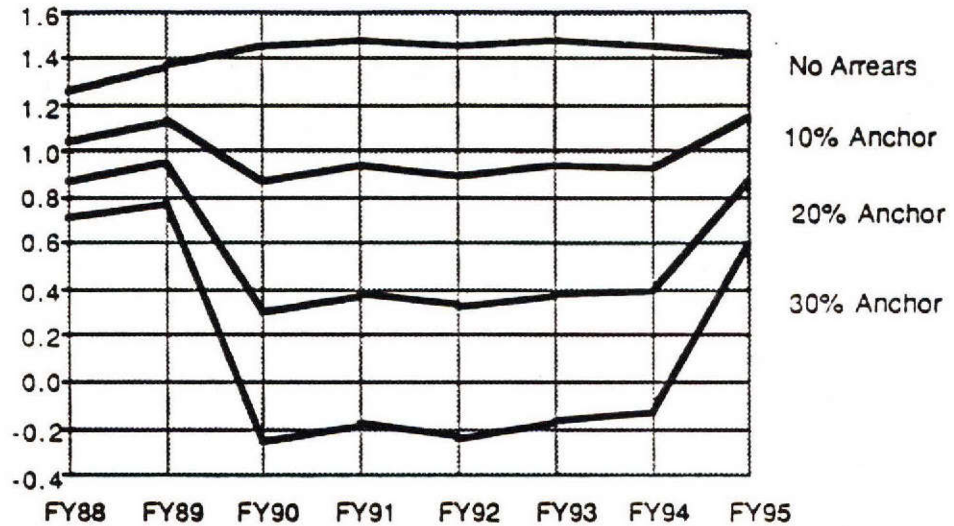


**Diagram 6:**
**Effects of Extended Arrears on IBRD Reserves/Loans Ratio**

Table 4.8: EFFECTS ON IBRD NET INCOME OF SPECIFIC COUNTRIES FALLING INTO ARREARS

A. Total Loans Which Would Go Into Arrears

| Countries | DOD at End-FY87 In Dollars Millions | DOD at End-FY87 As % of Portfolio |
|---|---|---|
| Peru | 974.5 | 1.4% |
| Romania | 1710.4 | 2.5% |
| Nigeria | 1989.5 | 2.9% |
| Philippines | 3086.5 | 4.4% |
| Peru, Nigeria and Romania | 4674.4 | 6.7% |
| Philippines and Nigeria | 5076.0 | 7.3% |
| Mexico | 5736.5 | 8.3% |

B. Effects on Projected Income and Reserves /a

| | FY88 | FY89 | FY90 | FY91 | FY92 | FY93 | FY94 | FY95 |
|---|---|---|---|---|---|---|---|---|
| 1. IBRD Net Income ($m) | | | | | | | | |
| No Arrears | 1086 | 1246 | 1417 | 1546 | 1645 | 1811 | 1917 | 2020 |
| Peru | 957 | 1112 | 1087 | 1256 | 1357 | 1526 | 1635 | 1936 |
| Romania | 906 | 107 | 909 | 1082 | 1186 | 1358 | 1467 | 1913 |
| Nigeria | 849 | 955 | 664 | 761 | 787 | 882 | 907 | 1318 |
| Philippines | 776 | 905 | 435 | 577 | 646 | 786 | 858 | 1541 |
| Peru, Nigeria and Romania | 620 | 728 | -95 | 7 | 39 | 144 | 175 | 1127 |
| Philippines and Nigeria | 578 | 654 | -278 | -209 | -212 | -144 | -152 | 839 |
| Mexico | 544 | 635 | 421 | -347 | -334 | -237 | -217 | 937 |
| 2. Return on Average Earning Assets (ROA) (%) | | | | | | | | |
| No Arrears | 1.25 | 1.36 | 1.46 | 1.48 | 1.46 | 1.48 | 1.46 | 1.42 |
| Peru | 1.10 | 1.21 | 1.12 | 1.21 | 1.20 | 1.25 | 1.24 | 1.36 |
| Romania | 1.04 | 1.17 | 0.94 | 1.04 | 1.05 | 1.11 | 1.11 | 1.34 |
| Nigeria | 0.98 | 1.04 | 0.69 | 0.73 | 0.70 | 0.72 | 0.69 | 0.93 |
| Philippines | 0.89 | 0.99 | 0.45 | 0.55 | 0.57 | 0.64 | 0.65 | 1.08 |
| Peru, Nigeria and Romania | 0.71 | 0.79 | -0.10 | 0.01 | 0.03 | 0.12 | 0.13 | 0.79 |
| Philippines and Nigeria | 0.67 | 0.71 | -0.29 | -0.20 | -0.19 | -0.12 | -0.12 | 0.59 |
| Mexico | 0.63 | 0.69 | -0.43 | -0.33 | -0.30 | -0.19 | -0.16 | 0.66 |
| 3. Reserves/Loans Ratio (%) | | | | | | | | |
| No Arrears | 9.9 | 10.5 | 11.1 | 11.8 | 12.4 | 13.0 | 13.6 | 14.0 |
| Peru | 9.9 | 10.3 | 10.8 | 11.1 | 11.5 | 11.8 | 12.3 | 12.6 |
| Romania | 9.9 | 10.3 | 10.7 | 10.8 | 11.0 | 11.2 | 11.6 | 11.8 |
| Nigeria | 9.9 | 10.2 | 10.5 | 10.3 | 10.2 | 10.1 | 10.1 | 10.0 |
| Philippines | 9.9 | 10.1 | 20.3 | 9.9 | 9.7 | 9.5 | 9.4 | 9.3 |
| Peru, Nigeria and Romania | 9.9 | 9.9 | 9.9 | 9.0 | 8.2 | 7.5 | 7.0 | 6.6 |
| Philippines and Nigeria | 9.9 | 9.8 | 9.8 | 8.6 | 7.7 | 6.8 | 6.1 | 5.4 |
| Mexico | 9.9 | 9.8 | 9.7 | 8.4 | 7.3 | 6.3 | 5.6 | 4.9 |

/a Each case except for the base "no arrears" case also includes the impact of Nicaragua on IBRD Net Income, ROA, and Reserves.

**Diagram 7:**
**Effects of Projected Income and Reserves**
**($ millions)**

% of total loan portfolio that would be in arrears at end of FY87:

| | |
|---|---|
| Peru | 1.4% |
| Romania | 2.5% |
| Nigeria | 2.9% |
| Philippines | 4.4% |
| Mexico | 8.3% |

No Arrears
Peru
Romania
Nigeria
Philippines
Mexico

2500
2000
1500
1000
500
0
-500

FY88 FY89 FY90 FY91 FY92 FY93 FY94 FY95

**Diagram 8:**
**Return on Average Earning Assets (ROA)**
**(%)**

No Arrears
Peru
Romania
Nigeria
Philippines
Mexico

1.6
1.4
1.2
1.0
0.8
0.6
0.4
0.2
0.0
-0.2
-0.4
-0.6

FY88 FY89 FY90 FY91 FY92 FY93 FY94 FY95

**Diagram 9:**
**Reserves/Loans Ratio (%)**

No Arrears
Peru
Romania
Nigeria
Philippines
Mexico

16
14
12
10
8
6
4

FY88 FY89 FY90 FY91 FY92 FY93 FY94 FY95

example, in such a way that Bank borrowing costs would rise. There could also be a domino effect where, if one or two major borrowers defaulted, other countries would follow. The conditions that might lead a major borrower to default, such as very high (or very low) petroleum prices for example, are likely to affect other borrowers as well. However, this serves only to strengthen further the principal conclusion: that the Bank's net income is exceedingly vulnerable to a situation of extended arrears by any single major borrower, or a combination of just a few medium-size borrowers.

4.45 Strengthening of the Bank's Financial Situation. When all country-specific measures fail and a country in financial difficulty ceases to make its debt service payments, the Bank must be prepared to absorb this loss. If at some point a decision is made to begin to write off any of these loans, the accumulated loan-loss reserves could be charged first.[19/] The Bank's Special Reserve, of $292.5 million, could also be charged prior to charging net income as this reserve was built up by special loan commissions up to 1964; they were not counted as part of net income at the time, and were set aside for the sole purpose of meeting liabilities of the Bank on its borrowings and guarantees. If the losses were greater, the Bank would then make the charges against, in order: current year net income, general reserves, paid-in capital, and callable capital. The financial ratios of Table 4.6 showed what shares of the portfolio could be absorbed through charges against these categories, and showed that the proportions that can be absorbed now are much less than before. There are essentially only three means, however, to increase the ratios.

4.46 First, loan charges can be raised. This would raise net income which, after a portion has been set aside for IDA, is added to General Reserves.[20/] There are limits, of course, to the extent to which the lending charges should be raised. Furthermore, the present system is such that the long-term decline in the reserves to loans ratio should now stop and begin to rise, and could reach a ratio of about 15% by FY95 if extended arrears or other problems do not become significant. Such a ratio, should it be realized, is currently in fact judged to be excessive in an environment where arrears are not a problem. To handle the risk of arrears, therefore, consideration is now being given to changes in the current loan charges system to deal with the issue of risk

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19/ Standard accounting practices allow Management some flexibility on this. Given the circumstances, Management could decide, for example, to charge first current year net income.

20/ A reduction in the IDA allocation would, of course, raise General Reserves by more. However, IDA is a high priority, and the additional amount that would accrue to reserves if the IDA allocation were reduced is relatively small.

directly. There are basically two options, which are discussed in a recent FPA paper.[21] One would be to maintain the current margins, and then to rebate to the borrowers at some later date the excess accumulation should the risk of arrears not materialize. The second would be to reduce the margins, but institute a contingent charge which would apply at some later date should a significant problem with arrears develop. This contingent charge could be an addition of up to 50 basis points to the regular margin of 50 basis points. However, as the new system could only be applied to new loans, the amount which could be raised by this charge would be small for many years. Furthermore, even with the system fully phased in, the amount which could be collected would still not be large. For example, if the system were now in effect for the entire loan portfolio of $69.4 billion (as of December 31, 1987), the additional 50 basis points would add only $347 million per year. Based on the results of the simulations of the effect on Bank net income of extended arrears (para. 4.43 above), this would cover roughly the effect of Peru going into arrears, or other countries making up only 1-1/2% of the loan portfolio. As an alternative to raising the loan margin by a relatively small amount over several years, one could raise the margin by a higher amount but treat it as a one time charge. However, a reasonable level for such a charge would still only be able to cover problems with perhaps 2% of the portfolio.

4.47 The use of increased loan margins to cover arrears by delinquent debtors operates as a charge on Bank borrowers, in proportion to their borrowings. It could be argued that such delinquencies by a Nicaragua or a Guyana should not be absorbed by the borrowing members who remain current, but rather by the Part I members of the institution. This brings up the second and third alternatives for strengthening the Bank's financial ratios, which are decisions on the size of the General Capital Increase and on the paid-in share of the capital increase. The larger the increase and the larger the paid-in share, the more the ratios will improve and the greater the ability to absorb a shock such as a default.

Conclusions

4.48 This chapter has reviewed Bank policies for managing country credit risk, and the state of that risk to the Bank's balance sheet and income statement. No changes in existing policies are proposed. However, it was noted that several trends indicate that credit risk to the Bank is growing. The sharp depreciation of the dollar since February 1985 has accelerated several of these trends. To manage this risk, the Bank has an array of instruments which, although perhaps individually limited, are mutually supportive. At the country specific level, further Bank lending

21/ "Review of IBRD Loan Charges Structure", FPC/86-2, December 3, 1986, supplemented by annexes distributed on December 17, 1986 to the Financial Policy Committee as FPC/86-6.

is not permitted to the very high risk (IIIc) countries, while for IIIb countries Bank lending is limited to those countries with a viable adjustment program in place. In countries where Bank exposure is considered excessive, an overall strategy to manage that exposure should be developed. This strategy should consider adjustments in the overall level of Bank lending and increased efforts to improve burden sharing with other creditors. In addition, the strategy should consider such factors as the relative shares of fast, medium, and slow disbursing operations in that lending program, the time phasing of the program, and the use of guarantees. Consideration is also now being given to the development of optional new Bank lending terms, where terms liberalization would be coupled with third party bridge financing. Preliminary calculations indicate that use of such a scheme could significantly raise Bank net transfers over what they would otherwise be, and significantly reduce debt service to the Bank, and hence exposure, during a critical period for Bank borrowers.

4.49 Despite such measures, the Bank must ultimately be prepared to absorb defaults on a certain share of its portfolio. As a development institution, the Bank cannot avoid a responsibility to lend in what are inherently high risk situations and it is for this reason that the Bank has been given a conservative financial structure. The various ratios of reserves, equity, and total capital to loans indicate the degree to which defaults can be absorbed. These ratios have all been trending downwards, with the dollar depreciation since February 1985 adding a discrete downward shift. The ratios have now reached levels which current policy indicates should be minima. The current system of loan charges should, however, lead to a reversal of the downward trend of the reserves to loans ratio. The contingent charge mechanism currently being considered could further increase the capacity to handle risk. However, the present system of risk absorption, even if supplemented by such a contingent charge mechanism, could not absorb extended arrears on loans accounting for more than some 3 or 4% of the portfolio. Beyond this, the issue is the adequacy of the Bank's capital. Discussion on the size, timing, and paid-in share of the General Capital Increase should therefore explicitly take into account the trends in the country credit risk factors reviewed above.

Record: April 3, 1987

# FINANCIAL POLICY COMMITTEE

## MINUTES OF MEETING OF THURSDAY, MARCH 19, 1987

Members Present: Messrs. Qureshi (Chairman), Asser, Gue, Hasan, Inakage, Paijmans, Rotberg and Wood.

Also Present: Ms. Hadler and Messrs. Asanuma, Baneth, Baudon, Jansen, Lysy, McPheeters, Mistry and Talvadkar.

### I. 1987 Review of Country Creditworthiness and Bank Loan Portfolio Issues, FPC/87-4.

1. The Chairman opened the meeting by asking for a summary of the OVP discussions on the same subject held on March 18, so as to brief the FPC members on the essential reactions of the Operations Complex to the report. A member then reported that the key views expressed during the OVP meeting in reaction to the deteriorating trends pointed out in the report, were:

(a) That the Bank should not consider retrenchment in lending as a viable option;

(b) That the trade-off between the financial strengthening of the institution and the "optimal" use of Bank funds would be difficult;

(c) That the increase in Bank exposure in selected countries should not be viewed in a static sense; a number of countries especially in Latin America were making good adjustment efforts and that the high exposure had been accompanied by increased Bank involvement in policy dialogue on macro and sector management issues. In specific cases, there had been deliberate decisions to increase Bank exposure beyond "norms";

(d) That while increased burden-sharing with other sources of funding could be explored, there were real constraints imposed by our limited leverage with commercial banks and inability to use guarantees; and

(e) The option of using quick disbursing assistance to manage debt service profile is already being used to the limit in many cases; further increases will lead to severe volatility in future disbursements.

The same member noted that the OVP meeting had concluded that the country ratings in the report were generally appropriate. OPC members had also expressed an overwhelming concern about the fast deteriorating global environment and the increasing risk which the institution confronted.

2. At the Chairman's request, another member summarized the purpose and broad conclusions of the paper. He first stated that the report had a "stock-taking" objective for the institution as a whole. From that point of view, the central message is very sobering: the Bank has now a high risk portfolio and is becoming increasingly vulnerable to protracted arrears in the servicing of its loans. He illustrated this by mentioning that the ratio of Bank debt service to exports has increased three or fourfold in many countries over the recent past. He then said that the second objective of the report was to point out that the Bank does have some capacity to manage its rising exposure. This could in particular be achieved through: (a) increases in the share of fast-disbursing operations in the lending program whenever possible and desirable; (b) a liberalization of repayment terms; and (c) changes in the loan charge structure to better withstand increased risk of non-accruals from small borrowers. However, the same member noted that the first action can reduce our exposure risk in the short-run only (by temporarily raising the level of net transfers), but would then lead to higher exposure levels in the future. In that sense, restored growth and improved fiscal/current account balances in borrowing countries will be crucial to avoid unmanageable Bank risk in the medium-term. He then concluded by saying that despite the "exposure management" tools it can develop, the Bank is in an increasingly difficult situation. The need for a General Capital Increase thus becomes paramount to avoid severe impairment of the Bank's capacity to absorb potential shocks in the future.

3. Before opening the discussions, the Chairman stated that in his opinion, the paper served several essential purposes in the present difficult environment: first, it triggered a Bank-wide debate and highlighted the riskiness of the situation; second, it put things in perspective by demonstrating that, contrary to what a purely static analysis would indicate, an increase in Bank's exposure in the short-run could ultimately reduce the overall risk to the institution if adjustment programs in borrowing countries are carefully designed and implemented; third, it showed that the problem of burden-sharing was real and; fourth, it provided additional evidence that a GCI will be a necessary part of the answer, even though it would not reduce the risk factor itself, but rather allow the Bank to withstand it better.

4. The Committee then focused its discussion on the following points:

(a) The lack of a fully satisfactory solution in the present world economic environment to deal with the deteriorating situation of the portfolio and the extent to which a GCI would be instrumental in giving the Bank additional strength and leverage to adjust to the increased risk factor; and

(b) The specific proposals made in the report with respect to the management of Bank exposure (country-specific limitations in lending and total exposure; the use of policy-based, fast-disbursing operations to manage the debt service profile; optional new Bank lending terms; and improved burden-sharing with other creditors).

5. The need for a broader response to an increasing risk and the potential contribution of a GCI. One member stressed that the main conclusion he drew from the report was the absence of a satisfactory solution at hand to deal with the increasingly difficult situation faced by the Bank. He felt that a GCI, though desirable, would not by itself be an adequate answer, and that a conflict situation is gradually arising between the Bank's need to protect its financial situation and the need to meet its basic mandate by assisting its member countries. Another member supported this by adding that the world economic environment was difficult and could deteriorate further, and that retrenchment by the Bank at this point could increase the likelihood of defaults rather than reduce it; he agreed that a GCI would not be sufficient, although it would definitely have the two major advantages of increasing financial flows to developing countries and allowing the adjustment process to continue. The same member pointed out that in his view the real issue was the debt problem, and how we could tackle it. He felt that the Bank should fully acknowledge the variability of situations among debtor countries and not put excessive hope in a quick resumption of voluntary lending by the commercial banks. The Chairman then stated that a GCI was absolutely essential and would greatly contribute to restoring the Bank's ability to cope with the deteriorating situation. It would bring back the Bank's financial ratios to more satisfactory levels and allow the institution to continue to meet its normal obligations by offsetting the constraints that sharp exchange rate movements will soon impose on our aggregate borrowing and lending capacity.

6. A member then said the situation had become so serious that the Bank should refuse to participate in any new concerted lending package unless it receives assurances by the major shareholders that a GCI will be implemented soon. In his opinion, the combination of slow growth prospects of the world economy with deteriorating Bank financial ratios and "headroom" was unprecedented and justified such a strong stance regarding a GCI. The Chairman replied that these were certainly valid causes for concern but that he did not see a drastic deterioration in either the situation of borrowing countries or the Bank portfolio itself over the last year. He noted that none of the underlying trends were new, but rather that we were one year farther along the path that we have been on for some time. He reiterated that the recent deterioration in financial ratios stemmed almost exclusively from exchange rate movements, i.e., the decline of the US dollar vis-a-vis other major currencies. A member emphasized, however, that what was new was the convergence at one time of several key adverse trends.

7. Several members expressed the view that the past year had been the fifth consecutive one of declining creditworthiness for our borrowers, despite the adjustment measures undertaken by a number of them. The cumulative effect of this steady degradation, which is likely to continue given the expected evolution of the terms of trade during the coming year, will ultimately take its toll if nothing is done to alleviate the excessive burden that debt service puts on several countries. They thought that the Bank should: (a) increase its reserves as quickly as possible; and (b) seriously consider a broad new approach to the global

problem of LDC debt and debt service. The Chairman also noted that the issue of net transfers is indeed a real one, and that the Bank should be very concerned about it. While the maintenance of positive net transfers over time was neither sustainable nor a realistic position, it would be equally wrong to ignore this aspect at a time when members countries' external positions were so heavily burdened.

8. Specific proposals with respect to management of Bank exposure. The discussion then turned to the specific recommendations made in the report to improve the management of Bank exposure. A broad consensus emerged in the Committee on the following points:

(a) The Bank should maintain a degree of flexibility in managing exposure limits and not be excessively bound by formal ratios; this would be justified in particular if a country is pursuing a high quality adjustment program. Retrenchment in lending, especially to the highly indebted countries, could prove to be a more risky proposition than continued support through increased capital flows, provided sound economic policies are being implemented; the risks associated with this proposition were fully acknowledged by Committee members, who agreed, nevertheless, that the Bank should preserve the option to pull out or retrench in certain specific cases;

(b) The liberalization of lending terms is a sound proposition which could benefit both the borrowers and the Bank, but further detailed work needs to be done before a fully operational proposal can be presented. In addition, the Bank should be sensitive to the timing of this proposal in relation to the discussions on the GCI; premature adoption of a liberalization policy could undermine the GCI process itself. A member pointed out that this liberalization would not have much effect in the short run; it was noted, however, that even modest positive effects are worth considering, particularly during the interim period preceding the implementation of the GCI; and

(c) Portfolio concentration in high risk countries could be alleviated in part, should the Bank decide to offer more attractive terms or better tailored products to its most creditworthy borrowers. This would increase their interest in borrowing from the Bank.

9. With respect to the Bank's vulnerability to arrears and the possible measures the Bank could take to avoid a significant deterioration in net income, the Chairman asked that reference to a contingent charge be dropped for the time being, pending conclusion of the on-going discussions on the structure of loan charges.

10. In conclusion, the Chairman stated that the discussion had highlighted the urgency of a GCI and increased the Bank-wide awareness of risks to which the Bank is increasingly exposed. He hoped that this awareness would be reflected in our policies and approaches: (a) on the operational side, our criteria for lending should remain as strict as possible since the quality of the programs we support is the key to restoring a viable situation; and (b) on the financial side, the Bank should be more sensitive than ever to financial policies and ratios and more broadly to its image in the financial markets; it should also be adequately prepared to deal with crisis situations should they arise.

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

# OFFICE MEMORANDUM

DATE July 30, 1987

TO The Policy Committee
(through: W. David Hopper, SVP/PPR) W.D.H.

FROM Alexander Shakow, Director, SPR

EXTENSION 78812

SUBJECT Draft President's Report to the Development Committee - Policy Committee Meeting, August 3, 1987

Attached is a copy of the agenda for the September 28 Development Committee meeting and the draft President's Report. The Board is scheduled to discuss the report (as a Committee of the Whole) on September 1 and we would like to send it to Executive Directors by August 7 if possible.

Two background reports are also being prepared, one by Finance on GCI issues (based on the July 30 C.O.W. discussion) and the other on low-income countries. The latter is a joint effort between Operations and the IMF; it should be completed next week.

The President's Report must cover all the agenda topics, and unfortunately the agenda has grown rather than shrunk. The main emphasis in the text is on explaining and gaining increased support for: 1) the Africa initiative (Section II) and; 2) the GCI (Section IV) although the latter is rather circumspect on the size question, which limits the force of what we can say. We have attempted in the review of middle-income countries (Section III) to convey the current status of Bank thinking in both the analysis and the prescriptions for action, but as this is a fast-moving target we may not yet have the balance correct and would appreciate Policy Committee guidance. (This is not unrelated, of course, to the August 5 Policy Committee discussion of the debt management paper and the annual meeting speech outline, both of which confront the same issue.)

Other matters are not as critical, but they do take up space. No new ground is being broken on industrial policies of developed countries (Section VII) and on options for commodities (VIIIa), and the transfer of resources message (Section V) remains constant, albeit very important.

We appreciate the help we have received from various parts of Operations, Finance, PPR, Legal and IFC in drafting this text. We are also consulting with the IMF on relevant parts of the text.

We shall tighten the text as much as possible in the final draft.

Attachments

P-1866

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# OFFICE MEMORANDUM

DATE July 28, 1987

TO Mr. Barber B. Conable

FROM W. David Hopper, SVP/PPR W.D.H.

EXTENSION 75678

SUBJECT Follow-up to the Poverty Task Force

On December 17, 1986, you appointed a Poverty Task Force to consider the Bank's approaches to the alleviation of poverty and to recommend new initiatives. On April 7, 1987, Mr. Shahid Husain, Chairman of the Task Force, sent you a preliminary report. Due to the numerous changes of responsibility associated with reorganization, this report has not formally been acted upon. Ms. Haug has asked for my recommendations on next steps.

Your annual meeting speech last year, the formation of this Task Force and other public statements, have generated high expectations within and outside the Bank that the Bank will be giving higher priority to poverty issues. This was evident in April's Development Committee meeting in which your oral statement stressed the vital interest of the Bank in this subject and indicated that additional efforts might be proposed in two areas based on the Task Force's initial work — i.e., increased funding of NGOs and expanded lending to influence policies in social sectors. Parliamentarians from the U.S. and Europe have recently begun sending strong letters of encouragement for a strengthened Bank focus on poverty, and on July 23, Deputy Assistant Secretary Conrow testified before the House Select Committee on Hunger where he spoke positively about your personal commitment in this area and of suggestions likely to emanate from the Task Force. In addition to the importance of our actual work in this area, there is a strong political need to provide evidence of the Bank's serious attention to poverty questions. Your annual meeting speech should leave no doubt about the importance of this topic to the Bank.

In addition to the brief preliminary report sent to you in April, the Task Force and its working group prepared a significant amount of additional data and analysis which provides the basis for a very substantive report when completed. This report should provide an

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P-1866

excellent basis for guiding future Bank poverty work as well as a useful document for Board and external audiences.

The establishment of PPR has created a natural focal point in the Bank to follow-up on the initiatives suggested by the Task Force - including the two mentioned to the Development Committee in April - and other steps that are needed to assure that poverty alleviation is given increased attention in the Bank's research, policy work and operations.

In light of the delays brought on by reorganization, the establishment of PPR, and changed responsibilities of senior staff, it would make most sense to fold the Task Force work into PPR's regular responsibilities. Thus, I suggest that you thank Mr. Husain and the Task Force members for their excellent work and indicate that you are now asking PPR to take the lead in completing their report. This would be done in close consultation with Messrs. Dubey (Operations) and Kavalsky (Finance), both of whom provided extensive support for the Task Force, as well as with Mr. Husain and other Task Force members, before being presented to the Policy Committee for review. The report should be produced as soon as possible so as to be of maximum use internally and to support GCI discussions. You might also wish to indicate to the Board that the report is delayed due to the reorganization but that it would be sent to the Board before the end of the year.

A draft note to Mr. Husain and his Task Force is included for your consideration, as well as a draft comment to the Board.

Enclosure

THE WORLD BANK / INTERNATIONAL FINANCE CORPORATION

# OFFICE MEMORANDUM

DATE: July 28, 1987

TO: Mr. S. Shahid Husain, LACVP

FROM: Barber B. Conable, President

EXTENSION: 72201

SUBJECT: Preliminary Report of the Poverty Task Force

On April 7 you sent me a letter setting forth the broad conclusions and recommendations of the Poverty Task Force. Regrettably, this hectic reorganization period and the associated changes in responsibilities for key staff resulted in your preliminary report receiving far less prompt attention than both the report and the subject deserves.

I want to take this occasion to thank you and the members of the Task Force for your important contributions to improving the Bank's poverty work. Your report identified "six steps that are vital to the success of reintegrating poverty concerns back into the center of [the Bank's] operations", and I believe we can all concur on the importance of these actions. I believe the Task Force's work has already resulted - particularly through the extensive contact the Task Force and its working group had with staff - in considerably more attention to poverty issues. This is especially true in Bank/NGO relations and in the stimulus for increased attention to protecting the poor during the adjustment process -- including lending for policy reforms in the social sectors.

As your preliminary report clearly indicates, there is much more to be done. I am committed to assuring an active Bank leadership in this area. The establishment of a PPR Senior Vice Presidency provides a natural focal point in the Bank for this work. I understand that much substantive work has been done by your Working Group on a longer report which could serve PPR and the rest of us well as a guide for further research, analysis and action. Given the changes brought about through reorganization, I am asking PPR to undertake the completion of the report begun by the Task Force under your leadership. This PPR will do in close consultation with you and members of

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the Task Force as well as with Messrs. Dubey and Kavalsky, both of whom, I understand, were deeply involved in preparation of the Task Force materials.

Thus, let me take this opportunity to thank you again for your strong leadership and initiative in addressing poverty alleviation issues; I know this will continue even as we fold the work of the Task Force into the mainstream of the Bank's work, for we will need in every part of the Bank strong commitment to achieving the important goals set out in your letter of April 7. You and the members of the Task Force have my gratitude and appreciation for a job well done.

cc: Members of the Poverty Task Force
Messrs. Baneth, Burki, Dubey, Isenman, Pfefferman, Kavalsky

Proposed Oral Statement to the Board on the

Poverty Task Force

As you know, last December I established a Poverty Task Force under the Chairmanship of Mr. Shahid Husain. In April Mr. Husain submitted a preliminary report, and in my oral comments to the Development Committee I touched on suggestions emanating from the Task Force's work. Mr. Husain and his colleagues have done a fine job in stimulating important initiatives and ideas which need to be followed up. The reorganization has, of course, resulted in many changes in structure and personnel which have regrettable slowed down our attention to the Task Force's work.

Given the establishment of PPR we now have a focal point in the Bank to provide leadership on research, analysis and actions in support of our poverty alleviation objectives. Accordingly, I have asked PPR to take the lead in completing the full report begun by the Task Force - working in close consultation with Operations and Finance - with the objective of having a report for you by the end of the year.

THE WORLD BANK INTERNATIONAL FINANCE CORPORATION

# OFFICE MEMORANDUM

DATE: July 30, 1987

TO: Members of the Policy Committee

FROM: W. A. Wapenhans, SVPAD

EXT: 75656

SUBJECT: Round 2: Managing the Selection Process and the Supplementary Budget

1. Round 2 of the reorganisation selection process is to commence on August 3, 1987. This is when final reorganization selections and separations of staff will take place, as managers place unselected staff currently on the roster that emerged from Round 1 into vacant positions; and as staff who have not found positions are made eligible to leave the Bank under Package A or B. Because the selection process has been conceived as a decentralized process, and because there are both budget and numbers limitations on total separations, there is no guarantee that the number of selections made by the "market" will be such as to reduce the numbers to be separated to 390 at a cost of $92.7 million (the limits set by the Board). This may lead to an awkward outcome at end of Round 2 in which a residual number of staff have not been placed and for which there are no budget resources left for separation.

Dimensions of the Problem

2. At the start of Round 2 there will be some 698 staff on the unselected roster, against 600 vacancies. Based on the unit costs used at the time the Board paper was written, the budget of $92.7 million is sufficient to handle 100 Package A and 290 Package B separations. Since the Board has expressed sensitivity to Management about the prospect of separations numbering more than 390; even if unit costs were less than anticipated we could not release many more than, say, 400 people.

3. This means that, if a clean outcome of Round 2 is to be achieved the selection process would have to place at least 308 people into the 600 vacancies (or a greater number, if the unit separation costs turn out to be higher than anticipated). Subtracting, say, 80 support level staff who could be carried on the TAP, this translates into a 46% placement rate for higher level staff.

4. Based on experience so far, the unit costs of the compensation packages is higher than anticipated, by some 15%. It is too early to know whether this experience will be generalized across the entire population of those who will leave. If, in fact, it does so, then the capacity of the Supplementary Budget to handle separations will be reduced by some 60 to 80 people. This would, therefore, mean that one would need to place up to 388 people during Round 2 - a placement rate of well over 50%

Management Options

5. In seeking to avoid a budget overrun and/or the emergence of an indigestible "residual", Management can operate on one or both sides of the selections/separations equation. It can make every effort to ensure that the Round 2 process maximizes the selection of staff with contributive skills so that the number of separations is not allowed to exceed, say 400 people. It can also reduce the unit cost of separations somewhat by influencing the ratio of Packages A to Packages B.

6. Senior managers have a key role to play by stressing to their selecting managers the nature of the institutional responsibility which they bear in making their selection recommendations.

Managing the Round 2 Selection Process

7. It is intended that Round 2 will be as much as possible a "free market" process, with unselected staff applying for jobs against a roster of vacant positions; and selecting managers making offers to candidates appearing on a roster of staff available after Round 1. But in order to ensure efficient market clearing, it is also intended to set up a central skills search and clearing capability, to monitor the process, to ease the information flow through the market, and to maintain a pressure on managers to be conscious of their institutional responsibilities in making their selection decisions. We believe that the newly formed MRG - backed up by task forces in each SVP/VP unit - is the mechanism that would be appropriate to guide the market towards the desired institutional result. Such a mechanism is also needed to ensure scrupulous observance of the Staff Rule and to "smoke out" those experienced and valuable staff who may (with or without the collusion of managers) be seeking to avoid selection in order to secure a package.

8. If this principle is agreed, the management of Round 2 could be structured around the following key elements:

(a) Preparation: Two rosters have been prepared: one of all unselected staff, which will be sent to all managers; a second of all vacancies, which will be sent to all unselected staff. Also, an Instruction Memorandum is being drawn up for all selecting managers, and an Advisory Note for all staff has been written, explaining the purpose and procedures to be followed during Round 2. Both would be sent out before the opening of Round 2.

(b) Opening: Round 2 will open on August 3, and the search for jobs/preparation of offers will begin. To give a fair time for all candidates to search and present themselves for available jobs, no offers would be made to candidates until August 10. A large share of Round 2 jobs would probably be assigned during this initial period.

(c) First Review: On August 15-17, there would be a stocktaking of the outcome of the opening phase of Round 2, with the following objectives: to make the first allocation of Package A; to ascertain the size of the remaining roster of unselected staff; to make preliminary determinations for Package B separations; to obtain a fix on the prospective claim on the separations budget; to ascertain whether a "residual" is likely to emerge, and its size; and to develop guidelines for SVP/VP units, including "fill ratio" targets to be reached by the end of Round 2.

(d) Second Phase: (August 17-September 10) During this second phase, the process of selection would continue but would be assisted by Personnel under MRG guidance. This would involve compiling short lists of candidates for managers, and assisting them in their skills search. From this phase until closure, selection decisions would be validated by MRG with Personnel and PBD support in order to help meet institutional objectives and maintain the separation program within the budget limits.

(e) Second Review: (September 10-11) This would be a second major stocktaking and allocation of Packages (A and B). It would be the critical point of judgement as to whether a contingency plan would need to be involved to handle any residual.

(f) Closure: (September 30) This will close Round 2; all packages and training commitments would have been awarded, all placements made. If successful, there would be no unplaced staff "residual".

(1) How maintain equity with other staff who, at the end of the process, would, as a result of non-selection, receive B.

(2) How wd. managers know whether someone selected have applied for Package A? Aren't they assuming those positions are filled?



Reducing Unit Separation Costs

9. Since budget constraints have now become a factor in the allocation of the compensation packages, it is evident that the Bank has an interest in maximizing - from among all those without jobs - the number of separations under Package A. Accordingly, at the time of the First Review (August 15-17) all applicants for Package A not yet selected (and unlikely to be) would be released under Package A. (1) For all those applying for Package A, but who have been selected into a job, they would be granted Package A (as the selection process proceeds) only if they can be replaced by someone who would otherwise have to be awarded a Package B to leave. (2) In this way we would economize the number of separations under Package B, maximize the number of those under Package A, thus minimizing, to a degree, the unit cost of separations.

Contingency Planning

10. Despite the structured format for the management of Round 2 - involving a combination of market processes, senior managerial exhortation, phased assessment and control points, and an MRG facilitating role - it would be foolhardy not also to consider what actions might be necessary if the desired zero-residual result is still not achieved. At that point, the options open to Management would be:

(a) A return to the Board for further funds to finance the separation of these staff members.

(b) Forced placement of remaining unselected (and unseparated staff).

(c) To extend Round 2, in the hope of securing further selections.

(d) The establishment of a Temporary Assignment Program, possibly in combination with a managed secondment program to other agencies.

good idea; but not clear how (d) + (e) differ — see next page.

(e) An expanded training/retraining program to accommodate all remaining staff.

11. It is our understanding that the Committee has already decided against (a) and (b). Option (c) would be unpalatable too since it would extend the disruption associated with the reorganization. Option (d) would be highly disruptive and affect managerial morale since it would require the commandeering of vacancies to fund the program. Besides, experience with centrally managed programs of this kind is not encouraging. Option (e) emerges as the only practical option although it implies an element of "leverage" on managers if not outright forced placement. Thus, this option should be resorted to as a last resort and, in the meantime, everything should be done to ensure that managers cooperate and "internalize" all major institutional objectives associated with this critical phase of reorganization implementation.

12. In light with the above, we seek an agreement from the Policy Committee:

(a) to pursue Round 2 in the fashion described above, with an agreed undertaking to brief subordinate managers on their institutional responsibilities, and to institute "fill ratio" targets by SVP/VP units for Round 2;

(b) to institute an MRG role in the selection process, in the way described to oversee Round 2 implementation; and

(c) to initiate preparation of a contingency "training-cum-placement" plan.

cc: Mrs, Marianne Haug