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Socialist Economies Reform

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Factors Affecting Private Financial Flows to Eastern Europe, 1989-91

Mohua Mukherjee

Data and factors that influence market perceptions of the relative creditworthiness of the different countries participating in Eastern Europe's economic transformation.

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Despite a common heritage of institutions and arrangements for economic planning and trade clearing, and their almost simultaneous adoption of reform, the countries participating in Eastern Europe's economic transformation differ greatly in economic performance and market expectations of performance.

Mukherjee examines those differences as the region's economic transformation nears its third anniversary, focusing on the underlying factors that drive private capital flows — from both commercial lenders and foreign investors.

Improved creditworthiness — or the ability to attract voluntary private-sector finance for successively longer periods, with fewer guarantees required — is a major signal that the economic reforms are beginning to take hold.

Mukherjee examines the different stages on the road to creditworthiness at which she finds the Eastern European countries. Hungary and Czechoslovakia (CSFR) are the only countries that can issue medium- to long-term sovereign bonds held by private investors (the ultimate test of creditworthiness, by some standards). In Hungary, maturities on the most recently issued deutschemark bonds now extend as long as seven years; private placements of yen are even more favorable — extending to ten years.

Mukherjee identifies and compares cross-country information about some of the factors that influence differing market perceptions of Bulgaria, Czechoslovakia, Hungary, Poland, and Romania. Among factors discussed:

- The importance of the former Soviet umbrella.

- Indicators of relative indebtedness.

- The flow of funds to the region, by source, from 1989 on.

- The maturity of commercial debt and especially the magnitude of short-term debt.

- The identity of "other private creditors," and factors that affect the amount of project finance and foreign direct investment available.

- The setup of emerging financial institutions.

- Long-term commercial flows — especially bond finance (access to the Eurobond market for medium- and long-term funds).

The region is not well known to lenders that might be able to meet its many emerging needs for financing. And the few statistics available may be doubtful or misleading in the context of a market economy. Mukherjee bases her observations largely on interviews with people in commercial banks and investors active in Central and Eastern Europe. All data have been provided by those sources and by country reports issued by the Institute of International Finance. The latter is a major source of figures used by private lenders when they assess a borrower's prospects.

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Background

This exercise was undertaken in order to examine selected cross-country aspects of the unprecedented regional economic transformation taking place in eastern Europe. Despite the common heritage of institutions, economic planning and trade clearing arrangements, and the almost simultaneous adoption of reforms, clear differences in performance and expectations are evident across countries as the regional transformation process passes its second anniversary.

A large set of financing needs has emerged in a region which is not well known to its potential lenders, and even in the few cases where detailed statistics are available, they may be doubtful or misleading in a market context. In this situation, it may be instructive to explore the *underlying factors driving private capital flows*, both from commercial lenders and foreign investors. Improved creditworthiness, or the ability to attract voluntary private sector finance for successively longer periods and requiring fewer guarantees, is a major signal that the economic reforms are beginning to take hold, and are recognized as such by the market. Countries in the region are at different points along the road to creditworthiness, and the paper attempts to look at this more closely. Certainly Hungary and CSFR are the only countries with the ability to issue medium to long-term sovereign bonds held by private investors (the ultimate test of creditworthiness, by some standards). In the case of Hungary, the maturities of the most recently issued DM bonds are now as long as seven years, and Yen private placements are even more favorable, extending up to ten years.

Part I of this paper aims at identifying and summarizing some of the factors which influence the market's differing perceptions of Czechoslovakia, Romania, Hungary, Bulgaria and Poland. Information on market perceptions was obtained as a result of numerous interviews[1] with commercial banks and a few investors active in central and eastern Europe (CEE).[2]

The first section summarizes and compiles cross-country findings in the following areas:

A. The importance of the Soviet umbrella;

B. Indicators of relative indebtedness;

C. A summary of funds flowing to the region, by source, from 1989 onwards;

D. A discussion of the maturity profile of **commercial debt**, in particular the magnitude of **short term debt**;

E. **Project finance and direct foreign investment**: who are "other private creditors"? What factors influence the amount of project finance available?

F. The institutional setup of the emerging financial sector; and

G. Long term commercial flows, in particular **bond finance**: access to the Eurobond market for medium term and long term funds.

Part II of the paper contains further details for individual countries. All data have been provided by commercial banks or country reports issued by the Institute of International Finance (IIF), since these figures are used by private lenders when assessing the prospects of a particular borrower.

[1]. Interviews were conducted in October 1991.

[2]. In keeping with the original intention of basing this paper on market perceptions of the region, every attempt has been made to avoid using World Bank or other multilateral sources for data presented here.

Part I: Introduction—Developments from 1989 to 1990

The table below highlights some of the issues this paper is seeking to follow up on. Clearly 1990 was the year of greatest uncertainty, with *negative transfers* (or at best zero, in the case of Poland) *to commercial banks from all countries in the region.* The picture has changed in 1991, as shown in subsequent tables in this paper.

It is widely accepted that few if any sovereign debtors in the region are likely to have access to general purpose commercial bank funding in the next five years. At the same time, the table below supports the anecdotal evidence that there are some private capital inflows, especially for Hungary, Czechoslovakia and Poland. The paper will examine the size and creditor composition of funds flowing to the region since 1989. In particular, it will examine the types of financial instruments which are being used to channel *private sector funds*, such as short term trade lines, project financing, equity investments in joint ventures, syndicated loans, offsets and countertrade etc. The implications for relative seniority of post-1989 *commercial inflows* will be of great interest in this context, and efforts have been made to learn about collateral or guarantees extended to investors in financing projects.

The term "financial market access" is extended in this paper to include the ability of the *enterprise sector* to raise funds in the capital markets e.g suppliers' credits and direct foreign investment (DFI). This is of course also related to the sovereign government's direct market access to borrowing for balance of payments support. Earlier findings have shown that the sovereign government borrowing rate usually sets a benchmark, and that the cost of funds for enterprises is heavily influenced by sovereign risk.[3] Private sector flows will set the tone for the relative ease of future access to all international capital flows.

A. The Soviet Umbrella, or a Different Set of Rules for the Region in the 1980s?

Under the old CMEA arrangements, it was a common assumption among western bankers that the USSR would not permit its allies to default on hard-currency obligations, and that in effect loans to the region were implicitly backed by Soviet gold reserves in a worst-case scenario. This, together with a solid track record of prompt and timely debt servicing, explains why the region was still able to attract hard currency on very favorable terms throughout the 1980s when banks were already facing the reality of insolvent debtors with similar debt ratios elsewhere in the world.

Both Hungary and Poland had debt/GDP ratios higher than Brazil's, for example. In fact, Hungary was quite comparable to Mexico and Argentina in terms of debt/

Table 1: **Private Commercial Finance and Relative Indebtedness at the Turning Point in CEE (in US$ million)**

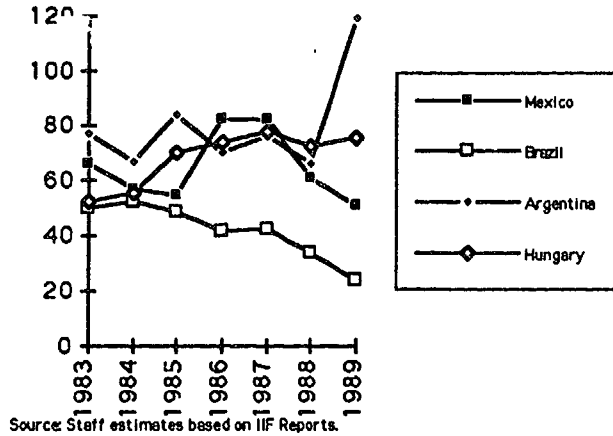
	Bulgaria		Czechoslovakia		Hungary		Poland		Romania	
	1989	1990	1989	1990	1989	1990	1989	1990	1989	1990
Commercial Banks, net credit flows	1,114	203	783	-271	529	-1,670	-388	0	-281	-6
Commercial Banks, interest arrears outst.	0	294	0	0	0	0	145	796	0	0
Other private creditors, net credit flows	675	-140	-189	221	818	677	-287	103	-47	-52
Equity Investment, net Flows	0	5	26	50	180	337	15	10	0	0
External Debt to commercial Banks	7,256	8,223	5,648	5,349	13,269	12,642	8,580	10,627	248	252
MLT External Debt to commercial Banks	4,924	5 ,057	2,795	3,120	10,574	10,981	7,360	8,386	1	0
Total External Debt	10,224	11,030	8,183	8,085	20,537	21,481	41,387	49,019	582	518
DOD/Total Exports	252.7	329.4	112.4	102	241.4	236.9	474.4	383.8	8.7	12.8
Percent of Total External Debt in US$	52.3	52.3	30.6	26.8	23.8	22.3	31.7	37.2	69.2	60.3

Source: Staff estimates based on Country Reports of the Institute of International Finance (IIF) dated November 91 through January 1992

[3]. Successive bond issues by Mexican public enterprises in 1990 were reportedly carried out as part of a strategy to buildon a consistently solid track record for bond debt payments and to demonstrate the increasingly improved terms for borrowers—the yields fell from 17% in June 1989 to 11% in September 1990. Foreign borrowing authorities in the Mexican government reportedly consider these as benchmark rates which are intended to support the Mexican private sector's reentry into the international capital markets.

GDP, and yet continued to have uninterrupted access to commercial lending throughout the 1980s.

Figure 1:Debt to GDP Ratio

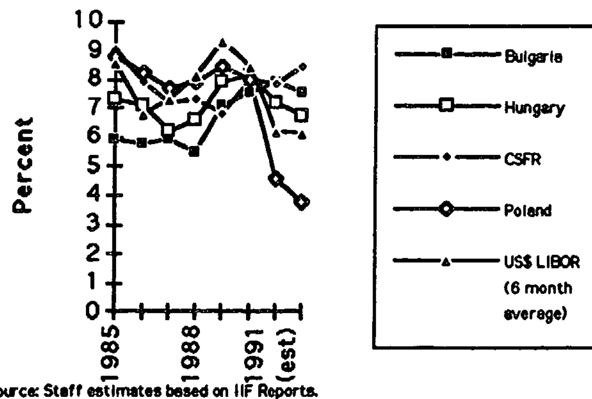


Source: Staff estimates based on IIF Reports.

Detailed information on actual interest rates paid on different types of loans throughout the 1980s is very hard to obtain. Both commercial banks and country authorities acknowledge that spreads for CEE sovereign debtors were often negative for trade lines and general purpose loans, reaching over 100 basis points below LIBOR in many cases. The following chart provides a rough indication of the *favorable interest rates that were enjoyed under the Soviet umbrella, in spite of the high debt ratios.* It traces the gross interest payments in a given period as a percentage of the average total external debt, relative to the average six-month dollar LIBOR.

In 1988 and 1989, all countries in the region paid average interest rates below LIBOR (Bulgaria paid the lowest). This trend reversed in 1990. Poland is the only country to register actual rates below LIBOR in 1991 and 1992, but this is due to non-payment of obligations.

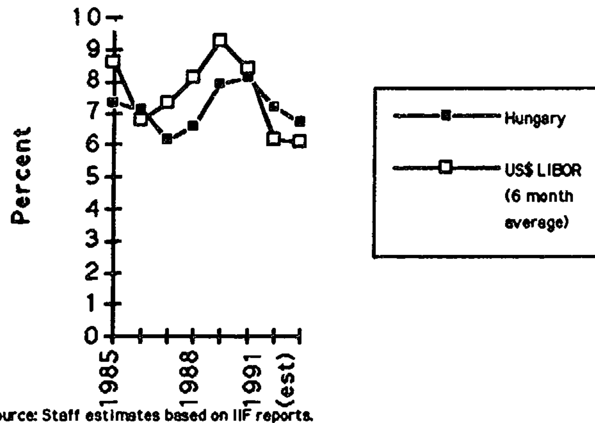
Figure 2: Average Interest Rate on Commercial Debt



Source: Staff estimates based on IIF Reports.

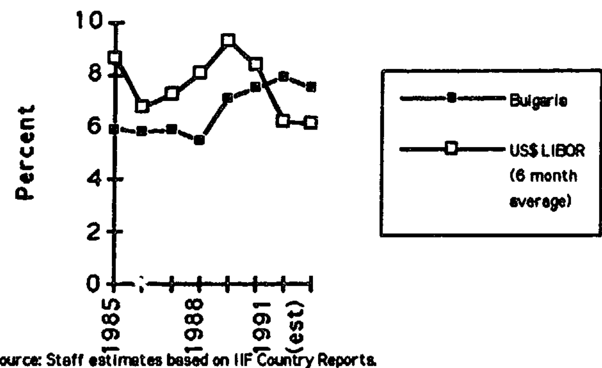
The following charts (Figs. 3 and 4) for Hungary and Bulgaria have been included to emphasize the point. Hungary has been the region's largest debtor to commercial banks, but mainly due to its good debt servicing record, has been able to access large volumes of funds at below LIBOR in the second half of the 1980s. Bulgaria, which was perceived by bankers to be most closely associated with the ex-USSR and therefore the main beneficiary of the "umbrella", enjoyed the largest negative spreads relative to US$LIBOR until 1989. The contrast in the relative fortunes of the two after 1989 is clearly seen in the figures. While LIBOR is declining from 1989-1992, the "average rate" for Bulgaria is on an upward trend. For Bulgaria, though, the information from 1990 onwards needs to be interpreted with caution. The below LIBOR reading for 1990 arises from non-payment of interest for 6 months of that year. After 1990, it has been calculated on the basis of unpaid obligations. In contrast to Hungary, *Bulgaria does not have access to funds* at the rates indicated for 1991 and 1992 in Figure 5. For Hungary, rates relative to LIBOR are declining after 1990, i.e. following the same pattern as the underlying cost of funds.

Figure 3: Hungary
Average Interest rate on external debt



Source: Staff estimates based on IIF reports.

Figure 4: Bulgaria
Average Interest rate on external debt



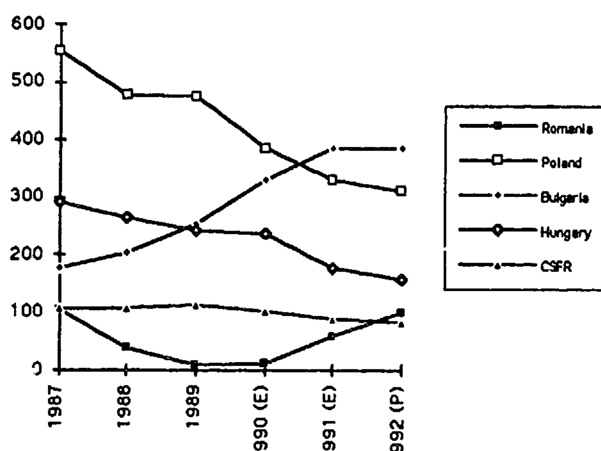
Source: Staff estimates based on IIF Country Reports.

B. Indicators of Relative Indebtedness in the Region

The following charts illustrate relative levels of indebtedness in the region, before and after the disappearance of the Soviet umbrella in 1990. The ratio of debt service to exports in Figure 6 has been chosen to shed more light on the information presented in Figure 5, to illustrate sustainability in addition to indebtedness.

Figure 5 shows that Poland's total debt/exports ratio was almost double that of Hungary in 1987. This ratio has

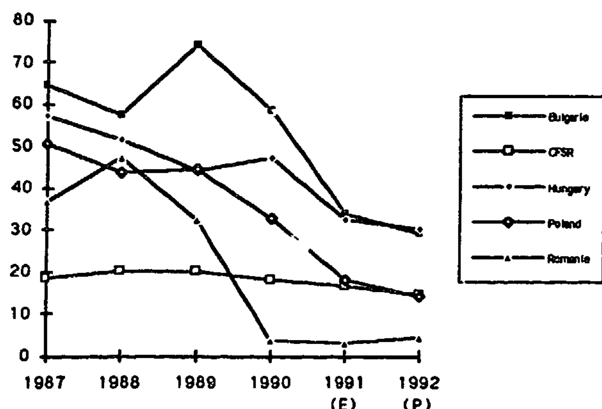
Figure 5: Ratio of Total Debt to Total Exports*



* Total Exports include exports of goods, services, and interest income receipts.
Source: Staff estimates based on IIF Reports.

been declining for Poland and Hungary, remaining relatively constant for CSFR and sharply increasing for Bulgaria and Romania. The policy change adopted by Romania with regard to external debt after 1990 is particularly evident in Figure 5. The debt reduction granted to Poland in 1990 by the Paris Club reduced the ratio for Poland by about 90 percentage points compared to the previous year.

Figure 6: Ratio of Debt Service to Total Exports *



* Total exports include export of goods, services, and interest income receipts.
Source: Staff estimates based on IIF Country Reports.

Figure 6 clearly shows the unsustainability of Bulgaria's debt situation in 1989—the country's debt service obligations, which were met fully and on time, consumed 74.4 percent of total export earnings. For Hungary, the debt service to exports ratio increased marginally between 1989 and 1990 (from 44 to 47 percent) and has dropped sharply to around 30 percent since then. The debt reduction agreement together with non-payment of commercial obligations has lowered the ratio for Poland from 50 to 20 percent between 1989 and 1991. Romania's sharp decline in debt service ratio appears to follow a pattern similar to Bulgaria's, peaking a year earlier. (The background in each case is of course very different). The ratio for Romania now appears to be holding constant at about 2 percent of export earnings.

C. Summary of Funds Flowing to the Region Post-1989

Multilateral and bilateral financing has been the only source of significant positive transfers to the region since 1989. However, after the adoption of the far-reaching reforms supported by this financing, the supply response will ultimately depend on the interest displayed by the *foreign private sector* in a given country. It is widely acknowledged that foreign direct investment and exports will have to be the engine of growth in the region. A newly created enterprise will be dependent on foreign savings, foreign technology and foreign management methods if it wishes to penetrate non-traditional markets and pass through a successful transition to establish market-based links with other economies. Overall, the extent to which enough enterprises in a given economy have access to foreign capital or foreign investors, will have an important effect on economic performance. The table below shows the role of each type of creditor.

Table 2: **Net Borrowing from Official Sources* (in US$million)**

	1989	1990	1991	1992(e)
Hungary	-79	346	1,540	843
CSFR	84	365	2,264	1,059
Bulgaria	-490	-154	915	905
Poland	n.a.	2,986**	1,245**	1,750**
Romania	-1,403	-20	1,295	1,475

Net Borrowing from other Private Creditors (US$ million)

	1989	1990	1991	1992(e)
Hungary	818	677	550	443
CSFR	0	221	-201	167
Bulgaria	675	-140	-150	-15
Poland	n.a.	103	40	-115
Romania	-14	-52	125	125

Table 2 (con't): **Net Borrowing from Commercial Banks (US$million)**

	1989	1990	1991	1992(e)
Hungary	529	-1,670	-1,150	-935
CSFR	469	-271	-364	-176
Bulgaria	1,114	497**	685**	700**
Poland	n.a.	796**	850**	855**
Romania	-278	-6	200	125

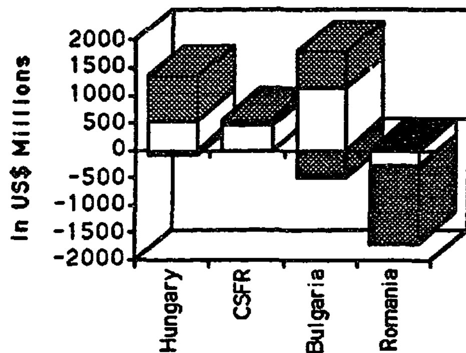
(*) Includes IMF, IBRD, and other multilateral creditors and official bilateral sources.

(**) Includes rescheduling of interest and principal.

In 1989 Romania was the only country making major negative transfers from the region, and this was based on deliberate government policy. The negative transfer totalled US$1.7 billion, of which US$1.5 billion was to official creditors. Other private creditors were an important source of funds for Hungary and Bulgaria in 1989. Commercial banks lent more to Bulgaria than to any other country in the region that year, amounting to over US$1.1 billion.

The following charts illustrate the developments since 1989:

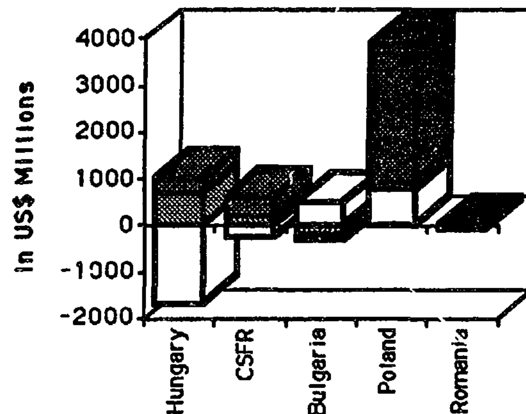
Figure 7: Net Borrowing by Source - 1989

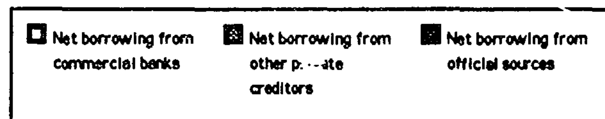


Source: Staff estimates based on IIF Country Reports.

Figure 7 shows Romania and Bulgaria making large net transfers to official sources. Also, for Bulgaria it is the last major borrowing episode from OECD commercial banks. The situation changed dramatically in 1990, as shown in Figure 8. Commercial banks retreated massively from Hungary (net negative transfer of US$1.8 billion) and to a lesser extent from CSFR. Other private creditors were the main source of funds for Hungary. Bulgaria's net

Figure 8: Net Borrowing by Source - 1990



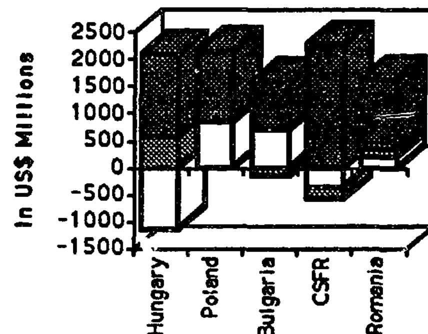


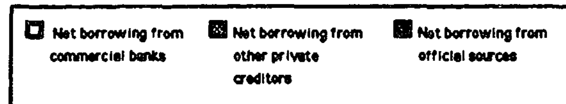
Source: Staff estimates based on IIF Country Reports

borrowing from commercial banks reflects unpaid obligations, and the figures for Poland mainly result from the official debt reduction deal.

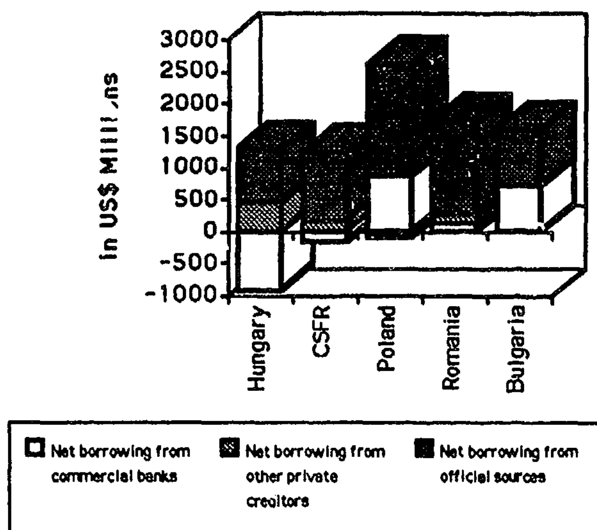
As shown in Figure 9, the official sector is the predominant source of funds in every country in the region in 1991. CSFR is the largest recipient in dollar terms, with net borrowing of almost US$2.5 billion. Again, the commercial bank presence for Poland and Bulgaria reflects unpaid obligations rather than new lending. Other private credi-

Figure 9: Net Borrowing by Source - 1991 (Estimate)





Source: Staff estimates based on IIF Country Reports



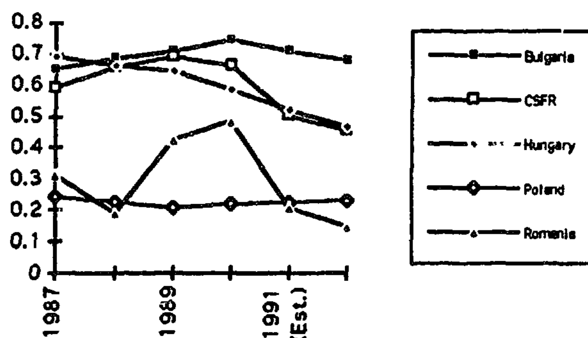
Source: Staff estimates based on IIF Reports.

tors have almost disappeared completely except from Hungary. Commercial banks continue to retreat from Hungary (net negative transfer of US$1.2 billion) and CSFR.

In Figure 10, the outlook for 1992 is much the same in terms of the relative importance of each type of creditor. The only change is that other private creditors are expected to make some positive transfers to CSFR and Hungary, although less than in the previous year for Hungary.

Characteristics of Commercial Lending to the Region

The relative exposure of commercial banks may be judged by the following:



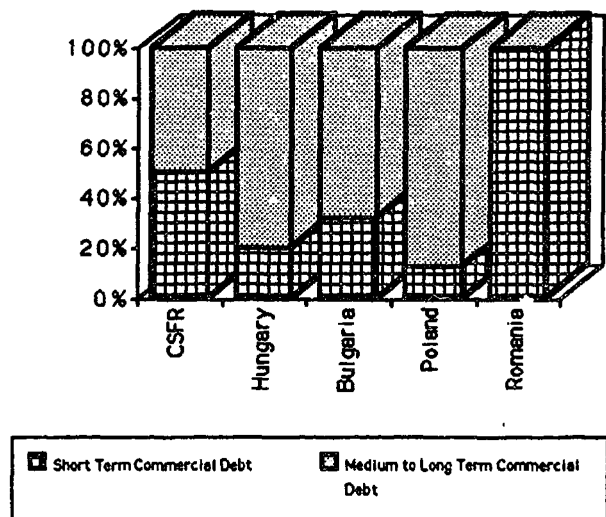
Source: Staff estimates based on IIF Country Reports.

For Romania, the impact of large prepayment of official obligations from 1988 onwards resulted in a jump in the importance of commercial debt to a peak of about 50% in 1990. Again, with large new borrowings from official creditors in 1991 and beyond, the relative weight of commercial debt falls to below 20% of the total debt.

Bulgaria's unresolved debt overhang is clear in Figure 11; commercial banks have the highest relative exposure to Bulgaria in the region. The role of commercial creditors is declining in CSFR and Hungary as the banks retreat through negative net transfers, and it is relatively constant at about 25% of the total in Poland.

Relative Importance of Short Term Commercial Debt

Another characteristic of commercial debt that varies in the region is the *maturity profile*, or the relative importance of short term commercial obligations. If a country experiences a liquidity crisis or other debt servicing difficulties, holders of its short term debt are at greatest



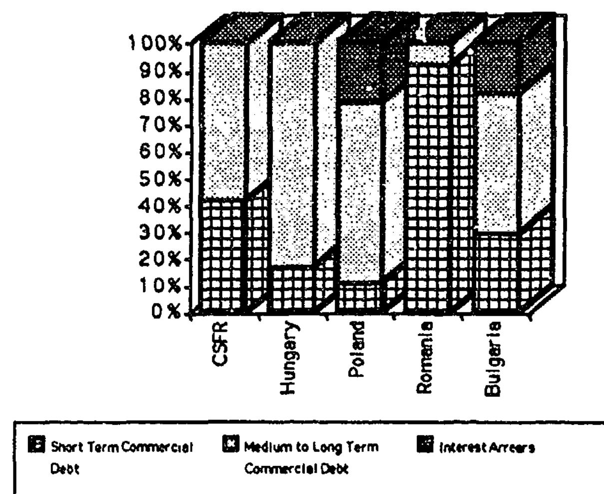
Source: Staff estimates based on IIF Country Reports.

risk, since such claims are costly for banks to reschedule. Bulgaria in particular is unable to service even its short term debt, and banks are reportedly nervous about setting a precedent by allowing any kind of restructuring or reduction of these claims. Figures 12 and 13 show the relative share of short term obligations in commercial debt.

As seen in Figure 11, commercial banks have clearly been Hungary's major source of financing in the past. Their exposure is in fact many times that of the other creditors put together. Within Hungary's total debt, only about 16% is in the form of ST obligations. In CSFR too, commercial banks have the largest exposure by creditor

category. Within commercial debt, a curious phenomenon is observed: CSFR and Romania both have more ST than long term obligations. **Poland** has a very low share of commercial debt altogether, of which a relatively tiny share has been in the form of ST obligations, even as far

Figure 13: 1992 (Projected)

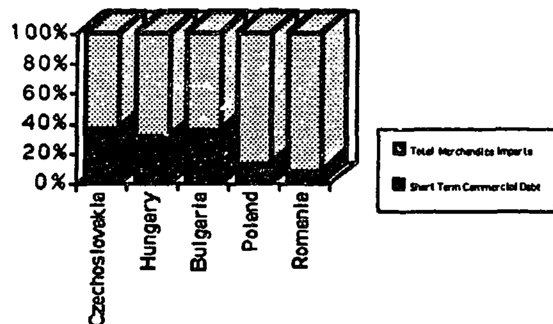


Source: Staff estimates based on IF Country Reports.

back as 1986.[4] Also, Poland's entire ST obligations are owed to commercial creditors. Commercial banks have the largest exposure of all creditor categories in **Bulgaria**. A major part of commercial exposure is in ST claims, but overall these form a relatively small share of the total debt. **Romania's** external debt is very low for well-known reasons. The share of ST commercial obligations is expected to decline from 99% in 1989 to about 90% in 1992, as shown in Figure 13.

Finally, the following chart provides a rough indication of the region's reliance on trade finance, by comparing hard currency merchandise imports to short term commercial borrowing in the corresponding period.

Figure 14: 1989



Proportion of Merchandise Imports Financed by ST Commercial Debt

All countries except Poland and Romania appeared to rely on short term credits in 1989. We assume that an important proportion of these represented trade lines. It may be argued that these figures reflect inherited condi-

Figure 15: 1990

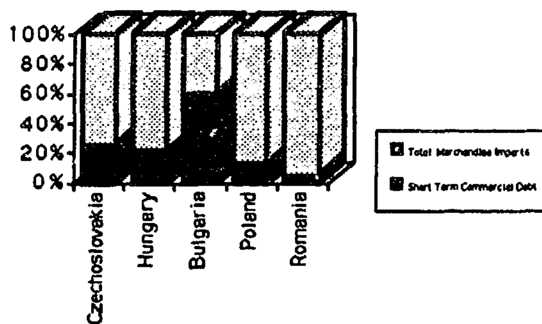


Figure 16: 1991 (Estimate)

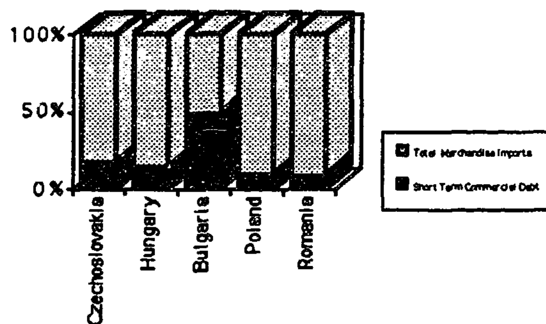
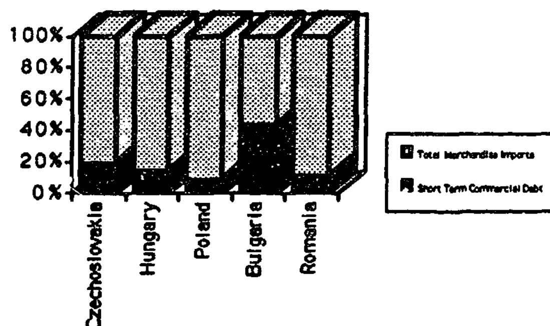


Figure 17: 1992 (Projected)



tions, and are based on borrowing and lending decisions made according to outdated assumptions, such as the Soviet umbrella or the presumption that all loans carried a

[4]. Perhaps Poland was not perceived by banks to be fully under the Soviet umbrella since the early 1980s.

government guarantee. The Romanian case is curious: borrowing from commercial banks in 1989 was US$248 million, of which US$247 million was short term. Merchandise imports in 1989, however, were US$3.41 billion. According to IIF statistics, reserves increased that year by over US$1 billion. Obviously, Romania does not appear to have financed its imports through short term credits, although bankers always say that the only business they did (and still do) with Romania is short term and trade related. Poland imported a total of about US$7 billion of merchandise in 1989, and borrowed a little over US$1 billion in short term commercial loans that year.

By 1990 (Fig. 15) the share of short term commercial debt was sharply reduced for Hungary and CSFR, while for Poland it remained roughly constant. (The figure for Bulgaria reflects the moratorium and three month rollovers, in particular arrears and penalty interest which is recorded as ST credits).

In 1991 the same figures for CSFR and Hungary fall even further, with the trend expected to continue in 1992 or at best remain unchanged.

Source: Staff estimates based on Institute of International Finance Country Reports.

D. Maturity Profile of Total External Debt

Given the discussion in the preceding sections of the relative importance of commercial debt, and the maturity profile of this debt, it may be useful to contemplate the *maturity profile of overall obligations to hard currency* creditors in the region. Table 3 below shows relative shares of short term and long term total financial flows for different countries:

Hungary and Poland have remarkably small portions of ST debt outstanding relative to their long term obligations. For CSFR, medium and long term debt is growing while short term debt is falling. For Romania both categories are growing dramatically. The figures for Bulgaria mainly reflect the effects of the moratorium.

Table 4 looks at *flows of short term debt from private sources in the period 1989-1991*, with commercial banks' projections for 1992:

As indicated earlier, private short term flows from non-bank sources, while modest, will be more important than from commercial banks.

Table 3: **Breakdown of Total External Debt by Maturity (in US$ million)**

	1989		1990		1991		1992(f)	
	MLT	ST	MLT	ST	MLT	ST	MLT	ST
Hungary	17,230	3,307	18,541	2,940	19,090	3,055	18,267	3,382
CSFR	4,596	3,587	5,180	2,905	6,808	2,443	7,444	2,383
Bulgaria	7,520	2,704	7,402	3,272	7,864	3,125	8,415	3,054
Poland	37,061	1,295	46,625	1,339	47,676	1,384	46,891	1,302
Romania	269	313	167	352	1,166	985	2,785	1,009

Table 4: **Net Short-term Flows to the Region**(*)

	1989		1990		1991		1992	
	Commercial	Other Private	Commercial	Other Private	Commercial	Other Private	Commercial	Other Private
Hungary	-56	42	-1,200	555	0	110	180	200
CSFR	182	-71	-423	-70	-150	50	0	40
Bulgaria	388	93	374	-12	0	-8	0	3
Romania	149	-11	-5	-23	180	50	100	50

(*) This information was not available for Poland

E. Direct Foreign Investment—Project Finance[5]**:**

A very limited subsector of investors may be ready to acquire fixed assets in the region if they feel the investment is "safe", and furthermore, that they may lose by going in later rather than now.[6] Which of the commonly mentioned factors—educated labor force, low wages, manufacturing skills, political stability— is more important to new foreign investors? Again, why are some countries preferred over others for DFI? What is the situation with regard to repatriation of profits in the newly adopted foreign investment laws of the region? Are investors responding to particular incentives, either in the host country or in their home countries? Does the attitude of export credit agencies (willingness to provide cover only in some countries) have a major effect? The mixed answers and lack of clear trends in response to these questions indicates that banks and investors are still operating on a case by case basis.

Most of the DFI is assumed to be undertaken in the form of a clearly defined, self-contained project that generates its own income. The project is financed with a commercial bank loan. In other words, information on DFI and joint ventures is taken here as a qualitative proxy for enterprise access to project financing from private/commercial sources. Project finance at this stage of development in the region implies a long term investment by a foreign entrepreneur who has an obvious interest in *increasing his return on equity employed via the leverage effect of debt financing.*[7] The basis for lending is the future cash flow from this project, and the loans are largely secured by i) the project's assets and ii) the contractual arrangements with the project participants. An essential feature of project financing is that the *actual initiators and owners of the project no longer assume full liability for the loans and thus the risks of the investment project. Commercial banks, and other project sponsors assume a part of the risks.*

Commercial bank attitudes toward project finance are based on a number of criteria which are widely known, but may be briefly summarized here in the context of the discussion that follows on conditions specific to the CEE region.

The foreign entrepreneur approaches a foreign commercial bank, which will then conduct a credit assessment of the project. Traditionally, this will be based on the analysis of financial statements, and/ or in the case of a start-up project, the analysis of security (mortgages, escrow accounts etc.) that must be furnished by the project sponsors.

A drawback of financial statement analysis is that balance sheets provide information on past performance, and such analysis implies that ratios calculated from these numbers will not change materially in the future. It may be argued that such a static view is not admissible in the case of long term finance in an uncertain environment, especially if the size of investment to be financed is large relative to the size of the existing assets. *Security therefore becomes more important, although it poses similar problems since its valuation is also based on present considerations.* Furthermore, in case of recourse, the value of assets pledged as security will depend on the price that a third party will be willing to pay for it at the time. This has a curious effect: highly specialized and expensive machinery should in theory provide sufficient collateral in terms of its value as measured by purchase price in the west. However, the complementary technological and managerial skill requirements alone may constitute a barrier to entry for the particular activity. This would limit the demand locally for the equipment in the event of liquidation of the business, and thus *depress its value as collateral.* Given the scarcity of western style managerial knowhow in the CEE region at present, it is likely that commercial banks will continue to be very conservative in their valuation of collateral.

Political risk comprises all measures by public authorities that impair the course of the project or threaten its commercial success as a result of changes in the original legal framework. Examples would be unilateral changes in licensing, tax, environmental and other regulations, belated export restrictions or expropriation.

Table 5: **Country Risk Forecasts.**[8]

	Transfer Risk		Invest. Risk		Export Risk		Growth (%)		Inflation (%)		Curr Acc($b)	
Bulgaria	B	(nc)	A	(B)	B+	(B-)	2.0	(nc)	10.0	(6.0)	-0.6	(-0.4)
CSFR	B	(nc)	A	(nc)	B	(nc)	2.0	(nc)	10.0	(nc)	-1.5	(nc)
Hungary	B-	(nc)	A	(nc)	B+	(nc)	1.5	(nc)	22.0	(nc)	-0.75	(-0.8)
Poland	B	(C+)	A+	(C-)	B-	(nc)	2.0	(2.5)	25.0	(20.0)	-0.55	(-0.5)
Romania	C	(nc)	C	(nc)	C-	(nc)	2.0	(nc)	15.0	(10.0)	-2.0	(nc)

5. Note: in some countries eg. Hungary, a portion of DFI is classified as imports and the remainder is "other private creditors". For all countries in the region, it is not clear what system is used to keep track of DFI as opposed to suppliers' credits etc.

6. It may be interesting to consider the impact of IFI involvement in attracting foreign investment—do long-time (pre 1989) foreign investors in general prefer (for arbitrage reasons) the distorted policy environment that prevails prior to IFI conditionality, and are they likely to withdraw once the subsidies are removed? To date there appears to have been no exodus of such longtime investors. This would indicate that there is still a premium on market knowledge and personal contacts.

7. "Project Finance from the Banks' Perspective", Paul Grosse, Deutsche Bank AG.

8. Source: Political Risk Services, Syracuse NY.

Special attention is paid by project sponsors to *transfer risk*, i.e. the country's ability to make payments in foreign exchange, where investments are financed in foreign currency but receipts are in local currency. A critical consideration is whether the country as a whole will have sufficient foreign exchange available over the life of the project. *In critical cases, where a country ceases its external debt service payments for lack of foreign exchange, or agrees on a restructuring of its obligations, the value of a transfer guarantee from the central bank is questionable from the commercial banks' viewpoint.* This is currently the case in two countries in the region, Bulgaria and Poland.

The situation is different if the project output is exported and sold for foreign exchange at world market prices. In this case the project generates the necessary foreign exchange itself. The banks then have the possibility of channelling the receipts, with the central bank's consent, initially to accounts outside the country and of servicing the debt in foreign exchange from these accounts (offshore escrow accounts). This is a method of substantially limiting the transfer risk. Table 5 is an example of commercially available risk assessment for the region that was published in September 1991. It shows the 5-year outlook for Transfer Risk, Investment Risk, and Export Risk. "A+" indicates least risk and "D-" indicates highest risk. The previous forecast is shown in parenthesis if there has been a change; (nc) indicates no change.

The Current Situation in the Region—Seniority Accorded to Project Finance

All banks interviewed for this paper stated that as long as there was no real convertibility of local currency, *only projects which generated sufficient foreign exchange revenues would in principle qualify for finance in hard currency.* The cost of this financing is likely to be high for the particular project, since as a prerequisite, according to an experienced banker lenders would require

"adequate cover to be provided in favor of the lender against all risks inherent to the project itself as well as those risks attributable to the economic environment in the country the borrower is domiciled in ... Ability of the borrower to freely dispose of its hard currency receivables would require special permit from the authorities, available only in exceptional cases...*Financings are structured as purchase of receivables, offtake or factoring type arrangements...* Due to...insufficiency or even total lack of legal provisions [on bankruptcy], restrictive foreign exchange policies and unsettled restitution claims, the structuring of a security/seniority arrangement acceptable to western banks often turns out to be a dreadful exercise...In general a two level security arrangement is demanded comprising direct access to the hard currency cash flow...*by the assignment of receivables and the pledge of amounts collected in an escrow account as well as title to the fixed assets of the project.* The latter, however, is not easily achieved due to lacking mortgage legislation or factual impossibility to enforce rights in case of foreclosure...In order to structure financing in such a way that it becomes a bankable transaction extremely creative structures have to be worked out..."[9]

Offtake refers to the prior sale of output to specialized trading companies who arrange for the sale of given volumes in hard currency. Examples were cited of CEE dairy and poultry products being pre-sold to CFA Zone African countries or other LDC governmental food importers who agreed to pay hard currency. In general, Austrian trading companies associated with banks were able to arrange for such transactions relatively easily since they say they have over 80 years of experience doing such deals with eastern Europe. Alternatively, there are often leasing arrangements with creative financing. For example, the Swedish furniture manufacturer IKEA has been active in Poland and Hungary for 20 years. It accepts pieces of furniture as installment payments for factories that it has set up in the region.

Most market sources said that, except for Hungary, the interest elsewhere was in *trading rather than manufacturing.* This is consistent with the weak legal frameworks which do not provide enough security to equity investors, and are not conducive to structuring creative arrangements as mentioned above. *Bankers and investors were very clear that the only factor they considered was the legal framework and repatriation of profits.* Low wages and other characteristics of the labor force reportedly would not enter their decision making process.

The share of the German speaking countries (Germany, Austria and Switzerland) in Hungarian foreign trade and DFI reached 40% in 1991—this corresponds to the share of the CMEA area prior to 1989. Bankers in both Germany and Austria mentioned that Hungary had adopted a legal framework almost identical to the German/Austrian one. This is also the case in CSFR, which has had about a third of its business dealings with the German speakers since 1989. Answers to the question of whether foreign investors were succeeding in mobilizing domestic resources, were mixed. Most bankers felt that foreign investors were coming in with their own funding, and that the domestic financial sectors in the region were either too unfamiliar or too bureaucratic to be tapped. Several bankers felt that foreign investors were instantly assumed to be totally creditworthy by nationals eagerly looking for joint venture partners.

According to the Central Statistical Office, 3000 new joint ventures were set up in Hungary in the first six months of 1991, with the investment of foreigners amounting to some US$350 million. The total number of joint ventures operating in Hungary at end-June 1991 was 8700. The accumulated

[9] Rosenmayr, Edgar in "Hard Currency Borrowings from Private Sector Banks", p.23, Creditanstalt Bankverein, Vienna, September 1991.

statutory capital of firms established with foreign participation was US$4.4 billion, a third of which was invested by foreign participants. So far no data are available on the exact geographical distribution of the foreign investors, but Germany, Austria and USA preserved their lead in the number of joint ventures set up. USA continues to rank first according to the total value of investments. According to NBH only US$20 million was transferred from Hungary in repatriation of profit in the first six months of 1991.[10]

In Hungary, foreign investments in the form of non-cash contributions are classified as imports. In particular, import data includes contribution in-kind by foreign investors to the statutory capital of newly set up joint ventures, deliveries under leasing agreements, repayment of earlier Hungarian credits to the Soviet Union by gas shipments from the Yamburg pipeline, etc. According to the Finance Ministry, this came to about US$550 million in the first seven months of 1991 this year. CSFR is the only other country in the region with active interest on the part of foreigners in joint ventures.

F. Institutional Setup—How is the Borrowing Managed in Different Countries?

Under the previous regimes, convertible currency borrowing requirements were set administratively and incorporated into the State Currency Plan. The Foreign Trade Bank was the authorized borrowing arm of the Government and would carry out the required transaction, without any input or participation in a borrowing strategy. Bankers stated that the "Soviet umbrella effect", i.e. the markets' belief that the USSR would bail out its allies rather than allowing them to default on western obligations, accounts for a large part of the access on favored terms for the various Foreign Trade Banks through the 1970s and 1980s. The most important reason of course is the prompt and timely commercial debt servicing record for the region as a whole prior to 1989.

What institutional arrangements have replaced the State Currency Plan? What is the new allocation of responsibility between the National Bank and the Foreign Trade Bank in each of the countries? Who is funding training and technical assistance for the new debt managers? What borrowing instruments are being considered by sovereigns that may still have access to the market (Hungary, Czechoslovakia, Romania)? Are there any pre-determined borrowing targets by currency? What is the institutional forum in each country for developing a national strategy to assist private enterprise to gain access to foreign financing?

The answers to these questions were pursued in the interviews with commercial banks, and turned out to be rather inconclusive. It appears that the National Bank of Hungary is the only well-organized entity with well-defined staff and a strategy to access the international capital markets, and that too appears heavily dependent upon what type of reception is expected for sovereign issues (i.e. borrowing wherever they can).

Western commercial banks were far more eager to discuss their impressions of the newly forming *commercial banking sector* in each of these countries, which they believe is an important prior step to managing foreign borrowings in any strategic way in future.

Institutional Setup—Domestic Commercial Banks

Throughout the region, previously the State Bank acted as both a central bank and a commercial bank, receiving savings from private citizens (channeled to it through the savings banks) and passing them on to specialized sectoral credit banks. These credits were granted in the framework of a "central credit plan" but no sanctions were applied in case the credit remained unpaid. The credit would simply be transformed into a subsidy.

This load of bad credit portfolios is in the very early stages of cleanup at present, and is compounded by the general problem of insufficiently capitalized banks. The political sensitivity of selling these banks to foreigners was noted by western bankers, but all felt that this was the only solution, since the banks in question would not be able to raise capital on the international markets for many years.

In this system, no sophisticated qualifications were required for bankers, who were predominantly officers of the same kind as in the ministries. This lack of experienced personnel today emerges as the main problem in setting up a modern banking sector, under which credits can only be granted to companies whose prospects can be evaluated and who can offer some collateral. *International experience is also lacking, since past relations with foreign countries were all concentrated in one institution.* In Hungary, CSFR and Poland, independent banking systems have been legislated but currently lack electronic data processing equipment and other technology.

The first steps towards a two-tier banking system were taken by Hungary and Poland in 1987. The essence of the reforms was enacted in Poland in 1989 when the National Bank of Poland (NBP) was completely separated from its commercial banking functions and given a high degree of autonomy. As of January 1990 NBP is no longer required to submit a detailed credit plan to Parliament for approval. CSFR initiated banking reforms in 1990, and the matter is still under consideration in Bulgaria and Romania.

The National Bank of Hungary was until recently under the control of the Council of Ministers, but legislation establishing its independence was passed in December 1991. A main role for the central bank is to provide finance for the public sector, but the new law limits the credit that NBH must provide to the public sector. It also requires the State to reduce its ownership share of commercial banks to 25% by 1997. Since the introduction of two-tier banking in Hungary in

[10] Vienna Institute of Comparative Economic Studies report of 9/91.

1987, five independent commercial banks were created in addition to the already existing specialized smaller financial institutions. The three largest commercial banks have a market share of loans outstanding of about two thirds. Furthermore, banks with foreign participation have been permitted to operate since the early 1980s. The number of banks in total has increased to about forty, of which one half have foreign equity participation. The new Hungarian banking law foresees foreign participation to be limited to 40% in the four largest banks.

G. Access to Bond Finance and other Private MLT Financial Flows

For new voluntary capital flows, (eg. commercial bank loans, bonds) creditors perceive clear benefits to waiting, unless adequate and credible assurances are obtained that the debt will be serviced. Czechoslovakia and Hungary are the only two countries in the region that have successfully placed medium term bonds in the markets since end-1989. Annex 1 lists the two countries' borrowings since 1989.

Hungary has led the way in recent borrowings by the region in the international bond market. Both Hungary and CSFR compete for funds with Latin American borrowers such as Mexico, Venezuela, Brazil, Argentina and to some extent South Africa. Market sources say that east European states attract less "flight capital" than their Latin American counterparts. This has some (limited) effect on the price at which a new issue can be sold. In other words, the spreads paid by the country have to be higher since there is no ready pool of nationals, well-informed about the significance of reforms in the country, prepared to buy its bonds. The country must therefore compete with other issuers of similar risk for a place in the foreign investor's portfolio.

The National Bank of Hungary (NBH) was extremely active in the international capital markets in the first nine months of 1989, borrowing in DM, Yen, Austrian schillings and ECU. Hungary appears to have been a great favorite of the Yen private placement market (known as Shibosai) in March 1989, when Daiwa Securities arranged six private placements in the same month, with maturities ranging from seven to ten years for amounts ranging from ¥20 to 40 billion.

The German and Austrian capital markets were the first to open their doors to NBH after the changeover in eastern Europe at the end of 1989. As early as February 1990, Hungary issued a seven year bond in each market, and returned a second time later in the year.

In August 1990 Hungary's State Development Institute borrowed US$200 million at a fixed coupon rate of 10.5%, under the Expanded Cofinancing Operations (ECO) arrangement whereby repayment of principal was backed by the World Bank. The bond was for ten years, with repayment of principal scheduled in the form of a bullet (single installment) repayment upon maturity. This first dollar issue was viewed by the markets as overt demonstration of financial support for Hungary by the World Bank. Subsequent to the ECO-enhanced Eurobond, interbank lines were re-established. (Hungary had been losing significant amounts of short-term interbank deposits in early 1990). A seven year Austrian schilling bond was launched in September 1990, and a five year DM issue came out in October 1990. Regular bond issues have followed in DM, ECU, US dollars and yen. None has been guaranteed since the ECO. A US$ 1 billion funding program was announced for the international capital markets in 1991.

In May 1991 NBH set up the country's first Euro-medium term note program. It is a relatively small facility at only DM200 million, but it provides a more flexible source of funding compared to bond issues. The program allows for paper to be issued as fixed rate, floating rate and zero-coupon notes with maturities from two to thirty years. Paper may also be issued with a call option. Deutsche Bank is the arranger and sole dealer, and says that NBH is most likely to place the paper in Germany, initially within the two to four year maturity range due to investor demand at the short end of the curve. NBH intends to list the paper on the Frankfurt Stock Exchange.

The first Eurodollar issue was launched in late June 1991 by Bankers Trust as a five year US$100 million, 10.5% deal, priced at between 250 and 285 basis points over the US Treasury curve. According to NBH officials, the major purpose of the deal was to widen Hungary's funding base and introduce its name to investors' portfolios. Moody's Investors Services rated NBH a Ba1, while Japan Credit Ratings Agency rated it A-.

Following the Eurodollar issue, there was talk of an introduction to the British capital markets. The hope was to raise around 50 million British pounds through a sterling issue (known as a bulldog) maturing in about 20 years, with a put option after seven years, for a yield spread over the seven year gilt as little as "below three hundred basis points". However, due to uncertainty in the region in neighboring Yugoslavia, this introduction has been postponed for now. In the remainder of 1991, there were four more bond issues, two in yen and one each in DM and ECU.

The largest DM bond to date for NBH has been issued in January 1992, in the amount of DM600 million. A Samurai bond of ¥30 billion was issued in the same month, not for private placement but instead as a public issue, representing larger-scale access by NBH to Japanese investors.

The risk inherent in Hungary's growing liabilities in the form of bonds is that these are considered the most inflexible of debt, held by widely scattered small retail investors who are difficult to find. In the event of debt servicing difficulties in future, Hungary would have to accord seniority to its

bondholders. Large amounts of IFI debt outstanding, also senior, would complicate the picture.

According to the International Financing Review of March 21, 1992, NBH is reportedly in discussion with Korean banks over the possibility of a new syndicated loan. The amount is likely to be US$40-60 million. Korea and Hungary have strong trade and investment ties so for the past couple of years NBH has headed to Seoul for its international term loan borrowings. Last year, KDB arranged a US$40 million loan for NBH priced at 150 basis points over LIBOR for seven years. In 1990 its loan only cost 87.5 basis points over LIBOR for four years, with the spread falling to 75 basis points for the remaining four years.

CSFR, while on a far more modest scale than Hungary, has also managed to keep its name in the international capital markets in 1990 and 1991. The State Bank was able to borrow US$200 million in November 1991. The three year bonds were priced to yield three percent more than US government securities of comparable maturity. This is a higher price than that paid by Hungary or Mexico, but cheaper funding than that achieved by Brazil or Argentina. In terms of financial ratios, CSFR is among the most creditworthy of borrowers. Debt per capita stands at US$506, compared with US$1887 for Hungary. However, the 300 basis point yield spread over US government bonds includes

(i) the political risk that internal divisions within the country might lead to default, e.g independence of Slovakia. For this reason the covenants of the bond issue make it a condition of default for Statni Banka to cease to act as the central bank of either the Slovak or Czech republics, or the country as a whole. Nomura Securities, the lead manager, states that only about 50 basis points of the yield spread reflected these concerns;

(ii) the residual risk that external political events might lead to damaging economic strain, e.g massive influx of economic migrants from Russia, and

(iii) the unknown economic risks of transforming from a command economy that was more centralized than Hungary or Poland under communist rule.

CSFR has recognized, in common with other emerging sovereign borrowers launching bond issues in 1991 and 1992, that the foundations for wider access to the capital markets can be laid early in the process of adjustment, even if the process of establishing a track record requires paying premium interest rates at first.

Part II contains country-specific information on debt and financial flows that was obtained from market sources, and may be helpful in the effort to understand the commercial bank/private sector financing attitudes towards the region. (See bibliography for a listing of IIF country reports).

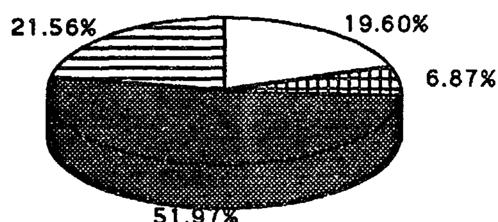
Conclusion

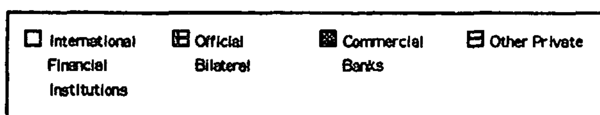
Bankers point to a pattern in the way emerging economies attract overseas capital: privatization of large scale enterprises is the first stage, attracting both international equity investment and project finance from foreign banks. This is followed by the development of a domestic stock market, the sale of equity-linked financial instruments abroad and then, finally, wider access to the international debt markets.

PART II. Details by Country

HUNGARY

Figure 18: Hungary - Relative Exposure by Creditor - 1991





Source: Staff estimates based on IF Country Reports.

Hungary's total external debt increased to US$21.5 billion at the end of 1990 from US$20.5 billion a year earlier. A positive valuation effect of US$1.7 billion more than offset net repayments amounting to about US$600 million. Of total debt at the end of 1990, about 85% or US$18.5 billion was medium and long term. Short term commercial debt decreased US$0.4 billion from the end of 1989 to US$2.9 billion in 1990 mostly as a consequence of outflows to commercial banks. Total debt to commercial banks at the end of 1990 amounted to US$12.2 billion, a decline of about US$1 billion from the previous year. Debt to other private creditors increased to US$4.4 billion, probably reflecting trade credits and joint venture working balances. Commercial banks have clearly been Hungary's major source of finance in the past. Their exposure is many times that of all other creditors put together.

Total external debt fell to US$19.8 billion at the end of July 1991, of which US$2 billion was short term and US$17.8 billion was long term debt. The fall in debt resulted from running down short term liabilities and a strong appreciation of the dollar, reducing nondollar liabilities in dollar terms. External reserves are reported to have been US$2.1 billion at the end of August 1991 compared with US$1.1 billion at the end of December 1990. Preliminary figures showed an increase to US$2.7 billion at the end of September, representing three months of imports. For all of 1991, commercial banks are likely to be repaid US$0.8 billion, while other private creditors provide US$0.6 billion. On this basis, total debt at the end of 1991 would be US$22.1 billion. Debt to commercial banks, however, would decline to US$11.6 billion at the end of 1991 from US$12.6 billion at the end of 1990. The share held by commercial banks would fall to 52 percent compared to 59 percent at the end of 1990. In addition to net credit inflows of US$1.3 billion, the assumption of a weaker dollar accounts for the rise in debt from its mid-year level of US$19.8 billion. Since a large share of this debt is in non-dollar currencies, its dollar equivalent rises and falls with the exchange rate.

In 1990 the pattern of external financing changed from the past several years. Access to private international

Table 6: **Breakdown of External Financing (in US$ million)**

	1986	1987	1988	1989	1990	1991	1992
Convertible Currency External Debt of which	17,106	19,752	19,681	20,537	21,481	22,145	21,649
MLT	13,612	16,649	16,318	17,230	18,541	19,090	18,267
ST	3,494	3,103	3,363	3,307	2,940	3,055	3,382
By Creditor							
IFIs	1,682	1,822	2,099	2,108	2,833	4,340	5,200
Bilateral	1,684	2,145	1,864	1,767	1,656	1,522	1,281
Commercial Banks of which	12,095	13,625	13,086	13,269	12,642	11,510	10,146
MLT	9,059	11,031	10,264	10,574	10,981	9,893	8,419
ST	3,036	2,594	2,822	2,695	1,661	1,618	1,727
Other Private Creditors	1,645	2,161	2,633	3,393	4,350	4,774	5,021
Reserves Excluding Gold	2,302	1,634	1,467	1,246	1,069	2,945	3,902
Deposits in BIS Banks	2,141	1,504	1,379	1,165	1,764	-	-

capital markets was reduced, and Hungary drew on reserves to meet net repayments of about US$1 billion to private creditors. A relatively strong current account performance in 1991 has limited Hungary's financing needs to amortization payments and reserve accumulation. In addition, DFI flows increased strongly to almost US$400 million for January through May 1991.

In the first eleven months of 1991, Hungary's external financing situation strengthened through better than expected current account performance, higher foreign direct investment inflows and large inflows from official creditors. As a result, access to international capital markets increased. Foreign direct investment amounted to US$750 million by the end of September 1991 compared to US$337 million for the whole of 1990.

No major new medium-term bank credits were announced in 1991, as banks continued to receive net payments, implying a reduction in their exposure. A US$ 100 million bond issue was placed in the European market by Bankers Trust in July 1991, carrying a coupon rate of 300 basis points over LIBOR. Bond issues announced in the sterling market were postponed, however, as the political situation in neighboring Yugoslavia contributed to uncertainty in the market. There were also three DM bonds in March, April and October 1991. The first two were issued each with a five year maturity, in the amounts of DM 200 million and DM 150 million. The October 1991 DM bond matures in seven years. Hungary also tapped the Euromarket in October 1991 with an issue of ECU 200 million and a Yen issue of 20 billion. The ECU issue matures in five years, and the Samurai in seven years. Two more bonds have been issued subsequently in 1992: a Samurai bond of 30 billion yen and a DM600 million bond. (See Annex 1 for a summary of Hungary's access to bond markets).

Table 7 shows that 1989 was the last year in which commercial banks made a positive net transfer to Hungary. No new short term credits have been recorded either. On the other hand, positive inflows are still coming from other private creditors.

Factors Influencing Foreign Involvement in the Economy.

Size of Private Sector

On the output side, recorded industrial production of enterprises with more than 50 employees, accounting for 80 percent of output, fell 9 percent in 1990. In 1991, output of enterprises employing more than 300 people decreased by 20%. At the same time, an expansion of over 50% occurred in the output of primarily private small businesses employing less than 50 persons. Large enterprises, in particular, showed less flexibility in shifting production into exports to western markets. Production of small enterprises is reported to have officially doubled, reducing the fall in total production somewhat.

Reorientation of Trade

Exports to the CMEA region amounted to US$630 million plus TR500m which is substantially less than the TR2.6 billion registered in the first half of 1990. The reorientation of Hungarian foreign trade continues: in the first six months of 1991 about 73% of exports were destined for the OECD region, of which 47% were for the EC. Exports to Germany increased by 58%, and imports from there by 71%. (Only some 10% of trade with Germany corresponds to former GDR territory). The volume of trade with Germany may reach some US$4 billion by end 1991.

In convertible currency trade with the Soviet Union, Hungarian deliveries amounted to US$400 million, and imports to US$675 million in the first eight months of 1991.

Despite real appreciation of the forint, exports to Western markets increased strongly. In November 1991 the Government devalued the forint by about 5% in order to strengthen competitiveness.

The situation is unbalanced with regard to trade-related payments; while Hungary reportedly transfers the payments for imported goods without delay, the USSR had opened letters of credit amounting to only US$163 million by the end of July. In effect, therefore, Hungary is extend-

Table 7: **Hungary: External Financing Flows (in US$ million)**

	1989	1990	1991	1992
External Borrowing, Net	1,268	-646	1,340	350
of which				
Commercial Banks	529	-1,670	-750	-935
Disbursements	1,866	1,015	700	550
Repayments	-1,280	-1,485	-1,450	-1,665
ST credits, net	-56	-1,200	0	180
Other Private Creditors, Net	818	677	550	443
Disbursements	1,000	382	750	600
Repayments	-224	-260	-310	-358
ST Credits, Net	42	555	110	200

Source: IIF,Country Report dated November 8, 1991

ing involuntary trade credits to that country. The Hungarian government has also signed agreements with individual republics. These include mutual deliveries of commodities with Russia of up to US$670 million, US$50 million with the Ukraine and US$300 million with Kazakhstan for 1991. Performance on these agreements remains to be seen.

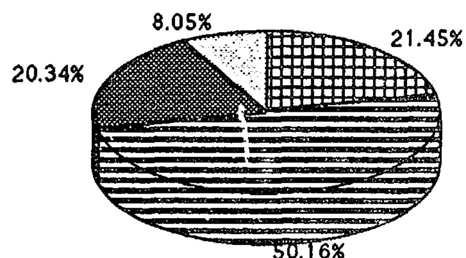
Other

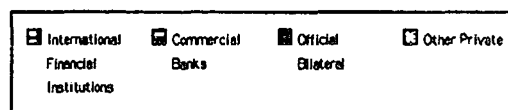
Tourism produced 20% higher convertible currency income than in the period January-May 1990 despite a 12% decrease in the number of visitors. There has been a substantial inflow of convertible currency in the form of unilateral transfers from abroad for private individuals. In the first quarter of 1991 this amounted to US$200 million. It is assumed that some of these transfers represent export incomes of private entrepreneurs who underinvoice their export deliveries and who later get part of their export receipts from western partners in this form. This reduces their corporate tax and personal income tax liabilities. Convertible currency deposits of the population at Hungarian banks doubled within a year and reached US$1.3 billion at the end of June 1991.

Hungary's approach to privatization is to sell enterprises to investors rather than distributing them to the population via a voucher or other mass privatization scheme. The privatization of small businesses and the self-privatization of companies is proceeding successfully and on track. A setback with one large, visible deal, the delay of the sale of a state-owned hotel chain, illustrates some of the complexities that may arise in particular cases. The sale was delayed after the government ended tax breaks allowing enterprises to offset the cost of construction and capital improvements. Moreover, the NBH has insisted that the new owner of the chain must refinance subsidized loans obtained in the mid-1980s to finance construction at market rates.

CZECHOSLOVAKIA

Figure 19: Czechoslovakia: Relative Exposure by Creditor 1991





Source: Staff estimates based on IIF Country Reports

Gross convertible currency debt of US$8.1 billion at the end of 1990 was little changed from the end-1989 total of US$8.2 billion although substantial movements in the debt position took place during the year. The debt declined to US$7.0 billion at the end of June as the payments difficulties of Bulgaria and the USSR in early 1990 led western banks to withdraw short term deposits from CEE countries, including CSFR. *In addition, importers preferred to pay in cash rather than use or renew trade credits, or even prepay in anticipation of the preannounced devaluation.* The total convertible currency debt increased to US$8.8 billion at the end of June 1991 from US$8.1 billion at the end of 1990. Large, medium and long term disbursements from official creditors were partially offset by valuation effects from the appreciation of the dollar. Short term debt in contrast, continued to decline in 1991. The State Bank reports that the issuance of trade credits stabilized in 1991 after it declined steadily in 1990. Still, some Western banks continue to withdraw short term deposits.

Table 8: **CSFR External Debt (in US$ million)**

	1986	1987	1988	1989	1990	1991(e)	1992(f)
Convertible Currency External Debt of which	5,568	6,656	7,281	8,183	8,085	9,251	9,827
MLT	2,877	3,580	3.875	4,596	5,180	6,.808	7,444
ST	2,691	3,076	3,406	3,587	2,905	2,443	2,383
By Creditor							
IFIs	27	131	136	134	135	1,984	2,683
Bilateral	1,513	1,876	1,454	1,701	1,576	1,882	2,062
Commercial Banks of which	3,114	3,927	4,786	5,648	5,349	4,640	4,229
MLT	1,202	1,456	2,164	2,795	3,120	2,738	2,440
ST	1,912	2,471	2,622	2,853	2,228	1,902	1,789
Other Private Creditors	914	722	905	701	1,025	745	853
Reserves Excl. Gold	1,115	1,382	1,583	2,157	1,102	2,673	3,929
Deposits in BIS Banks	1.217	1,598	1,671	2,197	1,353	-	-

Source: IIF, Country Report dated November 22, 1991

Again, by creditor category the commercial banks have the largest exposure. Within the commercial claims, it is surprising that up to 1989 a larger amount is ST than MLT. This pattern does not hold when the overall hard currency indebtedness is taken into account.

Debt increased again in the second half of 1990 as a result of net new medium and long term borrowing plus substantial valuation effects. Short term debt continued to decrease throughout the second half of 1990 *in spite of administrative measures introduced in October to restrict cash payments for imports and encourage the use of customary trade credits*. By the end of 1990, short term debt had fallen to US$2.9 billion, or less than 36 percent of total debt, compared to US$3.6 billion, or more than 45 percent of total debt at the end of 1989.

The 1989 swing of the convertible currency account into deficit was largely financed by a US$1.1 billion drawdown of reserves. Net external borrowing totaled just US$0.3 billion as net new MLT borrowing was largely offset by US$0.6 billion in net short-term repayments. In the first half of 1991, the convertible currency trade balance moved into deficit by about US$500 million, compared with a surplus of almost US$50 million in 1990. The deterioration was due to the transfer of most payments for Soviet oil onto a convertible currency basis. The underlying growth of nonoil imports and exports was roughly balanced. The value of convertible currency imports soared almost 50 percent to US$4.1 billion in the first half of 1991 compared to a year ago, reflecting both payments of US$80-100 million a month for Soviet oil as well as import liberalization. First half exports rose almost 30 percent compared to the first half of 1990 to a dollar value of US$3.5 billion. The increase is attributable to some redirection of exports from eastern to western markets and to higher EC quotas for some products such as textiles.

Financing in 1991 came largely from official creditors for the first time.

Table 9: **CSFR External Financing Flows (in US$ million)**

	1989	1990	1991	1992
External Borrowing, Net of which	553	315	1,699	1,050
Commercial Banks	469	-271	-364	-17[illegible]
Disbursements	493	467	170	285
Repayments	-428	-315	-384	-461
ST Credits, net	-21	-423	-150	0
Other Private Creditors, Net	0	221	-201	167
Disbursements	340	480	147	266
Repayments	-269	-189	-398	-139
ST Credits, Net	-71	-70	50	40

Source: IIF, Country Report dated November 22, 1991

Following a small negative transfer to commercial banks in 1990, there was a net inflow of US$182 million in 1991, and this trend is expected to continue, although in a smaller amount for 1992. Inflows from other private creditors jumped in 1990, dropped sharply in 1991 and are expected to rise again in 1992.

Funds in 1990 were raised primarily by two bond issues in Germany (each DM 350 million) plus a private placement in Japan at the end of the year (¥ 5 billion). These funds are assumed by market experts to have come equally from commercial banks and other private investors. Joint ventures raised most of the remaining net MLT financing, much of it guaranteed by western export credit agencies. The State Bank reports that the net short term outflow was accounted for in roughly equal parts by the withdrawal of short term deposits and by the net repayment of short term trade credits.

The State Bank was expecting to issue a bond in mid-1991 if market conditions were propitious and if they could be confident of a positive reception. This would be the State Bank's first issue on its own after guaranteeing the two bond issues by Obchodni Banka in 1990. The State Bank finally ventured into the private capital market at the end of October 1991 with a US$200 million three year bond. The issue was in fact very well received. The State Bank of Czechoslovakia also issued ¥10 billion of six year private placement bonds in November 1991. In addition, the State Bank authorized more than 20 Czechoslovak companies to borrow US$120 million abroad in 1991. Another Samurai issue in dollars, in the amount of US$200 million was arranged by Nomura Securities with a three year maturity, in December 1991. (See Annex 1 for a summary of bond issues since 1990).

It is estimated that official bilateral creditors provided in net somewhat over US$300 million, and that other private creditors provided almost US$60 million net. Commercial banks appear to have received net repayments of almost US$100 million in 1990.

The use of trade credits was expected to increase in 1991, largely due to payments restrictions introduced in October 1990 to force importers to take up customary trade financing.

More unguaranteed trade financing, plus the State Bank bond issue, could bring net financing of almost US$200 million from commercial banks and almost US$100 million from other private creditors. In addition, direct investment flows are up sharply and may total US$450 million for 1991, much of it accounted for by the VW investment in Skoda Auto. The capitalization of newly permitted foreign bank operations accounted for another US$30 million. The combination of substantial direct foreign investment inflows, large disbursements of official credits

and the better than expected current account performance have allowed the authorities to replenish foreign exchange reserves from the end-1990 level of US$1.1 billion. Reserves increased to US$1.6 billion at end-June 1991 and to about US$2.2 billion at end-September.

Total convertible currency external debt increased to US$9.3 billion by the end of 1991. This represents a sharp increase from US$8.1 billion at end-1990, but is still comparatively low. Large medium and long-term disbursements from official creditors were partially offset by valuation effects from the appreciation of the dollar. Short-term debt, in contrast, has continued to decline. The State Bank reports that the use of trade credits stabilized in 1991 after declining steadily in 1990. However, some western banks appear to have continued to withdraw short-term deposits in the face of heightened uncertainty in the region. Amortization payments rose from US$800 million in 1990 to US$1.1 billion in 1991. However, the debt service ratio may not rise sharply if higher payments are offset by increased exports to the west, and by the gradual transfer of previously nonconvertible exports to a convertible currency basis.

Factors Influencing Greater Foreign Involvement in the Economy

Size of Private Sector

Private sector employment has grown, but is still below 10 percent of employment in the state and cooperative sectors. Privatization has been divided into two stages. The so called "small" privatization encompasses restaurants, services and other locally controlled businesses. The "small" privatization began in late January 1991. As of the end of the third quarter of 1991, 10,002 establishments in the Czech republic and 5,044 in Slovakia had been sold at auction. This represents between 10 and 15 percent of the establishments to be included in the "small" privatization.

The groundwork is also being laid for the so-called "large" privatization program. In the spring of 1991 each of the large enterprises involved began preparing a "privatization project" to be presented to the government by October 31 1991. These projects include an inventory, a valuation and a proposal for privatizing the company by any of the approved methods: limited block auctions to foreign interests, issuing shares through domestic or foreign flotations, preferential share distribution to employees, or the issue of domestic investment vouchers. Voucher coupon booklets have been available since October 1, 1991 at any post office to anyone for about US$1 equivalent. Citizens older than 18 can register their vouchers for a fee of about US$33 equivalent, a little more than one week's average wage, and use them as a means of payment for shares of government owned enterprises which have been converted to joint stock companies.

A list of 2500 companies has been published, including information about the amount and nominal value of shares to be offered for vouchers. The portion of these companies to be privatized by voucher is reported to average 30 percent. The price of the companies' shares is defined in voucher units, so-called "investment points". The process is to go forward in two waves, each of which comprise one list of state-owned companies for sale against one batch of vouchers issued. Within each wave, there will be several rounds designed to match supply and demand for an equilibrium price in terms of investment points.

In the first round, a price is more or less set arbitrarily by the government. If there is an excess supply of investment points at that price, no shares will be sold and the price will be raised in the next round. Each round is expected to last no longer than a month and one privatization wave is not expected to have more than five rounds. If fewer investment points are offered at the first round than shares available for sale, all orders are filled and the unsold remainder is offered at a lower price in the next round.

The voucher program has made specific allowance for mutual funds, known as Investment Privatization Funds. A "pre-round" period has been set aside, during which individual owners can sign over their registered vouchers to one of the many such funds in return for shares in the fund. These funds are likely to be attractive, given the limited information available about the companies. The government has made substantial efforts to publicize and explain its voucher program. Preliminary estimates indicated that fewer citizens planned to take part, relative to the 4 million the government expected. Promotion efforts have been intensified, and as of May 1991 it was reported that as many as 8.6 million people were involved. The main difficulty is that very little information is available on the financial condition of the companies on the voucher privatization list. Price determination in this context will remain imperfect and may produce false expectations. With solid information at such a high premium in entire process, safeguards against insider deals of many conceivable kinds will be difficult to implement.

Reorientation of Trade

The commodity composition of CMEA trade differed greatly from the pattern of trade with the west. Thus, redirecting trade depends on structural change and not just greater marketing efforts. In 1990 about one-half of the dollar value of total trade was with the west, up from about one-third in 1985. However, most of this change was caused by a decline in CMEA trade in 1990, rather than by a successful redirection from east to west. In the absence of such redirection, the loss of the Soviet market is having a major impact on production and employment.

Industrial production declined 3.9 percent in 1990 following modest growth of 0.9 percent in 1989. On the other

hand, official statistics probably overstate the decline in production since they give insufficient weight to small new firms. (At the beginning of 1991 the index was broadened to include enterprises employing 25 or more persons from the previous minimum of 100). Also, a 30 percent decline in real private consumption i n 1991 has been estimated by the Federal Statistical Office, but this is probably an overstatement since consumers stockpiled goods in 1990 in anticipation of the price liberalization.

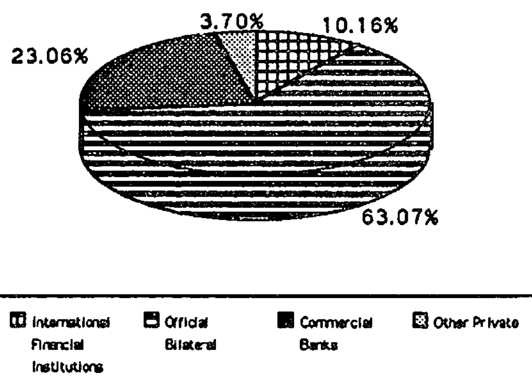
CSFR has taken the lead in negotiating new agreements to revive nonconvertible trade. This is in response to a shortage of convertible currencies in the former USSR, which prevents the orderly settlement of past imbalances in hard currency according to the agreement under which CMEA was dismantled in January 1991. Early in 1991, an agreement was signed with the USSR providing for mutual trade (excluding energy) equal to about 30 percent of the 1990 level. Subsequent arrangements have focused on bilateral deals with individual republics and producers.

Performance of Domestic Banking Sector

The two new commercial banks extended less credit than was allowed under the restrictive credit ceilings in the first quarter of 1991. This seems to have been largely due to their reluctance to extend any new credits to state enterprises whose continued existence is uncertain, and to new private entrepreneurs in the absence of a bankruptcy law. Following protests by state enterprises about the lack of credit availability, the State Bank relaxed slightly the regulations governing borrowing abroad. Companies were encouraged to make full use of normal trade-related foreign credits. In addition they may now take up foreign credits, with the permission of the State Bank on a case by case basis. In addition, at least two foreign banks have been granted licenses to do full banking business in CSFR.

POLAND

Figure 20: Poland - Relative Exposure by Creditor - 1991



Source: Staff estimates based on IIF Country Reports.

In February 1990, Paris Club creditors agreed to reschedule 100 percent of principal and interest arrears due through March 1991. This agreement in large measure contributed to net official bilateral financing of US$2.4 billion in 1990. Disbursements of new credits amounted to US$215 million only. Repayments of less than US$100 million were made to the US commodity Credit Corporation on loans not covered by the Paris Club rescheduling.

Negotiations with commercial banks remained deadlocked throughout 1990, and resulted in the accumulation of US$1.3 billion in total arrears to commercial banks by May 1991. Negotiations continued to be protracted in 1991, and further interest arrears of US$850 million were accumulated in the course of the year. The short-term trade facilities with commercial banks were serviced and remained available.

For the entire year of 1991, Poland is likely to have received about US$1 billion in new medium and long-term disbursements mostly from international financial institutions and official bilateral creditors. The new credits combined with the rescheduling of interest due in the first quarter to the Paris Club and the accumulation of interest arrears to commercial banks resulted in total net external borrowing of US$2.1 billion in 1991. This more than offset the current account deficit of US$1.9 billion (after Paris Club interest payment reduction). No new lending from commercial banks is foreseen prior to an agreement.

The tiny proportion of short term debt both in overall debt and in commercial debt alone, even as far back as 1986 is remarkable, given the situation in CSFR, a neighbor. In fact, the table shows that in all years except 1989, the entire ST obligations were owed to commercial banks. Other private creditors have experienced no debt servicing problems.

Table 10: **Poland: External Debt (in US$ million)**

	1986	1987	1988	1989	1990	1991	1992
Convertible Currency External Debt of which	33,528	39,249	39,165	41,387	49,019	50,780	50,700
MLT	30,593	37,749	37,133	37,061	46,625	47,676	46,891
ST	1,392	1,500	1,450	1,295	1,339	1,384	1,302
By Creditor							
IFIs	2,641	2,815	2,614	2,631	3,288	3,976	5,162
Bilateral	20,337	24,901	25,862	28,634	33,385	33,612	32,190
Commercial Banks of which	8,617	9,529	8,856	8,580	10,627	11,438	11,767
MLT	7,225	8,029	7,406	7,360	8,386	8,335	7,958
ST	1,392	1,500	1,450	1,080	1,339	1,384	1,302
Interest Arrears	0	0	0	140	901	1.720	2,507
Other Private Creditors	1,933	2,004	1,833	1,542	1,720	1,753	1,581
Interest Arrears	0	0	0	0	0	0	0
Reserves excl. Gold	698	1,495	2,055	2,314	4,492	3,968	4,069
Deposits in BIS Banks	1,721	2,995	3,619	3,929	7,762	-	-

Source: IIF, Country Report, dated November 3, 1991

For all of 1990, the combination of a Paris Club rescheduling, the accumulation of interest arrears and new credits permitted Poland to accumulate total foreign exchange assets of US$5.5 billion. Approximately US$2.2 billion of this was recorded as an increase in official reserves, with the remainder being deposited by Polish banks with banks abroad. This should give Polish banks the ability to generate trade "credits" on a fully covered basis. In fact, it is reported by a reliable source in the market that Polish commercial banks are becoming heavily involved in project finance and commodity financing in Poland. A number of them are involved in channelling (small amounts of) hard currency credits to the emerging private sector.

Table 11: **Poland's External Financing Flows (in US$ million)**

	1990	1991(e)	1992(f)
External Financing, Net of which	3,885	2,135	2,490
Commercial Banks	796	850	855
Disbursements	0	0	0
Repayments	0	0	0
Due	0	-345	-160
Rescheduled/Postponed	0	345	160
ST Credits, Net	0	0	0
Interest Arrears	796	850	855
Other Private Creditors, Net	103	40	-115

Source: IIF, Country Report, dated November 3, 1991

Factors Influencing Foreign Involvement in the Economy

Impact of Private Sector

The decline of industrial production has been broad-based. Output in the machine building and metallurgy sectors was hardest hit, while production in food processing and wood/paper sectors showed strong growth reflecting in part an increase of exports to western countries. Growth of output in the private sector has been buoyant, although measurement problems make it difficult to quantify.

Government hopes for speeding up the privatization process rest mostly on the implementation of a scheme involving the issuance of vouchers to the public. Holders will deposit the vouchers with investment funds which will use them to bid for shares at auctions. In this way, investor risk is to be reduced. The government also hopes to accelerate privatization through a substantial relaxation of existing legislation which requires the approval of the Foreign Investment Agency for a foreign equity stake of more than 10 percent.

Despite more than 3000 joint ventures with foreign partners having been approved, foreign direct investment has remained insignificant so far. The uncertain political situation combined with continued confusion about property laws has dampened the confidence of foreign investors. A revised Foreign Investment Act came into effect in July 1991, which eliminates the minimum investment amount, guarantees the repatriation of 100 percent after-tax profits and guarantees compensation for all losses resulting from expatriation.

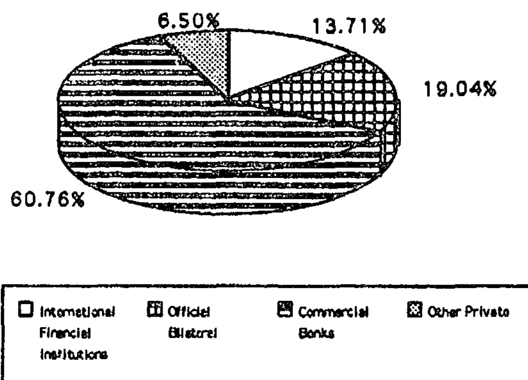
Reorientation of Trade

The severe contraction in domestic demand led enterprises to seek external markets both in the west and in the CMEA area. The value of convertible currency exports jumped about 43% in 1990 and in volume terms nearly 49%. A large part of the increase was with France, Italy and Germany. Imports in the final quarter of 1990 represented 46% of the total imports for the year, and were nearly 90% higher than in the corresponding quarter of 1989. Oil imports in convertible currency were substituted for delivery shortfalls from the Soviet Union, but shipments of other goods were also accelerated because of concern over a possible devaluation of the zloty. Nonconvertible currency import volume declined more than 30 percent.

In December 1991, Poland signed an association agreement with the European Community, effective as of January 1, 1992. The accord foresees the gradual phasing out of cusoms barriers on trade in industrial goods over the next seven years. Starting in 1992, Poland will remove customs duties on goods making up 27% of its imports from the EC which in turn will remove duties on 64% of its imports from Poland. The agreement leaves removal of farm trade barriers to further talks, but the Polish Government was able to negotiate cuts in custom dues on more than half of the value of food exports to the EC.

BULGARIA

Figure 21: Bulgaria - Relative Exposure by Creditor - 1991



Source: Staff estimates based on IF Country Reports

Throughout 1990 there was a severe shortage of foreign exchange at the disposal of the government. This was further exacerbated by the suspension of trade financing from western creditors, and imports fell even more sharply than exports. The value of convertible currency imports was 24 percent lower in 1990 than in 1989. The convertible currency trade deficit therefore narrowed to US$800 million in 1990, from US$1.2 billion in 1989. At the same time, about US$900 million in interest payments (including interest on rolled over maturities) were due, of which some US$300 million were paid before the June 1990 moratorium. The reduction in the trade deficit was almost offset by the increase in the invisibles deficit, and so the overall convertible currency current account balance posted a deficit of US$1.25 billion, very slightly smaller than the US$1.3 billion deficit in 1989.

External financing came to a virtual halt after the June moratorium. Practically no new money came from former multilateral creditors. Principal and interest payments to both official bilateral creditors and to commercial banks ran into arrears. Of the estimated US$360 million in principal due to official bilateral creditors, only US$70 million were paid. About US$80 million in interest arrears were accumulated. An estimated US$1 billion was owed to commercial banks, of which some US$270 million were paid. Almost US$280 million accumulated in interest arrears.

Debt repayments by developing countries to Bulgaria amounted to about US$200 million in 1990, but there was also an outflow of about US$300 million from Bulgarian commercial banks and enterprises as they increased their assets abroad.

The difficult external financial situation and the large current account deficit led to a rapid depletion of official foreign exchange reserves. According to the authorities, official reserves (excluding gold) fell from US$1 billion at end-1989 to less than US$140 million at the end of March 1990, with little change until the end of 1990.

Table 12: **Bulgaria's External Debt (in US$ million)**

	1986	1987	1988	1989	1990(e)	1991(f)	1992(f)
Convertible Currency External Debt	5,218	7,081	8,889	10,224	11,030	12,122	13,374
of which MLT	3,695	5,070	6,475	7,520	7,402	7,864	8,415
ST	1,523	2,011	2,414	2,704	3,272	3,125	3,054
Interest Arrears	0	0	0	0	357	1,133	1,905
By Creditor							
IFIs	310	490	700	660	752	1,517	2,150
Bilateral	1,519	1,620	1,703	1,238	1,063	1,169	1,380
Commercial Banks	3,362	4,599	6,111	7,256	8,223	8,626	9,071
of which MLT	2,146	2,978	4,178	4,924	5,057	4,886	4,752
ST	1,216	1,621	1,933	2,332	2,881	2,775	2,663
Interest Arrears	0	0	0	0	285	965	1,656
Other Private Creditors	27	372	375	1,070	993	810	773
Interest Arrears	0	0	0	0	0	0	0
Reserves excl. Gold	1,182	850	1,462	1,013	125	544	757
Deposits in BIS Banks	1,381	1,085	1,780	1,176	653	-	-

Source: IIF, Country Report, dated November 19, 1991

However, deposits in BIS-reporting banks throughout 1990 amounted to about US$630 million at the end of March, US$570 million at the end of June, and US$590 million at the end of September. The difference between Bulgarian BIS deposits and official reserves might reflect foreign exchange earnings kept abroad by Bulgarian enterprises reluctant to surrender earnings to the authorities.

No new commercial lending is foreseen until the government is ready to assume responsibility for the debt outstanding.

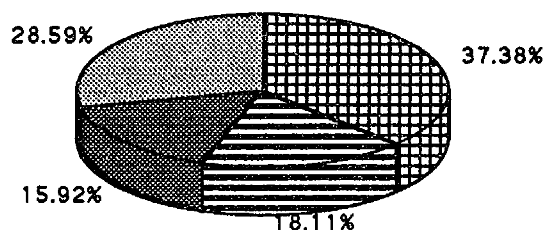
Table 13: **Bulgaria's External Financing Flows (in US$ million)**

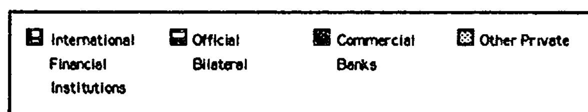
	1987	1988	1989	1990	1991	1992(f)
External Borrowing, Net of which	1,009	2,181	1,299	202	1,450	1,590
Commercial Banks	530	1,501	1,114	497	685	700
Disbursements	916	1,260	2,363	212	0	0
Repayments	-282	-416	-1,637	-383	0	0
Due	-282	-416	-1,637	-2,033	-1,030	-663
Rescheduled/Postponed			0	1,650	1,030	663
ST Credits, Net	-103	657	388	374	0	0
Interest Arrears	0	0	0	294	685	700
Other Private Creditors	296	146	675	-140	-150	-15
Disbursements	53	140	669	213	10	40
Repayments		-33	-87	-342	-152	-58
Due		-33	-87	-342	-152	-58
Rescheduled/Postponed	0	0	0	0	0	0
ST Credits, Net	243	39	93	-12	-8	-3
Interest Arrears	0	0	0	0	0	0

Source: IIF, Country Report, dated November 19, 1991

ROMANIA

Figure 22: Romania - Relative Exposure by Creditor - 1991





Source: Staff estimates based on IIF Country Reports.

The external balance of payments deteriorated sharply in 1990 as production declined and consumption increased. The convertible currency current account swung into a deficit of US$1.7 billion from a surplus of US$2.6 billion in 1989. Convertible currency foreign exchange reserves were almost depleted. The expected current account deficit for each of 1991 and 1992 is expected to be US$1.5 billion. Financial support for the program is expected to come from the official sector, with commercial bank lending likely to be modest.

The volume of convertible currency imports rose substantially in 1990 as the government sought to make up for production shortfalls and meet increased consumption demand. Imports of consumer goods jumped by more than 600 percent, and imports of raw materials also rose sharply. The dollar value of total convertible currency imports increased by more than 50 percent from 1989 to 1990, to US$5.1 billion. At the same time, the dollar value of convertible currency exports fell by 42 percent to US$3.5 billion.

The deterioration of the convertible currency current account balance was in part precipitated by the Gulf crisis. The dollar value of net oil imports increased from US$250 million in 1989 to almost US$1.1 billion in 1990. (Romania is an oil producing country).

The convertible currency current account deficit of US$1.7 billion was financed almost entirely by drawing down reserves. Official reserves (excluding gold) fell by US$1.6 billion in 1990 from US$1.9 billion at the end of 1989. No financing was provided by multilateral financial institutions in 1990. About US$40 million came from official bilateral creditors, while some US$100 million of short term trade credits were repaid to commercial banks. The total net outflow to external creditors seems to have been about US$50 million.

Total external debt was about US$500 million at the end of 1990, little changed from 1989. Most of the debt consisted of short term trade credits, with about 40 percent of the total owed to commercial banks. Official reserves amounted to about US$200 million, equivalent to about two weeks of imports.

Total external financing commitments could reach about US$2.1 billion for all of 1991. Most of the new money would come from multilateral lenders. The majority of the inflows from bilateral creditors are likely to be in the form of government guarantees of suppliers' credits. According

Table 14: **Romania: External Debt (in US$ million)**

	1986	1987	1988	1989	1990	1991	1992
Convertible Currency							
External Debt	6,592	6,859	2,798	582	518	2,151	3,794
of which MLT	5,649	6,063	2,605	269	167	1,166	2,785
ST	943	796	193	313	352	985	1,009
By Creditor							
IFIs	2,672	2,670	905	0	0	1,059	2,238
Bilateral	1,483	1,945	1,257	284	266	513	740
Commercial Banks	2,334	2,144	536	248	252	451	570
of which MLT	1,615	1,765	441	1	0	20	45
ST	719	379	95	247	252	431	525
Other Private Creditors	103	100	100	50	0	128	247
Reserves excl. Gold	582	1,402	780	1,859	524	838	1,177
Deposits in BIS Banks	638	1,387	811	1,843	584	-	-

Source: IIF, Country Report dated, November 20, 1991

to authorities, credit lines from western governments already amount to some US$600 million, but lack of proper investment projects have delayed their disbursement, and the likelihood is that no more than US$300 million would be disbursed in 1991.

Lending by commercial banks is still limited. A syndicated loan of US$100 million with a one year maturity was reportedly under preparation in May 1991, but has since been delayed due to political developments. The borrower would be the Romanian Bank for Foreign Trade, with the loan being guaranteed by the National Bank of Romania. The loan was to have been conditioned on the successful implementation of the IMF program and the disbursement of the last tranche of the standby arrangement in early 1992.

Convertible currency external debt could rise to US$2.6 billion by end-1991. Most would be MLT and owed to official creditors. Foreign exchange reserves could rise from US$0.2 billion to US$0.9 billion, which would be equivalent to 1.' months of imports of goods and services.

Table 15: **Romania's External Financing Flows (in US$ million)**

	1988	1989	1990	1991	1992
External Borrowing, Net	-3,595	-1,695	-77	1,620	1,725
of which					
Commercial Banks	1,582	-278	-6	200	125
Disbursements	0	5	-1	20	25
Repayments	1,320	-432	0	0	0
Due	-247	-95	0	0	0
Pre-payments	-1,073	-337	0	0	0
ST, net	-262	149	-5	180	100
Other Private Creditors, Net	-5	-14	-52	125	125
Disbursements	23	26	0	75	75
Repayments	-51	-29	-29	0	0
ST Credits, Net	23	-11	-23	50	50

Source: IIF, Country Reports.

ANNEX 1

PRESENCE OF CEE IN THE INTERNATIONAL CAPITAL MARKETS

Czechoslovakia:

Bond Issues in:
1990 and 1991

Size/Issue Price	Issuer	Maturity	Coupon/Yield	Lead Manager	Guarantee	Type of Bond
DM 250m/100.75	Obchodni Banka	7/90-8/95	10.0%/N.A.	Commerzbank	Unsecured	EURO
DM350m/101	Obchodni Banka	9/90-10/95	10.0%/N.A.	Deutsche Bank	Unsecured	EURO
Y 5 bn/100	Obchodni Banka	12/90-12/95	8.30%	Yamaichi LTCB		SAMURAI/PP
US$200m/99.61	Statni Banka	11/91-11/94	9.0%/9.152%	Nomura		EURO
Y 10 bn/100	Obchodni Banka	11/91-11/97	8.50%	Nomura		SAMURAI/PP
US$ 200m/99.61	Statni Banka	12/91-12/94	9.00%	Nomura		EURO

Hungary:

Bond Issues:
1989, 1990 and 1991

Size/Issue Price	Issuer	Maturity	Coupon/Yield	Lead Manager	Guarantee	Type of Bond
DM200m/100	National Bank of Hungary	2/89-2/96	6.625%/NA	Bayerische Vereinsbank International	NA	EURO
Y10bn/100	National Bank of Hungary	2/89-3/96	6.4%/NA	IBJ	NA	SAMURAI/PP
DM200m/100	National Bank of Hungary	2/89-6/97	8.0%/NA	DG Bank	NA	EURO
Y40bn/99.65	National Bank of Hungary	3/89-10/97	6.3%/NA	Daiwa Securities	NA	SAMURAI/PP
Y30bn/100.5	National Bank of Hungary	3/89-10/98	5.9%/NA	Daiwa Securities	NA	SAMURAI/PP
Y20bn/100	National Bank of Hungary	3/89-2/97	5.7%/NA	Daiwa Securities	NA	SAMURAI/PP
Y25bn/99.75	National Bank of Hungary	3/89-3/98	5.7%/NA	Daiwa Securities	NA	SAMURAI/PP
Y35bn/100.9	National Bank of Hungary	3/89-3/99	5.7%/NA	Daiwa Securities	NA	SAMURAI/PP
Y25bn/100.5	National Bank of Hungary	3/89-9/99	6.0%/NA	Daiwa Securities	NA	SAMURAI/PP
ECU75m/101.88	National Bank of Hungary	9/89-9/96	10.0%/NA	Kredietbank SA, Luxembourg	NA	EURO
ASch1500m/NA	National Bank of Hungary	9/89-9/96	8.25%/NA	Oesterreichische Laenderbank	NA	NA
Y25bn/100.5	National Bank of Hungary	9/89-9/99	6.0%/NA	Daiwa Securities	NA	SAMURAI/PP
DM300m/100	National Bank of Hungary	2/90-2/97	10.0%/NA	Commerzbank	NA	EURO
ASch1000m/99.45	National Bank of Hungary	2/90-2/97	9.5%/NA	Creditanstalt Bankverein	NA	EURO
DM200m/100	National Bank of Hungary	5/90-5/96	9.75%/NA	DG Bank Deutsche Genossenschaftsbank	NA	EURO
US$200m/99.6	State Development Institute	8/90-8/00	10.5%/NA	Daiwa Europe	Govt. Guarantee	EURO
ASch500m/99	National Bank of Hungary	9/90-9/97	10.75%	Oesterreichische Laenderbank	NA	EURO
Y15bn/100.5	National Bank of Hungary	11/90-11/95	9.0%/8.86%	Daiwa Securities		
Y10bn/100.8	National Bank of Hungary	11/90-11/95	9.0%/8.77%	Daiwa Securities		
DM200m/99.75	National Bank of Hungary	3/91-3/96	10.5%/11.11%	Commerzbank	NA	EURO
DM150m/100	National Bank of Hungary	4/91-4/96	10.5%/NA	Commerzbank	NA	EURO
DM200m/NA	National Bank of Hungary	5/91 (paper maturities are variable: 2-30 years)	Fixed, floating and zero coupon	Deutsche Bank	NA	EURO
SFr30m/100.5	Phoenix	6/91-6/98	7.00%	Bank Leu	NA	Straight/ Private
US$100m/97.2	National Bank of Hungary	7/91-7/96	10.5%/11.263%	Bankers Trust	NA	EURO
ECU200m/99.125	National Bank of Hungary	9/91-9/96	12.00%	CFSB		EURO
DM500m/100.5	National Bank of Hungary	10/91-10/98	10.75%	Dresdner Bank		EURO
Y20bn/100.5	National Bank of Hungary	10/91-10/98	8.7%-8.58%	Daiwa Securities		
Y30bn/100.6	National Bank of Hungary	12/91-12/2001	8.00%	Daiwa Securities		Samurai/Public
Y30bn/101	National Bank of Hungary	1/92-1/2002	7.0%/6.83%	Daiwa Securities		Samurai/Public
DM600m/100.25	National Bank of Hungary	1/92-1/99	10.25%	Deutsche Bank	Non callable: Fees 2.25/ 1.375	

Source: Based on information compiled by Frank Burdette - CFSPS

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