COMMISSION OF THE EUROPEAN COMMUNITIES

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REPORT FROM THE COMMISSION TO THE COUNCIL AND THE EUROPEAN PARLIAMENT

ON GUARANTEES

COVERED BY THE GENERAL BUDGET -

SITUATION AT 31 DECEMBER 1992

This report describes the situation as regards budget guarantees at 31 December 1992.

It is in response to the statement made by the Commission, when the vote was taken on supplementary and amending budget No 1/91, that it would report to the budgetary authority twice a year on budget guarantees and the corresponding risks.

The Commission has already presented three reports to the budgetary authority.

The report is in three parts:

1. Description of operations entered in the budget and events since the last report.

2. Situation at 31 December 1992 as regards risks for the budget in future years and guarantees already activated.

3. Assessment of the economic and financial situation of non-Community countries benefiting from the most important operations.

PART ONE: OPERATIONS ALREADY ENTERED IN THE BUDGET

At 31 December 1992 the budgetary authority had authorized 21 headings with token entries in the 1993 budget, including six new headings for operations in favour of Bulgaria, Romania, Latvia, Estonia and Lithuania and EIB loans in non-member countries. These headings can be divided into three categories: borrowing and lending within the Community, borrowing and lending outside the Community and guarantees given to financial institutions.

I. BORROWINGS TO BE ON-LENT WITHIN THE COMMUNITY

A. COMMUNITY BORROWING OPERATIONS TO PROVIDE BALANCE-OF-PAYMENTS SUPPORT

The Community is authorized to borrow on the capital markets or from financial institutions and make the sums raised available to Member States experiencing temporary balance-of-payments difficulties.

The outstanding amount of loans granted to Member States for this purpose may not exceed ECU 14 billion in principal.

At 31 December 1992 the only operations involved were the two in respect of Greece under the decisions of 9 December 1985 and 4 March 1991.

At 31 December 1992 the amount outstanding in loans to Greece was ECU 1.875 million (Table 1).

B. EURATOM BORROWING OPERATIONS

In 1977 the Commission was empowered to borrow funds to be used to help finance nuclear power stations.

Loans are made to electricity producers and carry the usual guarantee demanded by banks. Recipients are often State-owned companies or companies enjoying a State guarantee.

The maximum amount of borrowings authorized is ECU 4 billion, of which ECU 500 million was authorized by the 1977 decision, ECU 500 million in 1980, ECU 1 billion in 1982, ECU 1 billion in 1985 and ECU 1 billion in 1990. At 31 December 1992 the amount of borrowings contracted came to ECU 2 768,8 million.

At 31 December 1992 the total of borrowings outstanding was ECU 1 338 million.

On 9 December 1992 the Commission proposed that the balance of borrowings not used in the Member States could be used to finance the improvement of the degree of efficiency and safety of nuclear power stations in the countries of Central and Eastern Europe and in the CIS.

A maximum of ECU 1 124 million could be allocated.

C. BORROWING OPERATIONS FOR THE PROMOTION OF INVESTMENT IN THE COMMUNITY

The Commission was empowered by a Council Decision of 16 October 1978 to borrow funds to be used to promote investment in the Community (New Community Instrument).

The authorized borrowing ceiling was fixed at ECU 1 billion by the Decision of 16 October 1978 and was then raised by ECU 1 billion by the Decision of 15 March 1982. The ceiling was further raised by ECU 3 billion by the Decision of 19 April 1983 and by ECU 750 million by the Decision of 9 March 1987.

The proceeds of the operations are paid out in the form of loans granted by the EIB, acting for the Commission, to finance investment projects which contribute to greater convergence and growing integration and are consistent with the priority Community objectives in the energy, industry and infrastructure sectors, taking account of such factors as the regional impact of the projects and the need to combat unemployment. Support for small businesses was also made a priority objective by the Decision of 26 April 1982.

A Decision of 20 January 1981 also empowered the Community to contract loans in order to provide exceptional aid of ECU 1 billion to the regions of Italy affected by the earthquake of November 1980. A similar decision involving ECU 80 million was adopted on 14 December 1981 for the regions affected by the earthquakes in Greece in February/March 1981.

The maximum amount of borrowings authorized thus comes to ECU 6 830 million.

At 31 December 1992 the total outstanding was ECU 3 324 million, 15.9% less than on 31 December 1991.

The risk is spread over a large number of borrowers. In addition, most of the loans are global loans to financial institutions which guarantee repayment of the funds.

Every year the EIB provides the Commission with a list of debtors who, according to its information, risk defaulting in the coming year. So far, no names have been recorded on this list.

II. LOANS RAISED FOR ON-LENDING TO NON-COMMUNITY COUNTRIES

A. PROGRAMME OF BORROWINGS CONTRACTED BY THE COMMUNITY TO PROVIDE MEDIUM-TERM FINANCIAL ASSISTANCE TO HUNGARY (Hungary I)

The Community is granting Hungary a medium-term loan of up to ECU 870 million in principal for a maximum of five years. The loan is intended to facilitate the adjustment of the Hungarian economy in a way which will enable it to derive all the benefits of a market-based economy. It is being made available in tranches.

The first tranche of ECU 350 million was paid on 20 April 1990. A second tranche of ECU 260 million was paid on 14 February 1991. The third tranche, which is not to exceed ECU 260 million, was planned for 1992 but will probably not be paid out now that Hungary's balance of payments is more favourable than expected. The tranches will be repaid in one instalment after five years and interest, which is at variable rates, is payable annually.

B. ADDITIONAL MEDIUM-TERM FINANCIAL ASSISTANCE TO HUNGARY (Hungary II)

As the break-up of the Council for Mutual Economic Assistance (Comecon) and the Gulf crisis threatened to compromise the initial encouraging results of the reforms undertaken, it was decided to launch a supplementary borrowing and lending operation for ECU 180 million under an overall ECU 360 million G-24 aid programme.

The first tranche of ECU 100 million was paid on 14 August 1991. It will be repaid in one instalment after seven years, and interest, which is at variable rates, is payable annually. The second tranche of ECU 80 million was due to be paid on 15 January 1993.

C. BORROWING CONTRACTED BY THE COMMUNITY TO PROVIDE MEDIUM-TERM FINANCIAL ASSISTANCE FOR THE CZECH AND SLOVAK FEDERAL REPUBLIC

As part of G-24's total aid of around ECU 750 million, the Commission, on behalf of the Community, is empowered to borrow, in two tranches, ECU 375 million for a period of seven years. The proceeds of this operation will be on-lent on the same terms to the Czech and Slovak Federal Republic.

The first tranche of ECU 185 million was paid on 14 August 1991. It will be repaid in one instalment after seven years, and interest, which is at variable rates, is payable annually.

The second tranche of ECU 190 million was paid on 2 March 1992 and will be repaid in one instalment after six years.

Following the division of Czechoslovakia into the Czech Republic and the Slovak Republic on 1 January 1993, the status of the Community loan is being discussed by the authorities of the two Republics and the Commission.

D. BORROWING CONTRACTED BY THE COMMUNITY TO GRANT BULGARIA MEDIUM-TERM FINANCIAL ASSISTANCE

As part of G-24's total aid of ECU 580 million, the Commission, on behalf of the Community, is empowered to borrow, in two tranches, ECU 290 million for a period of seven years. The proceeds of this operation will be on-lent on the same terms to Bulgaria.

The first tranche of ECU 150 million was paid to Bulgaria on 14 August 1991. It will be repaid in one instalment after seven years, and interest, which is at variable rates, is payable annually.

The second tranche of ECU 140 million was paid on 2 March 1992 and will be repaid in one instalment after six years.

E. BORROWING CONTRACTED BY THE COMMUNITY TO GRANT BULGARIA ADDITIONAL MEDIUM-TERM FINANCIAL ASSISTANCE

Following Parliament's favourable opinion of 17 September 1992, the Council decided on 19 October 1992 to grant additional financial assistance to Bulgaria under the new G-24 aid package of ECU 220 million.

The Community will be lending a maximum of ECU 110 million in two tranches.

The maximum term of the loan is to be seven years.

The operation should start in the course of 1993.

F. BORROWING CONTRACTED BY THE COMMUNITY TO GRANT ISRAEL MEDIUM-TERM FINANCIAL ASSISTANCE

As part of the financial assistance agreed by the Council for Israel and the population of the occupied territories following Parliament's favourable opinion, the Commission is empowered to borrow, on behalf of the Community, ECU 160 million in one tranche for a period of seven years. The proceeds will be paid out to Israel on the same terms and will be accompanied by an interest subsidy of ECU 27.5 million paid from the Community budget.

This operation started on 2 March 1992. The borrowing is to be repaid in full on 15 December 1997.

G. BORROWING CONTRACTED BY THE COMMUNITY TO GRANT ROMANIA MEDIUM-TERM FINANCIAL ASSISTANCE

This new operation was approved by the Council on 22 July 1991 after Parliament delivered a favourable opinion on 17 May 1991 and involved the entry of a specific guarantee heading in the budget by means of supplementary and amending budget No 2/91 which was finally adopted on 23 December 1991. The operation involves the borrowing and lending of ECU 375 million for a maximum period of seven years. It will be paid in two tranches. The first tranche of ECU 190 million was disbursed in January 1992 for a period of six years. The second tranche was paid on 2 March 1992.

H. BORROWING CONTRACTED BY THE COMMUNITY TO GRANT ROMANIA ADDITIONAL MEDIUM-TERM FINANCIAL ASSISTANCE

Following Parliament's favourable opinion of 17 November 1992, the Council decided on 27 November 1992 to grant further financial assistance to Romania under the new G-24 aid package of ECU 160 million.

The Community will be lending a maximum of ECU 80 million for a maximum of seven years.

In view of its size, the loan will be paid out in a single tranche in the course of 1993.

I. BORROWING CONTRACTED BY THE COMMUNITY TO GRANT ALGERIA MEDIUM-TERM FINANCIAL ASSISTANCE

This operation was adopted by the Council on 23 September 1991 after Parliament delivered a favourable opinion on 12 July 1991 and the specific guarantee heading was entered in the budget by means of supplementary and amending budget No 2/91, which was finally adopted on 23 December 1991. The operation involves the borrowing and lending of ECU 400 million in two tranches of ECU 250 million and ECU 150 million. A bridging loan was granted on 23 December 1991 to cover the first tranche of ECU 250 million before arrangements were made to contract the corresponding borrowing in January 1992. The second tranche has not yet been paid.

J. BORROWING CONTRACTED BY THE COMMUNITY TO GRANT MEDIUM-TERM FINANCIAL ASSISTANCE TO THE SOVIET UNION AND/OR ITS REPUBLICS

The Commission has proposed a medium-term loan of up to ECU 1 250 million for the Soviet Union and/or its Republics in order to finance imports of agricultural products, foodstuffs and medicines from the Community and Eastern Europe.

Parliament delivered a favourable opinion and the Council adopted its formal decision on 16 December 1991. The guarantee heading was set up when the 1992 budget was adopted in December 1991.

The loan will be divided between the various Republics of the former Soviet Union for a maximum period of three years.

The first loan contracts were signed in July 1992:

- with Armenia (ECU 38 million), Kyrgyzstan (ECU 32 million), Turkmenistan (ECU 45 million) and Moldova (ECU 27 million) on 10 July 1992;

- with Ukraine (ECU 130 million) on 13 July 1992;

- with Belarus (ECU 102 million), Tajikistan (ECU 55 million) and Georgia (ECU 70 million) on 24 July 1992;

- with Russia (ECU 150 million) on 9 September 1992;

- with Russia (ECU 349 million) on 9 December 1992;

- with Kazakhstan (ECU 25 million) on 15 December 1992.

The first loans were disbursed in late 1992 and the amount outstanding at 31 December came to ECU 123 million.

K. BORROWING CONTRACTED BY THE COMMUNITY TO GRANT MEDIUM-TERM FINANCIAL ASSISTANCE TO ESTONIA, LATVIA AND LITHUNIA

Following Parliament's favourable opinion of 30 October 1992, the Council decided on 23 November 1992 to grant financial assistance to these three countries under the G-24 aid package.

The loans will be paid in two separate tranches for each of the three States.

They should be paid out in the course of 1993 for a maximum of seven years.

The maximum to be granted is:

- ECU 40 million for Estonia;
- ECU 80 million for Latvia;
- ECU 100 million for Lithuania.

III. COMMUNITY GUARANTEE TO NON-COMMUNITY COUNTRIES

A. EUROPEAN INVESTMENT BANK LOANS TO MEDITERRANEAN COUNTRIES GUARANTEED BY THE GENERAL BUDGET

Under the terms of the Council Decision of 8 March 1977, the Community guarantees loans to be granted by the European Investment Bank as part of the Community's financial commitments towards the Mediterranean countries.

This decision was the basis for the contract of guarantee signed by the European Economic Community and the European Investment Bank on 30 October 1978 in Brussels and 10 November 1978 in Luxembourg introducing a global guarantee of 75% of all credit lines made available for loans in the following countries: Portugal (Financial Protocol, pre-accession aid), Greece, Spain (financial cooperation), Malta, Tunisia, Algeria, Morocco, Turkey, Cyprus, Egypt, Jordan, Syria, Israel, Yugoslavia and Lebanon.

In addition, by way of exception, a 100% guarantee covers loans allocated for emergency aid to Portugal in accordance with the Council Decision of 7 October 1975.

A new extension of the contract of guarantee is established for each new Financial Protocol.

The loans authorized at 31 December 1992 total ECU 7 517 million, of which ECU 1 500 million is for Spain, Greece and Portugal and ECU 6 017 million for the non-member Mediterranean countries. At 31 December 1992 the total of outstanding loans came to ECU 2 089 million, of which ECU 645 million was accounted for by Spain, Greece and Portugal and ECU 1 444 million by the non-member Mediterranean countries.

However, as the global guarantee for most of these operations is 75%, the budget risk is no higher than ECU 3 269.2 million. Of this total, ECU 1 134 million is accounted for by loans to Spain, Greece and Portugal, which have all been granted to State bodies or are covered by a State guarantee.

When the signature of a fourth series of protocols is taken into account, the breakdown of authorizations by country (non-member countries only) is as follows:

	Old protocols	4th protocols Authorizations	Total
Algeria	360	280	640
Cyprus	92		92
Egypt	492	310	802
Israel	133	82	215
Jordan	118	80	198
Lebanon	177	45	222
Malta	55		55
Morocco	297	220	517
Syria	208		208
Tunisia	250	168	418
Turkey	90		90
Yugoslavia[1]	760	730	760
	3 032	1 185	4 217

The second protocol with Yugoslavia was suspended on 25 November 1991 but the EIB was asked to resume operations in Bosnia-Hercegovina, Croatia, Macedonia, Montenegro and Slovenia as part of the programme of positive measures.

There is also provision for EIB loans outside these protocols under Council Regulation (EEC) No 1763/92 of 29 June 1992 concerning financial cooperation in respect of all Mediterranean non-member countries.

EIB loans under this operation must not exceed ECU 1 800 million.

The loans are generally for 15 years with 3 to 4-year periods of grace on capital repayments.

1 The second protocol with Yugoslavia was suspended when ECU 100 million of credits were still to be agreed and ECU 290 million of credits agreed were still to be disbursed.

B. LOANS GRANTED BY THE EUROPEAN INVESTMENT BANK IN COUNTRIES OF CENTRAL AND EASTERN EUROPE

In response to a call made by the Council on 9 October 1989, the Board of Governors of the European Investment Bank decided on 29 November 1989 to authorize the Bank to provide loans from its own resources to finance investment projects in Hungary and Poland for a total amount not exceeding ECU 1 billion. These loans are granted to finance investment projects which satisfy the Bank's usual requirements for loans from its own resources. The contract of guarantee was signed on 24 April 1990 in Brussels and 14 May 1990 in Luxembourg.

On 14 May 1991 the budgetary authority extended this guarantee to loans made in Czechoslovakia, Bulgaria and Romania up to a maximum of ECU 700 million.

The extension of the contract of guarantee was signed on 31 July 1991.

On 23 October 1992 the Commission presented a proposal for a Council Decision extending this Community guarantee to losses incurred by the EIB as a result of loans granted to Estonia, Latvia and Lithuania.

The overall ceiling on loans which the EIB may grant in these countries was set at ECU 200 million for a period of three years.

On 18 December 1992 the Commission also proposed the extension of this guarantee to losses incurred by the EIB as a result of loans granted in Albania.

The overall ceiling on loans which the EIB may grant in Albania was set at ECU 50 million for a period of three years.

The loans are generally long-term: 15 years on average with 3 to 4-year periods of grace on capital repayments.

At 31 December 1992, ECU 820 million had been made available in these five Eastern European countries but only a little less than ECU 147 million had been disbursed.

C. LOANS GRANTED BY THE EUROPEAN INVESTMENT BANK IN NON-MEMBER COUNTRIES

At its meeting of 19 May 1992 the Council (Economic and Financial Affairs) agreed to give practical substance to the agreement reached in principle on this issue the previous year.

It adopted the following guidelines:

- EIB loans can be granted in countries with which the Community has concluded cooperation agreements and for projects of mutual interest;

- loans may be granted, for projects that meet the Bank's usual criteria, on a case-by-case basis by the Board of Directors;

- an overall limit of ECU 250 million per year shall be set for a 3-year period; this arrangement shall be reviewed at the end of the period.

The Council agreed that these loans should benefit from Community budget guarantees. The Commission presented a proposal for a decision to this effect on 3 June 1992.

The budgetary authority set up a heading for this purpose in the 1993 budget.

D. COMMUNITY CREDIT GUARANTEE FOR EXPORTS OF AGRICULTURAL PRODUCTS AND FOODSTUFFS FROM THE COMMUNITY TO THE FORMER SOVIET UNION

The Community has decided to guarantee loans granted to the former Soviet Union by a pool of banks to finance imports of agricultural products and foodstuffs originating in the Community and the countries of Central and Eastern Europe.

The Community guarantee covers 98%, up to a maximum of ECU 500 million, of any losses in principal and interest.

The Community will receive a surety commission of 0.67% of the amount guaranteed in consideration for this guarantee. Half of this commission was paid on 26 December 1991 under the terms of the contract. The balance is to be paid one month after the end of the drawing period.

On 26 November 1991 the terms of the loan and the arrangements for the utilization of the funds were laid down in an exchange of letters between the Commission and the Soviet authorities. On the same day the Community and the banks signed a contract of guarantee.

The loan is for three and a half years from the date of signature.

Interest will be payable half-yearly and the principal will be repaid in three instalments, 20, 31 and 42 months after the agreement has been signed.

The first repayment of capital is due on 26 July 1993.

The first interest payment was due on 9 September 1992 and was made on 25 September 1992.

Following the disappearance of the Soviet Union, it has been decided that the funds will be used by the Russian Republic.

PART TWO: RISK SITUATION

There are two possible methods for evaluating the risks borne by the Community budget:

- the method, often used by bankers, of the total amount of capital outstanding for the operations concerned on a given date;

- the more budgetary approach of calculating the maximum amount which the Community could have to pay out in each financial year.

The second approach itself has been applied in two different ways:

- by reference only to actual disbursements at 31 December 1992, giving the minimum level of risk to the Community assuming that there are no early repayments;

- on a more forward-looking basis, by reference to all the operations proposed by the Commission in order to estimate the impact on future budgets, giving the maximum risk borne by the Community assuming that the Commission's proposals are accepted.

For the latter exercise a number of assumptions have to be made about dates of disbursement, terms of repayment, interest and exchange rates, etc.; details are given in the annex. However, this method does give some idea about the future level of risks connected with the proposals made.

The results are shown in the attached tables, which assess the risk relating to countries inside the Community and countries outside the Community.

The overall figures quoted cover risks of different types; loans to one country in the case of financial assistance and loans for projects guaranteed by the borrowers in the case of NCI and EIB operations, for example.

I. AMOUNT OUTSTANDING AT 31 DECEMBER 1992 (Table 1)

The amount of capital outstanding on Community borrowings and guaranteed loans at 31 December 1992 can be broken down as follows:

- ECU 7 184 million for operations within the Community;
- ECU 4 249 million for risks in non-Community countries;[1]
- giving a total of ECU 11 433 million.

Since 31 December 1992 the total amount of loans outstanding has again dropped as a result of the fall in the amount outstanding in respect of operations within the Community; the amount outstanding accounted for by non-member countries has further increased from 34.5% to 37.2% of the total.

II. MAXIMUM ANNUAL RISK BORNE BY THE COMMUNITY BUDGET: OPERATIONS DISBURSED AT 31 DECEMBER 1992 (Table 2)

A. TOTAL

The total risk involved in the annual debt-servicing for all countries should peak at ECU 3 362 million in 1993 before dropping to ECU 2 001 million in 1996 after which it will rise to ECU 2 481 million in 1997 and then fall again.

However, a distinction should be made between Member States and non-member countries when the overall situation is being assessed.

B. MEMBER STATES

Payments of capital and interest on loans disbursed at 31 December 1992 should be slightly less than ECU 2.8 billion in 1993 and then fall to less than ECU 1 500 million.

1 Of which ECU 1 591 million in EIB loans and ECU 2 658 million for Community borrowing/lending operations.

C. NON-MEMBER COUNTRIES

The annual risk in respect of non-member countries depends on the timetable for the repayment of financial assistance, as shown in the table below:

	1995	1996	1997	1998
TOTAL RISK	1079	671	1117	915
of which				
Hungary I 1	(350)			
Hungary I 2		(260)		
Algeria 1			(250)	
Hungary II 1				(100)
Czechoslovakia 1				(185)
Czechoslovakia 2			(190)	
Bulgaria			(140)	(150)
Romania				(185)
Israel			(160)	

III. FORECAST OF ANNUAL MAXIMUM RISK: OPERATIONS DISBURSED, DECIDED BUT NOT YET DISBURSED AND OPERATIONS PROPOSED (Table 3)

This figure is an indication of the potential annual maximum risk borne by the budget. It does not mean that these amounts will actually have to be paid from the budget, since any default will lead to the suspension of further payments to the country in question.

A. TOTAL

The total annual risk for all countries will come to ECU 3 584 million in 1993, before dropping to ECU 3 121 million in 1994, increasing again to ECU 4 086 million in 1995, falling again to ECU 3 683 million in 1996 and reaching ECU 4 301 million in 1997 and ECU 4 578 million in 1998.

B. MEMBER STATES

Developments will be much the same as for loans disbursed since there are few operations which still have to be carried out. The risk will peak at ECU 2 843 million in 1993 and then drop sharply.

C. NON-MEMBER COUNTRIES

The risk in respect of non-member countries will be slightly different - there will be a steady rise to ECU 2 321 million in 1995, a fairly sharp drop the following year and another increase to ECU 2 015 million in 1997 and ECU 2 229 million in 1998.

IV. ACTIVATION OF GUARANTEES

In the second half of 1992 the EIB again called on the budget guarantee in respect of loans of around ECU 4.5 million to the Republics of former Yugoslavia (Bosnia-Hercegovina, Macedonia and Serbia). This was paid from the budget on 14 December 1992.

At 31 December the Republics of former Yugoslavia still had to repay ECU 8.5 million in respect of debts paid by the Community. Lebanon had repaid its debts in full.

PART THREE: CHANGES IN POTENTIAL RISKS

The figures given in the previous parts provide information on the quantitative aspects of the risks borne by the general budget.

However, these data should be weighted in accordance with aspects relating to the quality of the risk, which depend on the type of operation and the standing of the borrower.

I. TYPES OF OPERATION

The risks to which the above figures relate derive from a variety of operations which can be divided into two categories: operations with macroeconomic objectives and those with microeconomic objectives.

A. OPERATIONS WITH MACROECONOMIC OBJECTIVES

The first of these are the balance of payments loans for Member States, normally carrying strict economic conditions and undertakings.

Financial assistance operations are similar in nature but are intended for non-member countries.

Finally, this category includes the credit guarantee for imports of agricultural products and foodstuffs into the Soviet Union, since the risk involved in this operation depends to a large extent on macroeconomic and political developments in the country.

B. OPERATIONS WITH MICROECONOMIC OBJECTIVES

These are loans to finance specific projects which are usually repaid over the long term from funds which these projects are expected to generate; as a rule, they are granted to State companies or financial institutions and, in addition to the Community guarantee, are covered by the usual guarantees demanded by banks.

They are the Euratom and NCI loans in Member States and EIB loans outside the Community (Mediterranean and Central and Eastern Europe).

Economic and Financial Situation of Third Countries Receiving Assistance Under Operations with Macro-economic Objectives

All countries receiving assistance under operations with macroeconomic objectives have been implementing stabilization and reform programmes. The economic and financial performance of these countries largely depends on the degree of progress with the far-reaching structural reforms that the assistance supports.

This section also provides information on a number of countries of Central and Eastern Europe that are not receiving this type of assistance, the successor States to Yugoslavia and the ex-Soviet Republics.

A. HUNGARY

Since 1989 the Hungarian economy has embarked on a major effort of stabilization and medium-term adjustment. However, the reform process has been accompanied by a severe contraction of economic activity; GDP dropped by 10.2% in 1991 and by an estimated 5% in 1992. Inflation has gradually declined to a year-on-year rate of 21.6% in December 1992 but unemployment has continued to climb, reaching 663,000 (12.2% of the work force) in the same month. The State budget deficit is estimated to have reached Ft 197 bn in 1992 (above the target of 5% of GDP), mainly as a result of higher than expected falls in revenue. In response to this poor fiscal performance, the IMF froze its assistance in the second half of 1992.

The programme of structural reform proceeds, and key legislative acts were passed in 1991 and 1992. The bulk of the legislation to redefine ownership rights and to set up a market based business environment was passed in 1991. In 1992, the Government focussed on the reform of public finance and on legislation related to the infrastructure and social sectors. Restructuring is progressing slowly. End 1992, about 16% of State assets had been privatized. Some large sectors, such as transport, agriculture or banks, have so far remained unaffected by this move. Private sector growth is nevertheless sustained, with the rapid emergence of a new SMEs sector and the sizeable inflow of foreign capital. Overall the private sector contribution to GDP in 1992 is estimated at about 30%.

In 1992 as in the two previous years, the balance of payments performance has been better than expected. At the end of October 1992, the trade balance and current account recorded a surplus of, respectively, US$ 489 million and US$ 704 million against the initial forecast of a deficit. The combination of sustained export growth and substantial tourism and transfers surpluses freed Hungary from any foreign exchange constraint, in particular for the service of its debt. The debt service ratio fell from 43.2% in 1990 to around 30% in 1991 and is estimated to have fallen further in 1992. The inflow of investment into the country and the support from the IMF, the World Bank and the G-24 strengthened the official reserves, which are now at a satisfactory level (US$ 5.1 billion in October 1992, i.e. 5 months' imports).

The country's external gross debt stabilized around US$ 22.5 billion in the third quarter of 1992. In 1991 the structure of Hungary's debt improved significantly as the proportion of short-term loans was reduced to 9.6%. The price of Hungarian debt on the secondary market has levelled off at around 90% as a result of prompt debt servicing by the Hungarian authorities and the perceived reduction in the risk of rescheduling. In 1992 Moody's rated the National Bank of Hungary's bond issues BA1 while Standard and Poor's rated them BB+.

B. Czech and Slovak Republics

Some indications have become available that the economic stabilization which seemed to occur in mid-1992 (production in traditional sectors was stabilizing at its depressed level and output and employment growth in new sectors was gaining momentum) was only short-lived. First provisional estimates show a decline of GDP by almost 10% in 1992 compared to 1991 (GDP dropped by 16% in 1991), implying a significant deterioration in the economic performance in the second half of the year (minus 5% compared to the first half). Furthermore, inflation which came down to a single-digit figure between May and August 1992 accelerated again to a monthly rate of 2% since September, before the introduction of VAT led to another surge in prices in January 1993. The overall public budget has remained by and large balanced although its underlying trend is not very favourable, and Slovakia's deficit is approaching 4% of its GDP. The first wave of large-scale privatization was completed by end 1992.

Uncertainty about the procedures and effects of the split of Czechoslovakia into two independent states may have been the major cause for the surprising further decline in economic activity in the course of the year. Indeed, this issue dominated political discussion and political action throughout 1992, leading to significant irritations on behalf of potential domestic and foreign investors. Furthermore, investment and large-scale capital-stock modernization were also hampered by large-scale voucher privatization as new owners were not yet in power while old owners and managers were no longer seriously interested in structural adjustment. In consequence, underinvestment has continued in both republics. Unemployment rates continued to come down in the course of 1992 with the Czech unemployment rate dropping below 3% while Slovakia's unemployment rate came down from almost 13% in early 1992 to slightly above 10% by the end of the year. However, labour productivity has not yet picked up. This indicades that large-scale labour-market adjustment is still ahead.

The split of the two republics which also reflected divergent philosophies of economic policy (market-oriented in the Czech Republic versus more state intervention in Slovakia) has been managed in a peaceful way. Both republics agreed on the split of assets and liabilities with the general rule of 2 (for the Czech Republic) to 1 (for Slovakia). Furthermore, a customs union was established and monetary union has initially been maintained, but preparations are under way for an immediate split of currencies.

The balance of payments has been very strong in 1992. The overall balance of payments is estimated to have recorded a surplus of US$ 2.2 billion (US$ 1.2 billion in 1991). Trade balance is estimated to have registered a small deficit, although exports to the West have been growing strongly. Inflows of foreign direct investment, initially very strong, has been dampened by the impending dissolution of the federation during the second half of 1992. Official reserves were reaching the equivalent of 2.8 months of imports by year-end (1.3 months in 1991). In light of the strength of the reserves, the authorities decided not to draw on IMF resources under the stand-by arrangement during the latter part of the year (although the performance criteria were met and the review of the programme was successfully completed). At end-1992, gross external debt in convertible currencies stood at US$ 9.9 billion, and debt service at 13 percent of exports (down from 15 percent in 1991). The exchange rate, which is pegged to a basket of five currencies remained stable.

C. BULGARIA

Bulgaria's economic performance has been worse than that of most other countries of the region. In 1991 real GDP fell by 17%, real wages fell by about half, and inflation was over 300%. The decline continued in 1992, with GDP falling by a further 13% in real terms in the first half of the year; industrial output is down about 20% over 1991, with only tentative signs of recovery; inflation remains high at 4-6% per month (80% overall in 1992), and unemployment is over 15% of the labour force. External factors have exacerbated the crisis: the debt problem (Bulgaria has been cut off from foreign credits since 1990 when it declared a unilateral moratorium on debt-servicing), the collapse of the ex-USSR, on which Bulgaria was more dependent than other countries, large uncollectable claims on Libya and Iraq, and most recently, the embargo against Serbia, which was a major export market.

Economic reform has so far mainly consisted of liberalization and stabilisation measures. In particular, cautious macroeconomic policies and an early introduction of internal convertibility allowed most domestic prices to adjust to market-clearing levels without triggering an inflationary spiral. Structural reform has proceeded more slowly, in part because of inadequate political consensus during 1991. In the first months of 1992, however, considerable legislative progress on privatization and other structural measures was made. In particular, small-scale privatization and restitution are advancing well. On the other hand, there have been considerable delays in large-scale privatization; the fall of the government in October last year (a new government was only formed in the very end of 1992) further delayed its implementation. There are, however, some grounds for optimism for the near future since the new Prime Minister has declared his cabinet the "government of privatization". For medium-term prospects, much will depend on how vigorously the legislation is implemented. A resumption of growth will need to be export-led - there is no room for monetary or fiscal stimuli. This requires that the debt crisis be resolved, and that export markets, especially in Europe, be sufficiently open.

After the end of the political crisis, Bulgaria resumed its relations with the IMF in the framework of the stand-by arrangement with the Fund expiring in April 1993. The government is at present negotiating a new annual programme, to be supported by a new SBA.

The improvement of the external financial situation of the country continued in 1992. The current account deficit on a cash basis was once more below US$ 1 billion. The trade balance was slightly positive, following a bigger increase of exports than of imports (imports are still low, mainly due to shortfalls in external financing). International reserves increased to over US$ 1.1 billion in the end of October 1992, or three months' imports. They remain, however, weak in view of the likely needs that may arise in the context of the settlement of Bulgaria's commercial debt. The negotiations with the commercial banks on this issue have recently progressed. In November, the two parties reached an agreement on the main principles for a future debt and debt service reduction package. The new Bulgarian government's intention is to continue the negotiations and seek the conclusion of the deal during the months ahead. In December 1992, Bulgaria secured a further debt relief from its official creditors. The new Paris Club agreement reschedules the debt servicing due up to April 1993 and the arrears incurred since the expiry of the consolidation period covered by the previous agreement (concluded in April 1991). Overall, the external debt is estimated at US$ 12 billion. For almost half, this debt is made up of arrears on short-term deposits and letters of credit. The debt has been increasing in 1992 since Bulgaria is still accumulating arrears (the interest payments that were resumed in September amount to only 25% of current interest falling due). The price of this debt on the secondary market has fluctuated around 20%. The debt-service ratio is around 50% of convertible currency export earnings.

D. ROMANIA

The Romanian authorities continued to apply during 1992 the comprehensive stabilization and reform programme embarked upon in 1991. The new government, formed after the September 1992 elections, has pledged its commitment to continued reform. The main problem of the Romanian economy has been the sharp falls in output. Real GDP fell by 13% in 1991 and is estimated to have declined by 16% in 1992. Unemployment stood at 8.6% in October 1992 but is rising rapidly. The government has maintained prudent fiscal and monetary policies. In 1992, fiscal deficit was limited to 2 percent of GDP and credit expanded by only 70 percent, remaining below the programmed ceiling. However, the rate of inflation, although on a declining trend, still reached some 200 percent in 1992 (473 percent in 1991); a large part was due to price liberalization and subsidy cuts introduced in the course of the year.

Economic reform is proceeding at a steady pace. The operation of the tax system is being streamlined and VAT will be introduced in July 1993. The privatization process is well advanced in the farm sector but is proceeding slowly in the industrial area. A disturbing element has been the re-emergence of a parallel exchange market, where the national currency is sold at a discount, which by end-1992 exceeded 20 percent.

The external situation of Romania, which had deteriorated sharply in 1991, recovered in 1992. Export performance was strong, while imports declined, resulting in a significant improvement in the current account, which registered a deficit of some $ 0.75 billion (roughly half of its size in 1991). Despite delays in disbursements from official sources, international reserves increased by some $0.2 billion.

The policy of accelerated repayment of the debt pursued by the authorities in the latter part of the 1980s has resulted in a low debt-service ratio (2% in 1991 and 8% in 1992).

E. THE BALTIC STATES

The economies of the Baltic states were highly integrated within the Soviet Union economic system, from which they regained their independence in August 1991. All three countries have suffered a prolonged downturn in economic activity as trade with former Soviet republics, particularly Russia, has declined.

Estonia

Preliminary estimates of GDP for 1992 point to a decline of 26%, following declines of 12.6% in 1991 and 3.6% in 1990. Registered unemployment in December 1992 stood at 12,579 (about 1.5% of the labour force). Hidden unemployment is believed to be much higher. The budget for the first half of 1992 showed a surplus of 1.4% of GDP, and a similar figure is expected for the full year when the data are available. However, the problem of tax arrears is making the maintenance of budget balance increasingly difficult. Inflation is now under control: in December 1992 the monthly increase in the consumer price index was 3.3%.

Price liberalization has largely been completed, and the emergence of a rational price structure has been assisted by the introduction of Estonia's own convertible currency- the kroon. Privatization has so far been limited to small-scale enterprises, with over 40% sold into private ownership. The government aims to accelerate the process of privatization through a newly established privatization bureau. However, problems continue to surround the restitution issue, following the indefinite extension of the deadline for restitution claims. The commercial banking system is undergoing a liquidity crisis. This has prompted the government to pursue the recapitalization of the banks by means of a bond issue and support from the foreign exchange reserves.

In 1992, Estonia's current account, which had shown a substantial surplus in the previous year, deteriorated significantly as Russia started to charge world market prices for its exports to Estonia at the beginning of the year. However, there are first indications that the current account may have recorded a small surplus, as imports dropped below programmed levels owing to delays in the disbursement of expected external official financing. Estonia's trade with the FSU did not recover significantly in the course of 1992 (export and import volumes were more than 50% below the respective 1990 levels), whereas trade with the West expanded rapidly; in the third quarter it constituted roughly half of overall trade. The overall trade balance is estimated to have been in deficit. Official reserves increased by $ 75 mio in the course of 1992 excluding the restitution of prewar gold by the BIS, the UK and Sweden. Estonia purchased the first tranche (about $11 mio) from the IMF under a one-year stand-by agreement totalling about $39 mio for the period 1 July 1992 - 30 June 1993. At the end of last year, the foreign debt amounted to $ 24.2 mio (about 3% of GDP). This does not include the 0.62% share of the FSU debt (now estimated at close to $80 bn) which was attributed to Estonia in the negotiations on the responsibility of this debt, but was never recognized by Estonia. Bilateral negotiations with Russia will determine whether Estonia's external position has to be modified after all claims and liabilities have been taken into account.

Latvia

GDP is likely to have declined by about 30% in 1992. By December 1992 there were 33,200 registered unemployed in Latvia, or 2.3% of the workforce. Moreover, hidden unemployment is widespread, with 15% to 20% of industrial employees estimated to be on indefinite unpaid leave. The 1992 budget is expected to show a deficit of about 1.1% of GDP. The present budget proposals for 1993 envisage balance for current expenditures but a small overall deficit to allow for capital investment. The increase in retail prices has moderated in recent months, in line with the decline in real wages. In September 1992 the index of retail prices was 644% higher than in the same month in 1991.

Price liberalization has progressed well in Latvia; only a few items remain subject to control. Privatization, however, has progressed only slowly. This is partly due to the provisions for restitution, which set mid-1992 as the deadline for the submission of claims on enterprises and land, and October 1994 for housing. So far privatization has mainly been confined to small enterprises. A law adopted in August identifies an initial 25 large-scale enterprises suitable for early privatization. A list of 600 enterprises has also been identified as eligible for privatization.

Latvia's current account situation worsened significantly in 1992 due to the substantial terms of trade shock which affected the economy in the beginning of the year when Russia started to charge market prices for its exports to Latvia. There are first indications that the deficit in the trade balance, which was incurred entirely with the FSU, was more than compensated by a surplus in the services balance resulting in a current account surplus. However, an unexplained outflow of private capital points to an underreporting of actual import levels. As in the other two Baltic countries delays in the disbursement of external official aid constrained the expansion of imports and production. Gross national reserves increased by $48 mio in 1992, but only by $12 million on a net basis after taking into account the purchases of the first two tranches (together $36 mio) from the IMF under the one-year stand-by arrangement totalling about $77 mio. Latvia's official external debt outstanding stood at $59 mio (4.8% of GDP) on 31 December 1992 and the ratio of debt service to exports was 2.1%. Latvia never recognized the 1.14% share of the FSU debt it was assigned during the negotiations of the FSU; it will be the outcome of negotiations on this and other issues with Russia to what extent Latvia's official external debt has to be modified.

Lithuania

GDP is estimated to have declined by about 39% in 1992, following declines of about 13% in 1991 and 5% in 1990. Unemployment stood at 12,651 in November 1992, just 1% of the workforce. The average inflation rate for 1992 was over 1000% and the monthly increase in December was 27.7%. Nevertheless, the government is confident that it will soon achieve the programme objective of single-digit monthly inflation.

Price liberalization has progressed to the extent that all goods and services except household energy products and monopoly products are de-controlled. Privatization has progressed relatively fast in Lithuania. The government is concerned, however, that privatization has proceeded without sufficient attention to restructuring. Many firms are now effectively worker controlled, thus hindering rationalization and labour shedding. The government is, therefore, reviewing the privatization programme.

In 1992, Lithuania's current account situation deteriorated considerably. One negative factor was the severe drought which adversely affected agricultural production, the import needs and the export potential of all three Baltic countries. In addition, Lithuania's current account suffered from the terms of trade shock induced by Russia whose export prices for Lithuania reached world market levels in Fall 1992. The current account, constrained by the lack of official financing in 1992, still appears to have been in surplus for the year as a whole, as does the trade balance; but there is a possibility that imports, mainly from former Soviet republics, were underreported. Gross national reserves had increased by $75 mio until the end of 1992. Apart from the Fund purchase of about $17 mio (1.1% of GDP), there seems to be no other official foreign debt. During the interstate negotiations on the FSU debt, Lithuania was assigned 1.41% of the overall debt, which it never recognized. Negotiations are still going on with Russia how this and other issues can be settled bilaterally.

F. ALGERIA

In a context of tight external reserve contraint, the authorities have implemented austerity measures, mostly through the introduction of new trade restrictions. As a result, in 1992, the country has entered in a situation of recession, and employment has grown, exceeding 20% according to official statistics. Price liberalisation measures, rising import prices stemming from the dinar's depreciation during 1991 and the financing of the public sector deficit pushed up the inflation rate in 1992 to about 30% (compared to 16.6% in 1990).

A stable exchange rate combined with a high inflation rate has undermined the competitiveness of the domestic production and led the economic authorities to temporarily restrict certain imports.

Algeria's external debt currently stands at US$ 25 billion, with a strong short-term component. Debt servicing and repayments exceeds 70% of the country's export earnings (mostly from oil and gas). However, Algeria has avoided requesting any multilateral debt moratorium or rescheduling, and is seeking additional bilateral financing facilities. The stand-by arrangement approved by the IMF in June 1991 became non-operational in early 1992. Negotiations on a new programme could begin soon.

G . ISRAEL

In 1992, Israel has recorded its third straight year of strong growth. However, unemployment has risen to 11.5%, the highest level over the past two decades. The macro-economic situation improved substantially. Inflation declined to a single deficit and the budget deficit was substantially reduced. Exports of goods and services - tourism, in particular - picked up. The performance of the economy has increased its international ratings.

To finance the investment effort necessary to absorb the recent wave of immigration, in April 1992 Israel reveived an SDR 179 million Compensatory and Contingency Facility from the IMF. The American administration authorized a US$ 10 billion loan guarantee, which removed the constraint of a political shortage of foreign exchange as well as the problem of country limits and high borrowing costs. Gross external debt stood at US$ 33.8 billion (corresponding to 61% of GDP) at the end of 1991, while the debt service represented some 27% of exports down from 80 percent in 1985, a rather sound basis to undertake foreign borrowing to finance an investment programme.

H. FORMER SOVIET UNION

The economic crisis in the former Soviet Union has grown increasingly acute during 1992. Central planning has collapsed in most of the newly independent states. Trade between them has declined by an estimated 20-30%. Throughout most of the area, monetary conditions are chaotic, credit policy is lax and the financial system barely functions. Budgets are out of control, especially because of tax collection problems. Hard-currency exports have plummeted, resulting in external payments crises. As a result, output is declining rapidly (GDP is likely to have fallen by roughly 20%), and the region is very close to hyperinflation. Industrial restructuring and labour shedding have not really started; unemployment is still low.

Far-reaching economic reform has begun in many republics, but progress has been uneven. At the beginning of the year *Russia* set the tone by launching a bold, if insufficiently comprehensive, reform programme. From the spring onwards, the pace of reform began to falter as domestic opposition mounted, in particular from the parliament and the powerful state enterprise sector. As a result, macroeconomic stabilization failed and the country drifted into hyperinflation. Legal, institutional and structural reform has advanced only slowly, although some progress was made with privatization. In *Ukraine*, economic policy has been determined mainly by nationalist forces intent on asserting independence from Moscow, who have neglected to introduce the legal and institutional framework necessary for a market economy. The goal of a separate Ukrainian currency and reticence towards the CIS should also be seen in this context. The government which came to power in October appears to be more strongly committted to reform, however. Some republics have made considerable strides in the transition to market-based systems: *Kazakhstan* and *Kyrgyzstan* are both close to concluding stand-by agreements with the IMF. In others, however, few efforts at reform have been made, or civil war is disrupting the economy more than any attempt at transition.

The external financial situation of the area is extremely weak. This is particularly the case in the short run; in a longer run, the new states that have succeeded the Soviet Union present rather variable profiles. Some have considerable hard currency earning potential and industrial capacity; others are clearly close to developing countries and will therefore strongly depend on external assistance.

The external financial situation of the NIS is largely determined by the developments in the Soviet Union since the late eighties and, at present, by the questions related to the settlement of the external debt problem.

Since 1990, the only way the former Soviet Union was able to service its external debt, which was owed mainly to private creditors, was to cut back on imports and run down its gold and hard currency reserves. It made also an extensive cae of official and officially guaranteed credits provided by the main industrialized countries. However, in view of the growing difficulties in collecting hard currency resources, and the withdrawal of credit lines with Western commercial banks, the Vneshekonombank of the still existing USSR had virtually to suspend payments at the end of 1991. In December 1991-January 1992, the authorities of the new states concluded agreements with official and private creditors of the Soviet Union on deferral of principal repayments on medium- and long-term credits contracted prior to 1991. The agreements were based on the acceptance by the states of the principle of "joint and several responsibility" for the debt servicing.

Despite the deferrals, the former Soviet Union's liquidity crisis has not eased in 1992. Furthermore, the legal framework of the debt servicing based on the joint and several responsibility has not proved workable (Russia was the only state to make any actual payments), and significant arrears (some US$ 10 billion, including over US$ 2 billion in interest arrears), have been accumulated on non-deferred debt. As a result, the debt outstanding is now exceeding US$ 75 billion, up from US$ 67 billion in the end of 1991. Following these developments, the case for a longer-term solution to the debt-servicing problem has been gaining support. At present, the Paris Club of official creditors is seeking such a solution in the form of a comprehensive debt rescheduling package covering both principal and interest and possibly providing for some relief on payments due on credits extended in 1991 as well.

The package is being negotiated with Russia which is increasingly viewed by the creditors as the sole successor of the Soviet Union, at least as regards its foreign liabilities. For months, Russia has been seeking to take over all the former Soviet Union's foreign debt, in exchange of its assets, through the so-called "zero-option" arrangements. Ukraine, the second largest former Soviet republic, has not agreed so far with this solution, thus making impossible a comprehensive debt rescheduling.

I. FORMER YUGOSLAVIA

All successor republics to the former Yugoslavia are confronted with comparable problems: the transition to a market economy and to international competition, worsened by the collapse of Comecon trade, the effects of the war and the boycott of each other's trade, have resulted in a contraction of output, of employment, and increased inflation. The trade and current account deterioration is marked by the sharp contraction of imports (resulting from the drop in domestic activity). Furthermore, the widespread DM-ization of the inflationary economies and the provision of large-scale humanitarian aid (in the case of Croatia and Bosnia) make it particularly difficult to interpret balance of payments developments.

The successor republics are in the process of discussing the division of internal and external assets and liabilities under the aegis of the Peace Conference in Geneva. Yugoslavia's external debt amounting to US$ 16 bn has already been largely divided between the successor republics except for a federal part equal to US$ 3.1 billion, guaranteed by the National Bank of Yugoslavia, and largely owed to commercial banks. (The debt owed to commercial banks is equal to US$ 4.7 billion, to international organizations US$ 3.2 billion and to governments US$ 5.5 billion).

The Yugoslav debt was rescheduled in 1988 by the London and Paris Clubs. The agreements included grace periods through 1993 and 1994, respectively. Until March 1992, the entire debt was serviced by the National Bank of Yugoslavia and Slovenia for their respective parts in accordance with these agreements. The agreements will have to be renegotiated with each republic.

Yugoslavia (Serbia and Montenegro)

The Yugoslav economy and monetary system have practically collapsed due to the catastrophic effects of the civil war and sanctions. Gross domestic product is estimated to have fallen by 20% in 1992 and by 35% since 1989. The central bank funds nearly all the federal budget by money issue and has consequently lost control of the money supply; inflation in 1992 reached 20,000%. Although the authorities have maintained an official exchange rate of 470 dinars to the DM since November 1992, the black market rate in late January was about 3,400 dinars to the DM. About one third of the 2.3 million persons employed in social sector of the republic are currently on compulsory leave. All attempts at economic reform have been abandoned.

During 1992, Yugoslav exports were approximately $2.5 bn (-46% over 1991) while imports reached US$ 3.9 bn (-33% over 1991). However the bulk of this trade took place before July 1992, when most countries began to apply on sanctions. Foreign exchange reserves stood at US$ 1.35 bn in December 1992, very near the minimum level prescribed by law.

The combined foreign debt of the new republic is US$ 5.5 bn plus its share of the federal debt. In June 1992, the National Bank stopped servicing its debt to commercial banks. It continued however to make small payments to the IMF.

Slovenia

Slovenia was Yugoslavia's wealthiest and most industrialized republic. Output fell by 9.3% in 1991, mostly due to a large drop in industrial production (-12.4%). This decline has continued at about the same magnitudes in 1992 but production is expected to stabilize in 1993. Retail prices during the first ten months of 1992 rose by 240% over the same period in 1991 but the monthly rate has now dropped to 3%. Unemployment was 12.7% of the labour force in October 1992.

Since independence, Slovenia has implemented drastic economic reforms. Prices and foreign exchange operations have been liberalized, the banking sector deregulated and the fiscal system completely restructured. Following a long debate in Parliament, a privatization law was passed in November 1992.

Slovenia has introduced its own currency and has maintained rigourous monetary and fiscal policies. Foreign currency reserves have more than tripled during 1992, reaching US$ 1.4 bn in November 1992. The country has also minimized the negative consequences of the loss of the internal Yugoslav market by successfully reorienting its foreign trade activity. During the first ten months of 1992 there was a small trade deficit (US$ 92 million) but a current account surplus of US$ 828 million.

Slovenia's share of the Yugoslav foreign debt is US$ 1.7 bn, not including its part of the federal debt. The republic had continued to service its debt without interruption until May 1992. In June it refused to make payments to banks as long as the latter were referring to payments by Yugoslavia as a whole and were not explicitly acknowledging that Slovenia had paid its own share in the debt by itself. In November 1992, Slovenia regularized its situation. Banks are now beginning to negotiate with Slovenia on the servicing of the latter's part in the federal debt on the basis of the allocation of a part of the Yugoslav quota in the IMF to Slovenia (± 17%).

Croatia

Croatia's economic performance continues to be adversely affected by the civil war. One third of its territory is occupied and the country is flooded by Croatian and Bosnian refugees. The tourist industry has come to a standstill. GDP declined by 32.4% during the first eight months of 1992, following a 23.4% drop in 1991. This is mainly due to the fall in industrial production and in tourism. Retail prices rose by 655% during the first ten months of 1992 over 1991; recently inflation has been on an accelerating trend. The rate of unemployment reached 17.8% at the end of 1992.

Economic reforms were at a very early stage when civil war broke out. The privatization law enacted in May 1991 has been widely criticized as inadequate, and there is an urgent need to streamline the country's inefficient fiscal system.

Croatia showed a US$ 0.3 bn trade deficit in 1992 (US$ 0.4 bn in 1991). Foreign exchange reserves at the Central Bank stood at only US$ 170 million in the end of 1992.

The external debt is valued at US$ 2.7 bn plus Croatia's share in the US$ 3.1 bn federal debt. As of May 1992, Croatia ceased to service its share of the debt, alleging that part of it had been purchased on the secondary market by Serbia. Croatia is presently trying to convince the commercial banks to form another consortium and discuss the renegatiation of the outstanding debt and arrears on payments of interest.

Macedonia's total debt is valued at some US$ 1 bn and Bosnia-Herzegovina's total debt at US$ 2 bn.

TABLE 1

CAPITAL OUTSTANDING IN RESPECT OF OPERATIONS DISBURSED

(ECU million)

Operation	Authorized ceiling	Amount outstanding 30.6.1992	Amount outstanding 31.12.1992
MEMBER STATES			
A. Balance of payments	14000		
1. Greece I		953	875
2. Greece II		1000	1000
B. Other			
3. Euratom	4000	1452	1338
4. NCI and NCI earthquakes	6830	3502	3326
5. EIB Mediterranean, Spain, Greece, Port.	1500	676	645
THIRD COUNTRIES			
A. Financial assistance			
1. Hungary	1050	710	710
2. Czechoslovakia 1	375	375	375
3. Bulgaria 1	290	290	290
4. Romania	375	375	375
5. Algeria	400	250	250
6. Israel	160	160	160
8. Former Soviet Union	1250		123
B. Other			
9. EIB Mediterranean	6017	1358	1444
10. EIB Central and Eastern Europe	1700	60	147
11. Guarantee, CIS	500	408	375
TOTAL	38447	11569	11433
(Community)	26330	7583	7184
(non-Community)	12117	3986	4249

TABLE 2

MAXIMUM ANNUAL RISK BORNE BY THE COMMUNITY BUDGET

(Estimate in ECU million based on all operations disbursed at 31 December 1992)

	1992	1993	1994	1995	1996	1997	1998	1999	TOTAL
MEMBER STATES									
CAPITAL									
A. Balance of payments									
1. Greece	650	522	200		500		500		2372
B. Structural loans									
2. Euratom	287	350	99	44	152	575	91	16	1614
3. NCI and NCI EQ	824	1166	651	486	314	525	90	39	4095
4. EIB Med. Old Prot. Sp. G. Port.	105	100	86	76	79	73	72	55	646
Capital - subtotal	1866	2138	1036	606	1045	1173	753	110	8727
INTEREST									
A. Balance of payments									
1. Greece	349	144	110	95	95	46	46		885
B. Structural loans									
2. Euratom	138	110	79	71	67	55	10	3	533
3. NCI and NCI EQ	358	294	185	130	90	64	16	8	1145
4. EIB Med. Old Prot. Sp. Gr. Port.	67	57	48	40	33	26	20	15	306
Interest - subtotal	912	605	422	336	285	191	92	26	2869
MEMBER STATES-TOTAL	2778	2743	1458	942	1330	1364	845	136	11596
NON-MEMBER COUNTRIES									
CAPITAL									
A. Financial assistance									
5. Hungary				350	260		100		710
6. Czechoslovakia						190	185		375
7. Bulgaria						140	150		290
8. Romania							185	190	375
9. Algeria						250			250
10. Israël						160			160
11. Ex USSR				123					123
B. Guarantees									
12. EIB Med.	96	105	121	126	122	123	125	119	937
13. EIB C+E Eur.			2	10	15	16	16	15	74
14. Aid, Russia 500m		125	125	125					375
Capital-subtotal	96	230	248	734	397	879	761	324	3669
INTEREST									
A. Financial assistance									
5. Hungary	73	73	73	73	36	10	10		348
6. Czechoslovakia	36	38	38	38	38	38	19		245
7. Bulgaria	15	29	29	29	29	29	15		175
8. Romania		38	38	38	38	38	38	19	247
9. Algeria	22	25	25	25	25	25			147
10. Israël	16	16	16	16	16	16			96
11. Ex USSR		12	12	12					36
B. Guarantees									
12. EIB Med.	112	110	102	92	82	73	64	54	689
13. EIB C+E Eur.	4	11	11	11	10	9	8	7	71
14. Aid, Russia 500m	10	37	25	11					83
Interest-subtotal	288	389	369	345	274	238	154	80	2137
NON-MEMBER COUNTRIES- TOTAL	384	619	617	1079	671	1117	915	404	5806
GRAND TOTAL	3162	3362	2075	2021	2001	2481	1760	540	17402
(Eastern Europe)	138	363	353	820	426	470	726	231	3527
(Other non-member countries)	246	256	264	259	245	647	189	173	2279

TABLE 3

MAXIMUM ANNUAL RISK BORNE BY THE COMMUNITY BUDGET

(Estimate in ECU million based on all operations - disbursements, decisions and Commission proposals)

	1993	1994	1995	1996	1997	1998	1999	2000	TOTAL
MEMBER STATES									
CAPITAL									
A. Balance of payments									
1. Greece	522	200		500		1100		600	2922
2. Italy							4000	2000	6000
B. Structural loans									
2. Euratom + NCI	1516	750	530	466	1101	181	55	51	4649
3. EIB Sp. Gr. Port.	100	66	79	73	72	55	49	44	558
Capital-subtotal	2138	1036	609	1039	1173	1336	4104	2695	14129
INTEREST									
A. Balance of payments									
1. Greece	144	170	215	215	168	168	60	60	1200
2. Italy	100	500	700	800	800	800	700	300	4700
B. Structural loans									
2. Euratom + NCI	404	264	201	157	119	26	11	6	1189
3. EIB Sp. Gr. Port.	57	48	40	33	26	20	15	11	250
Interest-subtotal	705	982	1156	1205	1113	1014	786	377	7339
MEMBER STATES-TOTAL	2843	2018	1765	2244	2286	2349	4890	3072	21468
NON-MEMBER COUNTRIES									
CAPITAL									
A. Financial assistance									
4. Hungary			350	260	80	360			1050
5. Czechoslovakia					190	185			375
6. Bulgaria					140	150		55	345
7. Romania						185	190	80	455
8. Israel					160				160
9. Algeria					250			150	400
10. Ex USSR		146	929	175					1250
11. Baltic States								220	220
12. Euratom, C+E Eur.						20	35	48	103
B. Guarantees									
13. EIB Med.	105	121	126	158	215	293	354	404	1776
14. EIB C+E Eur.		2	10	37	75	114	140	146	524
15. EIB, other third countries					3	10	23	40	76
16. Aid, Russia, Guar. 500m	125	125	125						375
Capital-subtotal	230	394	1540	630	1113	1317	742	1143	7109
INTEREST									
A. Financial assistance									
4. Hungary	81	107	107	70	44	36			445
5. Czechoslovakia	38	38	38	38	38	19			209
6. Bulgaria	35	40	40	40	40	26	11	11	243
7. Romania	42	46	46	46	46	46	27	8	307
8. Israel	16	16	16	16	16				80
9. Algeria	32	40	40	40	40	15	15	15	237
10. Ex USSR	60	125	88	10					283
11. Baltic States	11	22	22	22	22	22	22	22	165
12. Euratom, C+E Eur.		30	52	72	92	112	110	107	575
B. Guarantees									
13. EIB Med.	144	177	232	311	376	427	445	432	2544
14. EIB C+E Eur.	15	42	85	132	160	162	157	146	899
15. EIB, other third countries		1	4	12	28	47	61	66	219
16. Aid, Russia, Guar. 500m	37	25	11						73
Interest-subtotal	511	709	781	809	902	912	848	807	6279
NON-MEMBER COUNTRIES-TOTAL	741	1103	2321	1439	2015	2229	1590	1950	13388
GRAND TOTAL	3584	3121	4086	3683	4301	4578	6480	5022	34856
(Eastern Europe)	444	748	1903	902	927	1437	692	843	7896
(Other non-member countries)	297	355	418	537	1088	792	898	1107	5492

EXPLANATORY NOTES

The purpose of these tables is to show the annual repayments of capital and interest in respect of borrowing and lending operations for which the risk is covered by the Community budget. The figures show the maximum possible risk for the Community in respect of these operations and must not be read as meaning that these amounts will actually be drawn from the budget. In the case of Table 3, it is not certain that all the operations described will actually be disbursed. No account has been taken of interest on late payment or any additional costs such as lawyers' fees.

I. TYPES OF OPERATION AND PAYMENT OF THE BUDGET GUARANTEE

A. Types of operation

The risk covered by the Community budget results from two types of operation:

- borrowing/lending operations;
- guarantees given to third parties.

In the first type of operation, the Community borrows on the financial market and on-lends the proceeds (at the same rate and for the same term) to Member States (balance of payments), non-member countries (medium-term financial assistance) or firms (NCI, Euratom).

The loan repayments are scheduled to match the repayments of the borrowings due from the Community. If the recipient of the loan defaults, the Commission must draw on its budgetary resources to repay the borrowing on the due date.

The loan guarantee is in respect of loans granted by a financial institution (EIB or commercial banks in the case of the former Soviet Union). When the recipient of a guaranteed loan fails to make a payment on the due date, the bank asks the Commission to pay the amounts owed by the defaulter.

B. Mobilization of funds

The funds needed can be raised by re-using amounts repaid or by means of transfers.

The re-use of amounts repaid by debtors allows payments to be made within a short period of time always providing, of course, that there are funds available for re-use.

Where there are insufficient funds for re-use or insufficient time for a transfer, the amount required will be taken provisionally from cash resources with an adjustment being made later by means of a transfer and/or a supplementary/amending budget as appropriate.

II. CALCULATION

Some of the amounts indicated are the result of estimates made on the basis of the following assumptions:

Generally speaking, the exchange rates for loans in currencies other than the ecu are assumed to have been stable since 31 December 1992. However, borrowing and lending operations should not involve exchange risks for the Community. Unless otherwise stated, the average rate of interest is estimated at 10%. This rate is probably a little high for EIB loans, which often attract interest subsidies under the protocols.

A. Member States

1. Greece I: The figures for repayments of capital and fixed-rate interest are final and certain.

2. Greece II: A total of ECU 2.2 billion has been granted with a first tranche of ECU 1 billion. This first tranche is repayable as follows: ECU 500 million in 1996 and ECU 500 million in 1998. It is assumed that the second tranche of ECU 600 million will be paid out in 1993 with a term of six years. It is assumed that the third tranche of ECU 600 million will be paid out in 1994 and will also run for a term of six years.

3. EIB, Mediterranean, old protocols: Spain, Greece, Portugal: These are Community guarantees for EIB operations in these countries prior to accession. The amounts are now final, since all the loans authorized have been disbursed.

B. Non-member countries

a. Financial assistance

1. Hungary I: The amounts and rates for the first two tranches are final and certain. It is assumed that the third tranche will be paid in 1993.

2. Hungary II: ECU 180 million has been granted in two tranches, with a first tranche of ECU 100 million.

3. Czechoslovakia: ECU 375 million has been granted in two tranches for a maximum term of seven years (bullet), with a first tranche of ECU 185 million and a second tranche of ECU 190 million for a term of six years.

4. Bulgaria: ECU 290 million has been granted in two tranches for a maximum term of seven years (bullet), with a first tranche of ECU 150 million and a second tranche of ECU 140 million for a term of six years.

   It is assumed that the new operation (ECU 110 million for a maximum term of seven years to be paid in two tranches) will be disbursed in full in 1993.

5. Romania: An estimated ECU 375 million in two tranches for a maximum term of seven years (bullet). The first tranche of ECU 190 million was disbursed with a term of seven years and the second was disbursed in 1992 with a term of six years.

   It is assumed that the new operation (ECU 80 million for a maximum term of seven years) will be disbursed in 1993.

6. Baltic States

   It is assumed that this loan of ECU 220 million will be paid in full in two tranches in the course of 1993 and repaid in one tranche seven years later.

7. Algeria: ECU 400 million has been granted in two tranches of ECU 250 million and ECU 150 million. The first was paid in December 1991 for a term of six years: it is assumed that the second will be paid in 1993 for a term of six years.

8. Israel: The Council (Economic and Financial Affairs) has decided on a borrowing/lending operation for ECU 160 million. The loan was paid in one tranche in 1992 for a term of six years.

b. Guarantees

1. EIB Mediterranean

Figures provided by the EIB for loans disbursed at 31 December 1992.

For the others, we have made the following assumptions concerning the signature of loans.

Year	1993	1994	1995	1996	TOTAL
Mediterranean countries	800	850	800	755	3205
Central and Eastern Europe	800	110	110	110	1130
Other non-member countries	50	150	250	250	700

In the case of these loans and those already signed at the end of 1992 but not yet disbursed (ECU 1 043 million for the Mediterranean countries and ECU 566 million for the countries of Central and Eastern Europe), we have assumed that an average of 10% of the loan will be disbursed in the year of signature and 30% in each of the three following years.

It is estimated that the average term will be fifteen years with a three-year period of grace.

2. Food aid for the former Soviet Union

(a) Guarantee

This is a guarantee for a bank loan of ECU 500 million, fully covered by the budget, with a term of three and a half years with three repayments at intervals of eleven months starting from the twentieth month.

(b) Borrowing/lending

An operation involving ECU 1 250 million for a maximum term of three years.

This borrowing will be divided between the various Republics of the former Soviet Union. Borrowings amounting to less than ECU 100 million will be repaid in one instalment three years after the start of the period in which the funds may be drawn. Borrowings exceeding ECU 100 million will be repaid in two instalments two years and three years after the start of the period in which the funds may be drawn.

Depending on the type of contract, there are two periods in which funds may be drawn; one starts on 20 October, the other on 15 July.

3. <u>Euratom, countries of Central and Eastern Europe</u>

Of the ECU 1 124 million involved, it is assumed that ECU 300 million will be disbursed in 1993, ECU 224 million in 1994 and ECU 200 million in each of the three following years.

It is assumed that the loans will be for an average term of twenty years with a five-year period of grace.

ANNEX

DEFINITION OF FIGURES USED IN THE REPORT

A. Authorized ceiling (Table 1)

This is the aggregate of the maximum amounts of capital authorized (ceilings) for each operation decided or of the amount proposed by the Commission for operations for which there has not yet been a Council decision.

In order to relate it to the risk which the budget might have to cover, account should be taken of the interest, which would increase the figure, and of three factors which would reduce it:

- limitation of the guarantee given to the EIB to 75% of the loans signed in the Mediterranean countries;
- operations already repaid, since the amounts concerned, except in the case of balance of payments support, are the maximum amount of loans granted and not outstanding amounts authorized;
- the amounts authorized are not necessarily taken up in full.

The breakdown of authorizations is as follows:

Member States

Balance of payments	14 000 [1]
NCI	6 830
Euratom	4 000 [2]
EIB; Spain, Greece, Portugal	1 500
Member States - total	26 330

1 Authorized amount outstanding: once this figure is reached, further loans may be granted as previous operations are repaid.

2 Including ECU 1 124 million which may be granted to the countries of Eastern Europe and the CIS.

Non-member countries

Hungary I	870
Hungary II	180
Czechoslovakia	375
Bulgaria I	290
Bulgaria II	110
Romania I	375
Romania II	80
Israel	160
Algeria	400
former Soviet Union I	408
former Soviet Union II	1 250
Baltic States	220
EIB, old protocols	3 032
EIB, Eastern Europe	1 700
EIB, Baltic States	200
EIB, Albania	50
EIB, new protocols	1 185
EIB, horizontal cooperation	1 800
Other non-member countries	750
Non-member countries - total	13 185
Grand total	40 015

B. Amount outstanding (Table 1)

This is the amount of capital still to be repaid on a given date in respect of operations disbursed.

Compared with the previous aggregate, the amount outstanding does not include loans which have not yet been disbursed nor the proportion of disbursed loans which have already been repaid. It may be described as the amount of loans which exist on a given date.

C. Annual risk

Estimated amount of principal and interest due each financial year.

This amount is calculated for:

- disbursements alone (Table 2), in which case the capital to be repaid corresponds to the amount outstanding;

- disbursements, decisions still awaiting disbursement and Commission proposals still awaiting decisions (Table 3), in which case the capital to be repaid corresponds to the ceiling on loans authorized plus, where applicable, the amounts in respect of operations proposed by the Commission and not yet decided and the amount still to be used for balance of payments operations which are much less likely to be called on than the other types of assistance.

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