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Collection Name DOBRIANSKY, PAULA: FILES

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File Folder POLAND - DEBT RESCHEDULING (7)

FOIA

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ID	Doc Type	Document Description	No of Pages	Doc Date	Restrictions
143085	CABLE	PARIS 14725 <i>R 4/8/2016 M434/4</i>	7	4/12/1984	B1
143086	PAPER	RE. DEBT RESCHEDULING <i>R 4/11/2016 M434/4</i>	4	ND	B1
143087	REPORT	RE. POLAND: PROGRESS AT PARIS CLUB <i>PAR 4/11/2016 M434/4; R 11/28/2017 M1749 #143087</i>	1	9/14/1984	B1
143088	REPORT	RE. POLAND [PG. 3 ONLY] <i>R 4/8/2016 M434/4</i>	1	3/3/1985	B1
143089	CABLE	WARSAW 02150 <i>R 4/8/2016 M434/4</i>	3	3/4/1985	B1
143090	CABLE	PARIS 6183 <i>R 4/8/2016 M434/4</i>	4	3/1/1985	B1
143091	CABLE	WARSAW 02185 <i>R 4/8/2016 M434/4</i>	2	3/5/1985	B1
143093	REPORT	RE. POLAND: STALLING FOR NEW MONEY [PG. 3 ONLY] <i>R 4/8/2016 M434/4</i>	1	5/17/1985	B1
143101	REPORT	RE. POLAND <i>R 4/11/2016 M434/4</i>	1	ND	B1 B3

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143102	CABLE	WARSAW 3140 <i>R 4/8/2016 M434/4</i>	2	3/29/1985	B1
143104	REPORT	RE. POLAND [PG. 2 ONLY] <i>R 11/29/2017 M1749/1</i>	1	6/16/1985	B1 B3
143106	REPORT	[PG. 3 AND TABLE ONLY] <i>D 4/11/2016 M434/4; PAR 11/28/2017 M1749 #143106</i>	2	1/22/1986	B1 B3
143108	REPORT	[PG. 3 AND TABLE ONLY] <i>R 4/11/2016 M434/4</i>	2	ND	B1 B3
143109	REPORT	<i>PAR 4/11/2016 M434/4; UPHELD 11/28/2017 M1749 #143109</i>	19	10/16/1986	B1 B3

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POLAND
DEBT

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 TO SECSTATE WASHDC IMMEDIATE 5614
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~~CONFIDENTIAL~~ SECTION 01 OF 03 PARIS 14725
 STATE FOR EB/OMA - HAUSER; TREASURY FOR CANNER
 E.O. 12356: DECL: OADR
 TAGS: EFIN, PL
 SUBJECT: PARIS CLUB: POLAND
 REF: PARIS 14445

1. ENTIRE TEXT - C.
2. FOLLOWING IS EXCHANGE OF LETTERS REFERRED TO IN REFTEL:

KARCZ LETTER

MR. CHAIRMAN,

WITH REFERENCE TO THE PROPOSAL THAT YOU PRESENTED LAST MARCH 21, DURING THE FINAL PHASE OF THE PARIS CLUB SESSION, I WOULD LIKE TO INFORM YOU OF THE FOLLOWING:

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1. THE POLISH SIDE CONSIDERS YOUR PROPOSAL AS AN IMPORTANT STEP TOWARD THE SEARCH FOR A SOLUTION THAT WOULD TAKE INTO ACCOUNT THE INTEREST OF EACH OF THE PARTIES.

WE NOTE WITH SATISFACTION YOUR PROPOSALS AIMING AT A RESTRUCTURING OF THE DEBT AND ITS SERVICE FOR THE YEARS 1982, 1983 AND 1984 IN THE FRAMEWORK OF A SINGLE ARRANGEMENT. WE APPRECIATE EQUALLY YOUR DECLARATION THAT YOU ARE PREPARED TO RESTRUCTURE THIS DEBT UNDER CONDITIONS MORE

FAVORABLE THAN THOSE CONTAINED IN THE 1981 AGREEMENT.

OUR POINT OF VIEW ON THIS PROBLEM RESULTS IN PART FROM THE TABLES ON THE BALANCE OF PAY-

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PAGE

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 BY RW NARA DATE 4/8/14

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MENTS THAT WERE PRESENTED TO YOU. WE UNDERSTAND THAT THESE QUESTIONS WILL BE THE SUBJECT OF DISCUSSIONS DURING THE NEXT MEETING OF THE PARIS CLUB.

WE CONSIDER YOUR PROPOSALS FOR A RESCHEDULING OF ARREARS ON THE DEBTS UNDER THE 1981 AGREEMENT AS PROOF OF YOUR BETTER UNDERSTANDING OF THE REALITIES OF THE POLISH ECONOMY AND OUR CAPACITY FOR REPAYMENT.

2. THE POLISH SIDE EXPRESSES ITS CONVICTION THAT THE FUTURE ARRANGEMENT WITH THE GROUP OF 17 CREDITORS SHOULD TAKE INTO CONSIDERATION, IN ADDITION TO THE SETTLING OF ARREARS UNDER THE 1981 AGREEMENT, OTHER VERY ESSENTIAL ELEMENTS.

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IN THE OPINION OF THE POLISH SIDE, IN ORDER THAT A FUTURE AGREEMENT MIGHT BE EFFECTIVE, IT WOULD BE NECESSARY TO HAVE:

- A/ NORMALIZATION OF FINANCIAL RELATIONS WITH THE CREDITOR COUNTRIES, WHICH SHOULD, IN PARTICULAR, TRANSLATE INTO AN URGENT OPENING OF NEW LINES OF CREDIT PERMITTING THE REALIZATION OF THE POTENTIAL PRODUCTION CAPACITY INSTALLED IN POLAND AND THE GROWTH OF EXPORTS.
- B/ NORMALIZATION OF CONDITIONS IN THE AREAS OF ECONOMIC AND TECHNICAL/SCIENTIFIC COOPERATION, IN BILATERAL RELATIONS WITH THE CREDITOR COUNTRIES, WHICH WOULD BE MANIFESTED BY A RESUMPTION OF THE WORK OF INTERGOVERNMENTAL COOPERATION COMMISSIONS, AS WAS THE CASE IN 1980 AND PREVIOUSLY.
- C/ THE ESTABLISHMENT OF A FAVORABLE CLIMATE FOR AN URGENT CONSIDERATION OF OUR REQUEST FOR MEMBERSHIP IN THE IMF AND THE IBRD.

IN ORDER TO ANALYZE THE POSSIBILITIES OF THE POLISH ECONOMY AND THE SITUATION OF ITS BALANCE OF PAYMENTS, IT WOULD BE NECESSARY TO TAKE INTO ACCOUNT THE REAL LOSSES SUFFERED BY THE POLISH ECONOMY RESULTING FROM RESTRICTIONS IMPOSED BY CERTAIN CREDITOR COUNTRIES.

WE BELIEVE THAT THERE ARE SUFFICIENT GROUNDS FOR THE SUGGESTIONS OF THE POLISH SIDE, IN THE ABOVE MENTIONED

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AREAS, BE TRANSMITTED TO THE APPROPRIATE GOVERNMENTAL
INSTITUTIONS OF THE INTERESTED COUNTRIES WITH YOUR FAVOR-
ABLE SUPPORT.
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O 121650Z APR 84

FM AMEMBASSY PARIS

TO SECSTATE WASHDC IMMEDIATE 5615

DEPARTMENT OF TREASURY WASHDC IMMEDIATE

INFO AMEMBASSY WARSAW

~~CONFIDENTIAL~~ SECTION 02 OF 03 PARIS 14725

STATE FOR EB/OMA - HAUSER; TREASURY FOR CANNER

E.O. 12356: DECL: OADR

TAGS: EFIN, PL

SUBJECT: PARIS CLUB: POLAND

- WE EXPECT THAT IT WILL BE POSSIBLE TO UNDERTAKE, IN PARALLEL AND IN THE NEAR FUTURE, MUTUALLY ADVANTAGEOUS NEGOTIATIONS OF FINANCIAL AND ECONOMIC RELATIONS BETWEEN POLAND AND THE CREDITOR COUNTRIES.

- 3. THE POLISH SIDE STATES THAT IT IS PREPARED TO PAY 15 PERCENT OF THE ARREARS ON THE 1981 AGREEMENT AND CONSIDERS THIS ACT AS PROOF OF ITS GOOD WILL TO PROGRESS IN THE NEGOTIATIONS IN PARIS, IN ORDER TO CREATE A PROPITIOUS CLIMATE FOR THE COMPLETE NORMALIZATION OF ECONOMIC RELATIONS WITH THE CREDITOR COUNTRIES UNDER CONDITIONS TAKING INTO ACCOUNT THE INTEREST OF OUR COUNTRY.

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- THE POLISH SIDE WISHES TO FULFILL ALL ITS OBLIGATIONS CONCERNING THE OTHER ARREARS IN A MANNER CLOSE TO THAT OF THE PROPOSED SCHEMA, THAT IS TO SAY, 35 PERCENT AT THE MOMENT OF THE INITIALLING OF THE AGREEMENT AND 50 PERCENT

THE DATE OF ITS SIGNATURE.

- THE REAL POSSIBILITY OF MAKING THESE PAYMENTS ONLY EXISTS AS A FUNCTION OF SUBSTANTIAL PROGRESS TOWARD THE NORMALIZATION MENTIONED UNDER POINT 2 ABOVE.

- I AM ALSO ENCLOSING PROJECTIONS OF THE BALANCE OF PAYMENTS THROUGH THE YEAR 1990. WE DO NOT FIND IT POSSIBLE TO DRAW UP A BALANCE OF PAYMENTS PROJECTION THAT DOES NOT INCLUDE ANY NEW FOREIGN CREDITS. WE SUPPOSE, HOWEVER, THAT

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IT IS NOT YOUR INTENTION TO CREATE CONDITIONS UNDER WHICH POLAND WOULD BE CUT OFF FROM FOREIGN CREDIT, SINCE THIS WOULD CONTRADICT IN A GENERAL WAY THE REASON FOR NORMALIZATION AND ITS RESULTS.

- HOPING THAT OUR POINT OF VIEW, SET OUT ABOVE, WILL BE ACCEPTABLE TO YOU AS WELL AS TO THE REPRESENTATIVES OF THE OTHER CREDITORS AS A CONSTRUCTIVE CONTRIBUTION TO THE GOAL OF A MUTUAL AGREEMENT, I REQUEST YOU, MR. CHAIRMAN, TO CONFIRM THE AGREEMENT OF THE CREDITOR COUNTRIES IN THIS MATTER AND TO ADVISE US OF THE DATE OF ARRIVAL IN WARSAW OF THE TASK FORCE. (COMPLIMENTARY CLOSE) SIGNED
ZBIGNIEW KARCOZ, WARSAW, APRIL 9, 1984.

-
CAMDESSUS LETTER

MR. CHAIRMAN,

- I ACKNOWLEDGE RECEIPT OF YOUR LETTER OF APRIL 9, AND AM APPRECIATIVE OF THE COMMENTS THAT YOU WERE SO KIND AS
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TO MAKE CONSIDERING THE INITIATIVE THAT I HAD TAKEN.

I UNDERSTAND THE EFFORTS THAT THIS REPRESENTS FROM YOUR SIDE.

- NEVERTHELESS, YOUR RESPONSE AS IT IS PRESENTED DOES NOT ALLOW ME TO PERCEIVE WITH THE COMPLETE CLARITY WHICH IS DESIRABLE AN UNRESERVED ACCEPTANCE OF THE CHAIRMAN'S

COMPROMISE. IN CONSEQUENCE, IT DOES NOT PERMIT ME TO OPEN THE SECOND PHASE OF THE NEGOTIATION.

- IN ORDER THAT NEGOTIATIONS MAY BEGIN IN THE POSITIVE CLIMATE THAT WE ALL WISH, IT APPEARS TO ME THAT IT WILL BE NECESSARY THAT YOU CLARIFY THE FOLLOWING POINTS:

- 1/ YOUR GOVERNMENT ACCEPTS THE PROPOSAL OF THE CHAIRMAN, AND THE COMMENTARIES APPEARING UNDER POINT 2 OF YOUR LETTER ONLY CONSTITUTE YOUR VIEW OF THE DESIRED OUTCOME OF THE PROCESS OF NEGOTIATION.

- 2/ SINCE IT IS NOT POSSIBLE TO MODIFY FOR ANY ONE OF THE DELEGATIONS THE COMPROMISE PROPOSED TO ALL OF THEM, I SHOULD CONFIRM TO YOU THAT A PAYMENT OF 20 PERCENT IS INDISPENSABLE TO THE AGREEMENT OF ALL PARTIES. IF IT IS IMPOSSIBLE FOR YOU TO MAKE AN IMMEDIATE PAYMENT BEYOND 15 PERCENT, KINDLY INDICATE THE DATE, WHICH MUST BE IN ANY CASE BEFORE RESUMPTION OF NEGOTIATIONS, ON WHICH THE REMAINING 5 PERCENT WILL BE SETTLED.

- 3/ AS CONCERNS THE BALANCE OF PAYMENTS FOR 1984, TAKING ACCOUNT OF THE GUARANTEED COMMERCIAL CREDITS EXPECTED AS A RESULT OF ASSURANCES WHICH

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- YOU MAY HAVE RECEIVED, OR WHICH YOU ESTIMATE TO
- BE LIKELY FROM YOUR COMMERCIAL PARTNERS, DOES NOT
- IMPLY ANY NEW IMPLICIT UNDERTAKING BY THE GROUP
- OF COUNTRIES WHICH I REPRESENT.
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O 121650Z APR 84

FM AMEMBASSY PARIS

TO SECSTATE WASHDC IMMEDIATE 5616

DEPARTMENT OF TREASURY WASHDC IMMEDIATE

INFO AMEMBASSY WARSAW

C O N F I D E N T I A L SECTION 03 OF 03 PARIS 14725

STATE FOR EB/OMA - HAUSER; TREASURY FOR CANNER

E.O. 12356: DECL: OADR

TAGS: EFIN, PL

SUBJECT: PARIS CLUB: POLAND

-
-
- SINCE THE ENTRY FOR FINANCING FROM THE BIS CAN NOT BE ACCEPTED (AS IT ASSUMES YOUR ADMISSION INTO THE IMF BEFORE THE END OF 1984 AND THERE ARE NO CLEAR INDICATIONS AVAILABLE THAT THIS IS LIKELY) YOU SHOULD APPROPRIATELY REFLECT THE MODIFICATION TO THE BALANCE OF PAYMENTS THAT WILL BE PRODUCED BY A WITHDRAWAL OF THAT ENTRY.

-
- AS LONG AS I DO NOT KNOW WHAT YOUR ANSWER ON THESE POINTS WILL BE, YOU MUST UNDERSTAND THAT IT IS IMPOSSIBLE FOR ME TO CONFIRM A MEETING OF THE TASK FORCE FOR APRIL 18. IN ORDER TO BE ABLE TO SET A NEW DATE BEFORE THE END OF THIS MONTH OR THE BEGINNING OF MAY, I WOULD APPRECIATE IT IF YOUR ANSWER COULD REACH ME BEFORE APRIL 20. (COMPLIMENTARY CLOSE) MICHEF CAMDESSUS, APRIL 10,

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1984.

GALBRAITH

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Debt Rescheduling

POLAND ✓
143086

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The U.S. has had little experience with the use of debt rescheduling as a an instrument to influence political and économic events in other countries. Our traditional approach to rescheduling has been largely reactive in that we decide to reschedule (generally in the multilateral context of the Paris Club) following a formal request by the country concerned and a USG détermination that the country was in "imminent default" (i.e. in such bad financial shape that rescheduling offers the only hope of being repaid). Thus, the USG and other governments have almost always based rescheduling decision exclusively on financial criteria. While the U.S. generally insists on IMF approval of a new lending program for countries seeking rescheduling before agreeing to proceed, the purpose of this condition has been to promote balance of payments justment and ~~thus~~ enhance ability to repay, ~~to~~ thus reducing the incidence of "rescheduling recidivism", rather than to induce fundamental structural changes consistent with our broadly foreign policy objectives.

The handling of Eastern European debt represents a dramatic departure from the traditional apolitical approach and is a potentially powerful instrument for the implementation (or abandonment) of a policy of differentiation. Thus far, only Poland and Romania have sought a rescheduling.

Poland: Official creditors rescheduled \$2.3 billion in debt service payments due in 1981 and provided Poland with

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BY AW NARA DATE 4/8/16

substantial new credits. Our objective was to weaken a major pillar of the Warsaw Pact by: (1) helping to insure that the nascent liberalization process did not founder on the shoals of economic disruption; and (2) encouraging the establishment of a more Western-oriented economic structure in Poland through the implementation of far reaching economic reforms. In pursuit of the latter objective, the Western governments kept Poland on a short economic leash, agreeing to reschedule Polish debt at only six-month intervals and conditioning successive rescheduling agreements on the implementation of the economic reform program which the Government of Poland was to implement in January, 1982.

With the imposition of martial law in December, 1981, the NATO Alliance agreed to suspend discussions on rescheduling of Poland's 1982 debt pending: (1) lifting of martial law; (2) the release of political prisoners; and (3) the restoration of a meaningful dialogue between the government, the Church and Solidarity. The continued refusal to reschedule will increase the risk of a Polish default and will drive Poland closer to the Soviet Union. However, it is not clear that dropping the three conditions and agreeing to reschedule would lead to a favorable evolution of the Polish political situation. Accordingly, rescheduling would appear to be a weak political instrument viewed in a narrow perspective of the Polish situation.

Romania: The GOR has explained informally an official rescheduling. All official creditors, with the exception of the U.S., have agreed. The U.S. has indicated that it would be premature to make a decision on an official rescheduling absent IMF Executive Board approval of a new lending program for Romania. There are arguments for and against our agreeing to a Paris Club rescheduling of Romania. Arguing for doing so are the financial considerations involved in increasing the chances of being repaid. Indications are that banks will not reschedule in the absence of an official rescheduling. Moreover, the IMF staff will not send its non-approved lending program to the Executive Board unless they are certain that a private rescheduling will take place. Thus, our continued refusal to agree to participate in an official rescheduling could well (a) scuttle Romania's IMF program at a time when the prospects it offers of balance of payments adjustment and IMF loans offer the best chance of orderly -- if stretched out -- repayment. There are political reasons for rescheduling Romania's debt. In effect, we are now holding the re-establishment of a more normal U.S.-Romania bilateral financial relationship hostage to GOR measures to get its economic house in order. A decision not to reschedule would be viewed by the GOR as a political decision calculated to downgrade sharply the bilateral relationship; and would drive Romania toward a much closer economic, and therefore political, relationship with the USSR. Therefore, a rescheduling would help the GOR

quasi arm's length relationship with the Warsaw Pact.

Arguing against rescheduling is the risk of diversion of Western resources (IMF loans, as well as new financing the Romanians might obtain from banks or governments) to the USSR, which is also experiencing a difficult cash/flow problem. It is not at all clear that such diversion could or would occur, but it cannot be ruled out. Nonetheless, a decision to reschedule Romanian debt while continuing to hold back on Poland would constitute a powerful statement on differentiation. It would also help lift the veil of political uncertainty which is adversely affecting such countries as Hungary and Yugoslavia. Accordingly, the modulated use of rescheduling can be an effective instrument in implementing a policy of differentiation.

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Paula DEBT

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143087

BUREAU OF INTELLIGENCE AND RESEARCH - ANALYSIS - SEPTEMBER 14, 1984

1. POLAND: PROGRESS AT PARIS CLUB, BUT NO PANACEA

Poland is prepared to pay all arrears owed the United States under the 1981 Paris Club agreement, thus clearing the way for negotiations on Poland's 1982-84 official debts. Although significant progress has been made in the effort to normalize financial relations with the West, Warsaw's hopes for sustained recovery from the economic crisis will depend on further cooperation from Western creditors.

* * *

The Poles agreed in April to make a 20 percent "down payment" on arrears due official creditors under the 1981 Paris Club rescheduling agreement. However, Warsaw opposed payment of unrescheduled principal and interest due the United States under a 1981 bilateral agreement, because implementing agreements had not been signed. The ploy was designed in part to separate the United States from the rest of the Club on the issue; in addition, the Poles might have had difficulty coming up with the money. Some other creditors initially received only part of their 20 percent payments.

The remaining arrears under the multilateral 1981 agreement are to be paid before the signing of a Paris Club agreement covering 1982-1984 official debt. Club members are prepared to offer generous terms for rescheduling those debts, so negotiations should not prove difficult. Realistically, the Club has no alternative. After meeting their obligations to Western commercial banks and paying off the balance of the arrears due governments, the Poles will be strapped for funds.

The 1984 rescheduling agreement with Western commercial banks (covering 1984-1987 maturities) provided some help, though the banks were several million dollars short of the \$645 million they were supposed to provide in new credit. Warsaw's acceptance of the reduced package of new money last month underscored a strong desire to normalize financial relations with the West.

Even with agreements with the banks and the Paris Club in place, Poland will have considerable difficulty managing its \$27 billion debt. Warsaw faces the prospect of having to reschedule previously rescheduled debt when payments begin falling due next year. IMF membership could provide some relief, but the entry process would take months. Negotiations on a stabilization program would likely result in further delays before sizable credits became available. Warsaw must continue to depend on its creditors for favorable rescheduling terms and new credit, a situation that should allow Western governments to retain a measure of leverage with the regime.

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3. POLAND: ANOTHER PAYMENTS CRUNCH IN 1985

Poland will meet with its official creditors (Paris Club) on March 4-5 to discuss the rescheduling of 1985 obligations. Even a generous rescheduling agreement would probably leave Poland short of its debt-payments goal. In an effort to shore up their financial position this year, the Poles will continue to press Western creditors--and perhaps approach other non-bloc countries--for new credits and trade assistance.

* * *

Poland's hard-currency debt payments may total \$2.8 billion in 1985, according to recent Treasury estimates (see table). At best, however, the current-account surplus and drawdown of official reserves may cover only \$2.2 billion, leaving a \$600-million gap. The gap could grow to \$1 billion if domestic conditions or international terms of trade worsen.

Given the unlikelihood that Poland will normalize its financial relations with the West any time soon, insolvency remains a real concern. Since IMF benefits remain remote, Poland's options are limited and not particularly attractive. If requests for more aid are unsuccessful:

--Tougher austerity measures might close the gap but risk political and social unrest.

--Assigning low priority to debt payments would block any return to creditworthiness and increase the eventual costs of dealing with the debt problem.

Poland may be able to tough out its debt problems this year. The Poles are canvassing Western creditors to seek new credits before the signing of the 1982-84 rescheduling agreement, which may occur by mid-year. Sweden appears receptive to normalizing financial relations prior to the signing. Some of the other Paris Club creditors may join Sweden. If so, Poland could conceivably receive \$450 million in new credits, including money from commercial as well as official sources.

Libya, Iran, and China are possible candidates outside of the Paris Club to provide additional assistance to the Poles, perhaps enough to allow Poland to service its remaining debt. These countries could supply Poland with crude oil and raw and intermediate goods through barter trade arrangements. This assistance would free Polish hard-currency reserves for Western debt payments.

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POLAND

DEBT

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~~C O N F I D E N T I A L~~ SECTION 01 OF 02 WARSAW 02150

E. O. 12356: DECL: OADR
TAGS: EFIN PL
SUBJECT: MFA DEMARCHE PROPOSING U. S. - POLISH TALKS
ON PARIS CLUB RESCHEDULING AND NEW CREDITS

REF: WARSAW 1949

1. WARSAW 1949

1. (C - ENTIRE TEXT)

2. SUMMARY: DCM WAS CALLED TO MFA MARCH 4 TO RECEIVE DIPLOMATIC NOTE PROPOSING BILATERAL TALKS ON RESCHEDULING POLISH DEBT TO USG WITHING FRAMEWORK OF THE PARIS CLUB AGREEMENT AND ON PROVIDING NEW U. S. CREDITS. THE NOTE IS SIMILAR TO THAT GIVEN BY THE POLES TO ALL THE OTHER PARIS CLUB CREDITORS WITH THE NOTABLE EXCEPTION THAT IT DOES NOT CALL FOR A SPECIFIC AMOJNT OF DESIRED NEW MONEY FROM THE U. S. IN THE ENSUING DISCUSSION MFA AND MINISTRY OF FINANCE REPS. STRESSED THAT THE PAYMENTS DUE IN 1985 BY POLAND CANNOT BE MET WITHOUT A CREDIT INFUSION OF DOL 1.2 BILLION. THE POLES ARE ALSO OFFERING TO HAVE THE NEW CREDITS DIRECTLY LINKED TO COMMODITY PURCHASES IN THE CREDITOR COUNTRIES, THUS FREEING POLAND FROM PAYING CASH FOR THOSE IMPORTS AND ALLOWING THAT MONEY TO BE USED TO MEET THIS YEAR'S OBLIGATIONS. DCM, STRESSING HE HAD NO INSTRUCTIONS ON THE MATTER, NOTED THAT RECENT POLISH ACTIONS HAVE DAMAGED THE ALREADY STRAINED BILATERAL RELATIONSHIP. IN THIS ATMOSPHERE HE SUGGESTED IT IS HARDLY LIKELY WASHINGTON WILL AGREE TO ANY NEW CREDIT LINES, ALTHOUGH HE THOUGHT, SPEAKING PERSONALLY, THAT BILATERAL RESCHEDULING TALKS TO CONCLUDE THE UMBRELLA PARIS CLUB AGREEMENT COULD BE AN APPROPRIATE TOPIC FOR U. S. - POLISH DISCUSSION. TEXT OF THE MFA NOTE IS BEING TRANSMITTED SEPTTEL. END SUMMARY.

3. DEPARTMENT III (N. AND S. AMERICA) DIRECTOR BIALY INVITED DCM TO MFA MARCH 4 TO PRESENT A NOTE PROPOSING BILATERAL NEGOTIATIONS ASAP TO: A) DISCUSS ARRANGE-

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BY RW NARA DATE 4/8/16

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DTG: 041447Z MAR 85 PSN: 023408

MENTS "PERMITTING A PROMPT NORMALIZATION OF CREDIT RELATIONS AND ELIMINATION OF OBSTACLES IN ECONOMIC RELATIONS" BETWEEN POLAND AND THE U. S.; B) PREPARE A BILATERAL AGREEMENT ON RESCHEDULING POLAND'S 1982-84 GUARANTEED DEBTS; AND C) DISCUSS THE "CONDITIONS AND WAYS OF A FURTHER EXPANSION OF COMMERCIAL EXCHANGES AND ECONOMIC COOPERATION, INCLUDING THE FACILITATION OF PAYMENT, FINANCE AND CREDIT ARRANGEMENTS TO STIMULATE INCREASED IMPORTS FROM THE UNITED STATES TO POLAND." THE NOTE IS NEARLY IDENTICAL IN SUBSTANCE TO SIMILAR ONES THE POLES DELIVERED TO ALL THE OTHER PARIS CLUB MEMBERS (REFTEL), WITH THE EXCEPTION THAT IT DOES NOT REQUEST A SPECIFIC AMOUNT OF NEW MONEY FROM THE U. S.

4. IN THE ENSUING DISCUSSION, BIALY, ASSISTED BY A SPECIALIST FROM THE MINISTRY OF FINANCE, NOTED THAT POLAND UNDER THE TERMS OF THE PARIS CLUB AGREEMENT INITIALLED IN JANUARY WILL HAVE TO REPAY BETWEEN 1.5 AND 1.6 BILLION DOLLARS IN 1985, CONSISTING OF 1981 ARREARS AND CURRENT INTEREST ON THE RESCHEDULED 1982-84 DEBT. THIS AMOUNT, THEY STRESSED, CAN IN FACT BE PAID THIS YEAR ONLY IF THERE IS AN INFLOW OF NEW CREDITS. THE POLISH SIDE INITIALLED THE AGREEMENT IN GOOD FAITH, WANTS TO SIGN THE MULTILATERAL AGREEMENT ASAP, AND WISHES TO COMMIT ITSELF TO ALL THE TERMS ARISING THEREFROM, BUT TO MEET THOSE TERMS IT SIMULTANEOUSLY REQUIRES AN ACCELERATION OF THE "NORMALIZATION OF CREDIT RELATIONS" AS WELL AS PROVISION OF NEW GUARANTEED CREDITS. FOR 1985, THEY SAID, POLAND REQUIRES IN ALL DOLS 1.2 BILLION (U. S.) FROM THE PC COUNTRIES. THESE FUNDS WOULD BE TIED TO COMMODITY PURCHASES IN THE COUNTRIES PROVIDING THEM, THUS FREEING POLAND FROM BUYING NEEDED IMPORTS WITH CASH AND ALLOWING THAT MONEY TO BE USED TO MEET THE

1985 OBLIGATIONS. IN THE CASE OF THE U. S. , NEW CREDITS MADE AVAILABLE IN 1985 AND 1986 WOULD BE USED TO FINANCE PURCHASES OF CEREALS AND FODDER, MACHINERY, AND CHEMICAL PRODUCTS.

5. TURNING BRIEFLY TO THE TALKS ON RESCHEDULING THE 1982-84 DEBT, BIALY STRESSED THAT CERTAIN DETAILS CAN BE DISCUSSED ONLY IN THE BILATERAL FRAMEWORK, MOST NOTABLY THE ISSUE OF INTEREST RATES TO BE CHARGED.

6. BIALY EMPHASIZED THAT THESE BILATERAL TALKS ON RESCHEDULING (AND, THE POLES HOPE, NEW CREDITS) SHOULD PRECEDE THE SIGNING OF THE MULTILATERAL AGREEMENT, SO AS TO PERMIT THE LATTER TO TAKE PLACE. ONCE IT IS SIGNED, THEN THE BILATERALS WOULD BE FORMALLY CONCLUDED AS WELL.

7. BIALY PROPOSED THAT THE U. S. - POLISH BILATERAL BEGIN THIS MONTH OR AT THE LATEST IN APRIL, IN WARSAW. (ACCORDING TO THE NOTE THE MEETING SHOULD BE IN WARSAW OR ANOTHER MUTUALLY-AGREED PLACE "SHOULD THE ARRIVAL OF A DELEGATION OF THE GOVERNMENT OF THE UNITED
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STATES OF AMERICA TO POLAND BE "INCONVENIENT.")

8. DCM, IN ACCEPTING THE NOTE AND AGREEING TO CONVEY ITS CONTENTS AND THE ORAL CLARIFICATIONS TO WASHINGTON, POINTED OUT THAT HE OF COURSE HAD NO INSTRUCTIONS AT THE MOMENT FOR RESPONDING TO THE DEMARCHE. HE NOTED, HOWEVER, THAT THE ALREADY STRAINED BILATERAL RELATIONSHIP HAD BEEN SEVERELY BURDENED BY THE EXPULSION OF THE EMBASSY'S DEFENSE ATTACHE, AN INCIDENT FOR WHICH WE HOLD THE POLISH SIDE FULLY RESPONSIBLE. OTHER RECENT GOP MOVES HAVE LIKEWISE NOT HELPED THE CLIMATE OF BILATERAL RELATIONS. DCM THUS THOUGHT IT QUITE UNLIKELY THAT WASHINGTON WOULD FIND THIS A PARTICULARLY PROPITIOUS MOMENT TO ACCEDE TO THE POLISH SIDE'S REQUEST FOR NEW CREDITS. ON THE OTHER HAND, BILATERAL DISCUSSIONS ON RESCHEDULING 1982-84 MATURITIES AND INTEREST WITH A VIEW TO SIGNING THE MULTILATERAL PARIS CLUB RESCHEDULING AGREEMENT MIGHT BE A REASONABLE OBJECTIVE.

9. BIALY RESPONDED THAT THE PRESENT POLISH PROPOSAL FOLLOWS UP ON THE JANUARY PARIS CLUB INITIALLING, IS A SIGN OF POLISH GOOD FAITH TO REPAY ITS DEBTS, AND IS MADE IN THE MULTILATERAL AND NOT BILATERAL CONTEXT. HE CONCLUDED BY STRESSING THAT AS U. S. REPRESENTATIVE AT THE U. N. THEMSELVES HAVE SAID ECONOMIC RELATIONS BETWEEN STATES SHOULD NOT BE POLITICIZED. THE POLISH SIDE HOPES FOR RESOLUTION OF THIS MATTER IN A NON-POLITICAL, BUSINESS-LIKE MANNER.

10. DCM REPEATED AGAIN THAT THE POLISH PROPOSAL COULD NOT BE VIEWED IN ISOLATION FROM THE BILATERAL ATMOSPHERE. IN CONCLUSION, HE UNDERTOOK TO BE BACK IN TOUCH WITH ANY RESPONSE ONCE WASHINGTON HAS HAD A CHANCE TO CONSIDER THE MATTER.
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EOB453

WARSAW 2146
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E. O. 12356: N/A
TAGS: EFIN, PL
SUBJECT: TRANSMITTAL OF MFA NOTE ON PARIS CLUB RESCHEDULING
AND NEW CREDITS

1. THERE FOLLOWS IN PARA. 2 AN MFA UNOFFICIAL TRANSLATION OF ITS NOTE PROPOSING BILATERAL NEGOTIATIONS WITH THE U. S. ON DEBT RESCHEDULING AND NEW CREDITS TO EFFECT THE PARIS CLUB AGREEMENT INITIALLED LAST JANUARY. NOTE WAS HANDED TO DCM BY MFA DEPARTMENT III DIRECTOR BIALY DURING MARCH 4 MEETING. SEPTEL REPORTS SUBSTANCE OF THE DISCUSSION.

2. BEGIN TEXT:
(COMPLIMENTARY OPENING)

THE GOVERNMENT OF THE POLISH PEOPLE'S REPUBLIC WOULD LIKE TO REFER TO THE RESULTS OF THE MEETING BETWEEN THE REPRESENTATIVES OF THE SEVENTEEN PARTICIPATING CREDITOR COUNTRIES AND THE POLISH DELEGATION HELD AT THE PARIS CLUB ON JANUARY 14 AND 15, 1985. DUE TO THE ATTITUDE OF THE DELEGATIONS OF THE PARTICIPATING CREDITOR COUNTRIES AND THE ATTITUDE OF THE POLISH DELEGATION AT THIS MEETING, A MULTILATERAL AGREEMENT WAS REACHED AND THE AGREED MINUTE ON THE CONSOLIDATION OF THE DEBT OF POLAND WAS INITIALLED. IT SPECIFIES THE TERMS OF REPAYMENTS BY POLAND TO THE SEVENTEEN PARTICIPATING CREDITOR COUNTRIES OF FINANCIAL OBLIGATIONS FALLING DUE IN 1982 THROUGH 1984. THE LETTERS CONCERNING THE PAYMENTS OF ARREARS PURSUANT TO THE AGREEMENTS SIGNED IN 1981 ON THE BASIS OF THE PARIS PROTOCOL OF APRIL 27, 1981, WHICH ARE TO BE EXCHANGED BETWEEN THE CHAIRMAN OF THE PARIS CLUB AND THE CHAIRMAN OF THE POLISH DELEGATION, WERE ALSO AGREED UPON AND INITIALLED.

THE GOVERNMENT OF THE POLISH PEOPLE'S REPUBLIC EXPRESSES THE HOPE THAT THE AGREED MINUTE INITIALLED IN PARIS WILL LEAD TO A SIGNIFICANT PROGRESS IN THE NORMALIZATION OF FINANCIAL AND CREDIT RELATIONS BETWEEN OUR TWO COUNTRIES AND IS CONFIDENT THAT IT WILL ALSO LEAD TO THE RESUMPTION BY THE APPROPRIATE INSTITUTIONS OF NEW GUARANTEED CREDITS FOR POLAND.

ACCORDING TO THE LETTER PRESENTED BY THE CHAIRMAN

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DTG: 011447Z MAR 85 PSN: 023588

OF THE POLISH DELEGATION TO THE CHAIRMAN OF THE PARIS CLUB DATED JANUARY 15, 1985, WHICH HAS BEEN TRANSMITTED TO THE AUTHORITIES OF THE UNITED STATES OF AMERICA, THERE IS AN OBVIOUS INTERDEPENDENCE BETWEEN THE REAL ABILITY OF THE POLISH SIDE TO FULFILL ITS FINANCIAL OBLIGATIONS AND THE NORMALIZATION OF TRADE AND CREDIT RELATIONS BETWEEN POLAND AND THE CREDIT COUNTRIES.

IT IS, THEREFORE, EVIDENT THAT SUCH NORMALIZATION IS ONE OF THE BASIC CONDITIONS FOR UTILIZING THE INDUSTRIAL PRODUCTION CAPACITY AND ENSURING APPROPRIATE SUPPLIES OF RAW AND OTHER MATERIALS, MACHINERY AND EQUIPMENT TO OTHER, INTER ALIA, NUMEROUS FACTORIES WHICH HAVE BEEN BUILT ON THE BASIS OF WESTERN TECHNOLOGY.

SUCH NORMALIZATION IS ALSO ONE OF THE PREREQUISITIES INDISPENSABLE TO THE NECESSARY INCREASE OF EXPORTS THAT POLAND INTENDS TO MAKE TO THE MARKET-ECONOMY COUNTRIES. FURTHER STRENGTHENING OF THE POSITIVE RESULTS OBTAINED BY POLAND IN EQUILIBRATING ITS BALANCE OF PAYMENTS DURING 1982-1984 THROUGH EMPLOYMENT OF INTERNAL FACTORS REQUIRES NOW THAT POLAND'S OWN EFFORTS BE SUPPLEMENTED BY REAL AND CONSTRUCTIVE COOPERATION ON THE PART OF HER TRADING PARTNERS OF THE CREDITOR COUNTRIES.

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IN THIS CONNECTION AND IN ORDER TO CREATE NECESSARY CONDITIONS FOR AN EARLY SIGNING AND IMPLEMENTATION OF THE AGREED MINUTE INITIALLED ON JANUARY 15, 1985, THE GOVERNMENT OF THE POLISH PEOPLE'S REPUBLIC REQUESTS THE GOVERNMENT OF THE UNITED STATES OF AMERICA FOR THE EARLIEST POSSIBLE BEGINNING OF BILATERAL TALKS BETWEEN AUTHORIZED DELEGATIONS OF BOTH COUNTRIES.

THE TALKS SHOULD BE CONDUCTED WITH THE AIM TO:

- DISCUSS ARRANGEMENTS PERMITTING A PROMPT NORMALIZATION OF CREDIT RELATIONS AND ELIMINATION OF OBSTACLES IN ECONOMIC RELATIONS BETWEEN POLAND AND THE UNITED STATES OF AMERICA.
- PREPARE A BILATERAL AGREEMENT ON RESCHEDULING POLAND'S GUARANTEED DEBTS FALLING DUE IN THE PERIOD 1982-1984.
- DISCUSS THE CONDITIONS AND WAYS OF FURTHER EXPANDING COMMERCIAL EXCHANGES AND ECONOMIC COOPERATION, INCLUDING THE FACILITATION OF PAYMENT, FINANCE AND CREDIT ARRANGEMENTS TO STIMULATE INCREASED IMPORTS FROM THE UNITED STATES TO POLAND.

THE GOVERNMENT OF THE POLISH PEOPLE'S REPUBLIC WOULD LIKE TO INFORM THAT THE POLISH SIDE IS INTERESTED IN OBTAINING MEDIUM AND LONG-TERM GUARANTEED LINES OF CREDIT TO BE DRAWN IN 1985 AND 1986 FOR FINANCING IMPORTS TO POLAND OF SUCH COMMODITIES AS: (1) CEREALS AND FODDER, (2) MACHINERY, (3) CHEMICAL PRODUCTS.

ANTICIPATING THAT THE GOVERNMENT OF THE UNITED STATES OF AMERICA WILL ADOPT A FAVORABLE APPROACH TOWARD THE FOREGOING MATTERS, THE GOVERNMENT OF THE POLISH PEOPLE'S REPUBLIC WISHES TO INFORM THAT AN AUTHORIZED POLISH DELEGATION INCLUDING OFFICIALS FROM THE MINISTRY OF FINANCE, MINISTRY OF FOREIGN TRADE AND BANK HANDLOWY W WARSZAWIE S. A. IS READY TO MEET IMMEDIATELY THE REPRESENTATIVES OF THE GOVERNMENT OF THE UNITED STATES OF AMERICA AND ITS APPROPRIATE AGENCIES IN ORDER TO CONDUCT PROPER BILATERAL NEGOTIATIONS ON THE ABOVE MENTIONED ISSUES.

CONSIDERING THE URGENCY OF THE MATTER AND THE NECESSITY TO HOLD MEETINGS BETWEEN THE REPRESENTATIVES OF POLAND AND THE REPRESENTATIVES OF THE SEVENTEEN PARTICIPATING CREDITOR COUNTRIES, THE GOVERNMENT OF THE POLISH PEOPLE'S REPUBLIC ANTICIPATES THAT THE

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DATE OF A MEETING WILL BE PROPOSED IN A SHORT ITME
AND THAT IT WILL TAKE PLACE EITHER IN WARSAW OR--
SHOULD ARRIVAL OF A DELEGATION OF THE GOVERNMENT OF
THE UNITED STATES OF AMERICA TO POLAND BE INCONVENIENT
--IN ANOTHER MUTUALLY AGREED PLACE.
(COMPLIMENTARY CLOSE)

END TEXT.
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PAGE 01 WARSAW 2185 DTG: 051333Z MAR 85 PSN: 025646
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THAT FORUM. END SUMMARY AND CONCLUSIONS.

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E.O. 12356: DECL: OADR
TAGS: EFIN, PL
SUBJECT: PARIS CLUB AND POLISH PUSH FOR CREDITS

REF: A/ WARSAW 2150; B/ WARSAW 2034

1. ~~CONFIDENTIAL~~ - ENTIRE TEXT.

2. SUMMARY AND CONCLUSIONS. DURING MARCH 4 MEETING OF OECD COUNTRY ECON COUNSELORS, THIRTEEN PARIS CLUB MEMBER EMBASSIES WERE IN A POSITION TO PROVIDE DATA ON AMOUNTS OF CREDIT SOUGHT BY WARSAW, THE TYPES OF COMMODITIES SUCH CREDITS WOULD COVER AND THE CIRCUMSTANCES OF THE POLISH REQUEST. FROM THAT LARGE SAMPLING A PATTERN EMERGES WHEREBY MOST COUNTRIES WERE REQUESTED TO OPEN CREDIT LINES FOR TWO YEARS IN THE RANGE OF 50 TO 60 PERCENT PER YEAR OF THEIR RECENT ANNUAL EXPORTS TO POLAND, ALTHOUGH THERE WERE STRIKING EXCEPTIONS TO THE PATTERN. FOR 1985 REQUESTS RANGE FROM USDOLS 15 MILLION FROM SPAIN AND NORWAY TO USDOLS 450 MILLION FROM THE FRG. THE MAIN COMMODITY GROUPS TO BE COVERED WERE THE TRADITIONAL ONES WITH VARIOUS PARTNERS, BUT WERE OVERWHELMINGLY FOCUSED ON CEREALS AND FODDERS, CHEMICAL PRODUCTS, METALLURGICAL PRODUCTS, AND MACHINERY, EQUIPMENT AND PARTS. GOP PRESENTATION OF NOTES WAS UNVARIABLY TO CHIEFS OF MISSION BY EITHER DEPUTY MINISTER OF FOREIGN AFFAIRS KUCZA OR THE APPROPRIATE OFFICE DIRECTOR. WHILE NONE OF THE DIPLOMATIC NOTES WAS REPORTED TO CONTAIN CONCRETE STATEMENTS ON LINKAGE BETWEEN NEW CREDITS AND POLAND'S SIGNING OF THE PARIS CLUB MULTILATERAL AGREEMENT, THE IMPLIED CONDITIONALITY IS UNMISTAKABLE. IN ADDITION TO FRANK STATEMENTS IN A NUMBER OF CONVERSATIONS AT THE TIME OF PRESENTATION OF NOTES ABOUT POLAND'S INABILITY TO MEET ITS COMMITMENTS ABSENT CREDITS, BOTH THE FINNS AND AUSTRIANS REPORT THAT THEY WERE SPECIFICALLY ASKED TO SIGN A CREDIT AGREEMENT PRIOR TO THE SIGNING OF THE MULTILATERAL RESCHEDULING. MEANWHILE, TWO COUNTRIES (CANADA AND NORWAY) HAVE ALREADY SCHEDULED THEIR BILATERAL NEGOTIATIONS ON RESCHEDULING (BETWEEN NOW AND MID-APRIL) ALTHOUGH THEY HAVE NOT TAKEN CONCRETE DECISIONS ON HOW TO RESPOND TO THE CREDIT DRIVE IN

3. SPECIFIC COUNTRY REQUESTS IN USDOLLARS ARE NOTED BELOW, ALONG WITH THE MAIN COMMODITY CATEGORIES TO BE COVERED. FIGURES COLLECTED INFORMALLY IN USDOLLARS ON LEVELS OF POLISH IMPORTS FROM INDIVIDUAL PARTNERS ARE ALSO PROVIDED. REQUESTS TO THE THIRTEEN PARIS CLUB MEMBERS LISTED TOTAL USDOLS 1.420 BILLION IN 1985 AND USDOLS 1.547 BILLION IN 1986, CONFIRMING KARCZ'S COMMENT TO US THAT THE TOTAL WAS ABOUT USDOLS 1.7 BILLION.
--SAPIN: 1985, 15 MILLION; 1986, 18 MILLION. POLISH IMPORTS, 33 MILLION. METALLURGICAL PRODUCTS, CHEMICAL PRODUCTS, FOOD PRODUCTS, TRANSPORTATION INDUSTRY.
-- NORWAY: 1985, 15 MILLION; 1986, 18 MILLION. POLISH IMPORTS, 25 MILLION. CHEMICAL PRODUCTS, FOOD PRODUCTS, FORESTRY PRODUCTS ORES (ESPECIALLY IRON ORE FOR THE COAL INDUSTRY ACCORDING TO THE NORWEGIAN EMBASSY). NORWAY'S BILATERAL DISCUSSIONS ARE SCHEDULED FOR APRIL 10 IN WARSAW.
--FINLAND: 1985, 25 MILLION; 1986, 28 MILLION. POLISH IMPORTS, 33 MILLION. METALLURGICAL PRODUCTS, FORESTRY PRODUCTS, MACHINERY, EQUIPMENT AND PARTS, CHEMICAL PRODUCTS. (NOTE: THIS REQUEST IS AROUND BT

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80 PERCENT OF IMPORTS AND TAKES PLACE IN A TRADE SCENE CHARACTERIZED BY A HEAVY -- USDOLS 135 MILLION -- DEFICIT DUE TO FINNISH PURCHASES OF POLISH COAL.)
-- BELGIUM: 1985, 25 MILLION; 1986, 28 MILLION. POLISH IMPORTS 60 MILLION. CHEMICAL PRODUCTS, METALLURGICAL PRODUCTS, MACHINERY, EQUIPMENT AND PARTS.
-- DENMARK: 1985, 50 MILLION; 1986, 50 MILLION. POLISH IMPORTS, 60 MILLION. MACHINERY, EQUIPMENT AND PARTS, CHEMICAL PRODUCTS, CEREALS AND FODDER. (NOTE: LIKE WITH FINLAND, DENMARK CARRIES A HEAVY TRADE DEFICIT BECAUSE OF COAL PURCHASES.)
-- NETHERLANDS: 1985, 60 MILLION; 1986, 65 MILLION. POLISH IMPORTS 120 MILLION. CHEMICAL PRODUCTS, MACHINERY, EQUIPMENT AND PARTS, CEREALS AND FODDER, CONSUMER GOODS AND AGRICULTURAL PRODUCTS.
-- CANADA: 1985, 130 MILLION; 1986, 130 MILLION. POLISH IMPORTS, 40 MILLION. (NOTE: ACCORDING TO CANADIAN EMBASSY, TRADITIONAL PATTERN WOULD BE HIGHER BY USDOLS 100 MILLION FOR GRAIN SALES.) CEREALS AND FODDER, MACHINERY, EQUIPMENT AND PARTS, CHEMICAL PRODUCTS, PHARMACEUTICALS.
--FRANCE: 1985, 130 MILLION; 1986, 150 MILLION. POLISH IMPORTS, 210 MILLION. CHEMICAL PRODUCTS, METALLURGICAL PRODUCTS, CEREALS AND FODDER, MACHINERY, EQUIPMENT AND PARTS.
-- ITALY: 1985, 130 MILLION; 1986, 150 MILLION. POLISH IMPORTS, 210 MILLION. CHEMICAL PRODUCTS, MACHINERY, EQUIPMENT AND PARTS, TEXTILES, METALLURGICAL PRODUCTS. (NOTE: THE ITALIAN EMBASSY HERE WAS SOMEWHAT SURPRISED THAT THE REQUEST WAS NOT SOMEWHAT HIGHER IN VIEW OF PLANS FOR COOPERATIVE PROJECTS NOT YET REFLECTED IN TRADE STATISTICS.)
-- AUSTRIA: 1985, 150 MILLION; 1986, 160 MILLION. POLISH IMPORTS, 150 MILLION. CHEMICAL PRODUCTS, METALLURGICAL PRODUCTS, MACHINERY, EQUIPMENT AND PARTS, CEREALS AND FODDER.
-- UNITED KINGDOM: 1985, 240 MILLION; 1986, 250 MILLION. POLISH IMPORTS, 200 MILLION. CHEMICAL PRODUCTS, CEREALS AND FODDER.
-- FRG: 1985, 450 MILLION; 1986, 500 MILLION. POLISH IMPORTS, 900 MILLION. MACHINERY, EQUIPMENT AND PARTS, CHEMICAL PRODUCTS, TEXTILES, CEREALS AND FODDER, METALLURGICAL PRODUCTS.
-- USA: NO AMOUNTS SPECIFIED. POLISH IMPORTS, 225 MILLION. CEREALS AND FODDER, MACHINERY, EQUIPMENT

4. COMMENT. WHILE THERE APPEARS TO BE SOME PATTERN TO MANY OF THE CREDIT REQUEST LEVELS, THE NUMBER OF EXCEPTIONS IS LARGE ENOUGH TO LEAVE OPEN TO SERIOUS QUESTION WHAT TYPE OF ECONOMIC OR OTHER LOGIC DECTATED THE FULL LIST. THE UK IN PARTICULAR STANDS OUT WITH POLAND'S REQUEST FOR ALMOST 125 PERCENT OF THE REGULAR IMPORT LEVEL IN CREDITS AS OPPOSED TO THE 50-60 PERCENT NORM. OTHER EXCEPTIONS SEEM TO BE GROUPED AMONG THOSE WHO HAVE BEEN SIGNIFICANT SUPPLIERS OF GRAINS OR CUSTOMERS OF POLISH COAL. IN BROADER ECONOMIC TERMS, IT APPEARS THAT THE CREDITS SOUGHT BY POLAND FROM ITS PRESENT CREDITORS ARE CONCENTRATED SOLELY IN TRADITIONALLY TRADED GOODS AND ARE NOT INTENDED TO REFLECT APPLICATION OF POLISH ECONOMIC PRIORITIES AS DEFINED IN RELEVANT PLANS OR REFORM OUTLINES.
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3. POLAND: STALLING FOR NEW MONEY

Poland will meet with its official creditors (the Paris Club) today to discuss the rescheduling of 1982-85 obligations. Given the unlikelihood that Poland will boost hard-currency exports this year, insolvency remains a serious concern. Some Paris Club members may provide the needed new money but would likely link this to the signing of rescheduling agreements.

* * *

Official debt coming due this year exceeds \$1 billion. At best, the current-account surplus and other flows of funds may cover \$600 million. The hard-currency gap could easily reach \$1 billion if terms of trade or domestic conditions worsen.

Poland's ability to service debt is limited in the absence of financial normalization with the West. Any effort to squeeze the population or the economy further runs the following risks:

- tougher austerity measures could trigger social and political unrest;
- tighter restrictions on the import of capital goods would retard industrial recovery;
- using private bank deposits (\$1.1 billion) to finance the gap risks a reduction of remittances from abroad.

New money. The Poles may be able to tough out their debt problems if some \$150-200 million in new credits were to materialize. The FRG and the UK recently pledged around \$52 million in new credits, linking them to payment of 1981 arrears and a rescheduling of maturities due through 1985. Among others, Austria, Switzerland, Sweden, and Italy are likely to follow suit.

Other forms of aid might enable the Poles to narrow their financing gap. The Soviets recently agreed to buy back with hard currency a steel-rolling mill which they sold the Poles in 1981. China and Libya could provide an additional \$100 million in barter trade involving raw materials, agricultural goods, and energy, allowing the Poles to trim hard-currency imports.

Debt moratorium and the IMF. Pressure is on Western countries to provide new money to keep financial negotiations on track. Otherwise, the Poles will continue to enjoy a de facto moratorium on debt payments through 1985. In 1986, however, pressure should be on the Poles, who will risk IMF benefits--assuming they join the Fund by then--if they are not current on debt payments.

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POLAND: RESCHEDULING OFFICIAL DEBT

After long delay Poland signed an agreement on July 15 rescheduling official debt due in 1982-84. Honoring the agreement this year is likely to require obtaining \$150-200 million in new money from Western governments. The expected entry of Poland into the IMF in 1986 could encourage the West to provide still more new credit if the regime were willing to implement a tough adjustment program.

* * *

The agreement reschedules approximately \$12 billion in overdue debt over a period of 11 years. To implement the agreement Poland must now sign bilateral accords with individual governments, repay \$500 million in arrears from the 1981 rescheduling agreement, and cover future debt payments.

While the Poles have enough foreign exchange to meet the initial payment on 1981 arrears, the trade surplus and other inflows of funds will probably not cover approximately \$400 million in interest payments due later this year. Not surprisingly, Poland agreed to the proffered terms only after submitting a side-letter outlining its option to reopen negotiations if payments difficulties develop by the end of the year.

Several Paris Club creditors will probably provide some new money in the next few months if Poland repays 1981 arrears and shows progress in rescheduling maturities due in 1985.

--The FRG, the UK, Switzerland, and France recently pledged around \$92 million in new money.

--Among others, Austria, Sweden, and Italy are likely to provide an additional \$50 million.

--The remaining amount of debt could be covered by trimming hard-currency imports and drawing down reserves.

New credits and the IMF. Attainment of IMF membership in early 1986 might encourage Western lenders to extend additional credits and possibly provide more generous rescheduling terms. In addition the Poles would be able to draw some \$135 million from the IMF by the end of 1986, assuming they successfully negotiate an adjustment program.

Soviet reaction. Soviet leaders, including Gorbachev, probably believe that IMF membership will help normalize Poland's financial relations with the West. Improved relations with the West would permit the Soviets to reduce further--though modestly--their aid to Poland.

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EXDIS

EO 12356: DECL: OADR
TAGS: EFIN, PL
SUBJECT: THE PARIS CLUB RESCHEDULING AND THE POLISH CAMPAIGN
FOR NEW CREDITS

1. ~~(ENTIRE TEXT)~~

2. SUMMARY: HAVING INITIALED THE PARIS CLUB AGREEMENT, THE POLISH GOVERNMENT HAS TACITLY RECOGNIZED ITS INABILITY TO FULFILL IT WITHOUT NEW CREDITS AND LAUNCHED A SERIES OF DIPLOMATIC NOTES TO CREDITORS REQUESTING ABOUT 1.7 BILLION U.S. DOLLARS IN NEW CREDITS THIS YEAR. IN THEIR GENERAL EAGERNESS TO END THE DE FACTO MORATORIUM ON POLISH DEBT SERVICING, MANY NATO CREDITORS ARE LIKELY TO JOIN THE ITALIANS AND WEST GERMANS IN OFFERING MORE OR LESS QUALIFIED PROMISES OF NEW OFFICIAL EXPORT CREDIT GUARANTEES AS A SWEETNER TO THE PARIS CLUB PACKAGE. A DIRECT APPEAL TO THE NATO ALLIES TO WITHHOLD NEW CREDITS TO PRESERVE NATO UNITY ON SANCTIONS CARRIES A HIGH RISK OF FAILURE UNLESS WE CAN OFFER SOME ALTERNATIVE WHICH PRESERVES THE PROSPECT OF GETTING POLISH REPAYMENTS STARTED. ONE POSSIBLE SOLUTION IS TO AGREE TO SOMEWHAT SMALL PARIS CLUB REPAYMENTS IN 1985 AND TELL THE POLES THAT THE QUESTIN OF NEW CREDITS WILL BE EXAMINED NEXT YEAR IN THE LIGHT OF THEIR PROGRESS IN IMPLEMENTING ECONOMIC REFORMS AND NATIONAL RECONCILIATION, BOTH OF WHICH ARE NECESSARY TO RESTORE THEIR CREDITWORTHINESS. THIS WOULD REMOVE THE POLISH ARGUMENT THAT THEY CANNOT PAY AND MIGHT PRESERVE ALLIED UNITY. END SUMMARY.

3. REACTION TO DATE. IN RESPONSE TO POLAND'S MAJOR PUSH TO ELICIT COMMITMENTS FROM PARIS CLUB GOVERNMENTS FOR NEW CREDITS LINKED TO SIGNING AND IMPLEMENTATION OF THE 1982-84 PARIS CLUB RESCHEDULING AGREEMENT, THE ONLY MAJOR PLAY TO GIVE A FORMAL RESPONSE TO DATE IS ITALY. IN AN ORAL DEMARCHE BY THE AMBASSADOR, FOLLOWED

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NATIONAL SECURITY COUNCIL
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UP BY A WRITTEN NOTE VERBALE, ITALY PLACED CONSIDERATION OF NEW CREDITS AT THE FAR END OF A CHAIN OF FINANCIAL EVENTS WHICH INCLUDED PAYING CURRENT COMMITMENTS UNDER EXISTING RESCHEDULING ARRANGEMENTS, SIGNING THE 1982-84 AGREEMENT, WORKING OUT A SATISFACTORY BILATERAL IMPLEMENTING AGREEMENT AND MAKING A GOOD FAITH EFFORT ON A NEW MULTILATERAL AGREEMENT FOR 1985 MATURITIES. AS REPORTED REFTEL, DURING THE RECENT VISIT OF FRG ECONOMICS MINISTER BANGEMANN THE FRG ALSO ESTABLISHED A STRING OF PRECONDITIONS, ALTHOUGH A FAIRLY EARLY EXTENSION OF DM 100 MILLION IN HERMES GUARANTEES ON 3-6 MONTH LOANS FOR COMMODITY TRADE FACILITATION IS A DISTINCT POSSIBILITY. OTHER PARIS CLUB MEMBERS' EMBASSIES INDICATE THAT THEIR GOVERNMENTS APPARENTLY HAVE HAD LOWER LEVEL CONTACTS ON PARIS CLUB AGREEMENT IMPLEMENTATION, BUT HAVE BEEN SIMILARLY UNFORTHCOMING ON CREDITS.

4. COMMON ELEMENTS. MOST PARIS CLUB MEMBERS ARE JUSTIFIABLY SKEPTICAL OF POLAND'S CREDITWORTHINESS, AND RELUCTANT TO MAKE PREMATURE COMMITMENTS TO THE GOP; BUT THEY ALSO RECOGNIZE THAT THE DEPRESSING STATE OF POLAND'S ECONOMY OFFERS LITTLE PROSPECT FOR REPAYMENT OF THE COUNTRY'S HUGE DEBT WITHOUT SOME DEGREE OF PRIMING OF THE POLISH EXPORT SECTOR'S PUMP. THIS EMERGED WITH PARTICULAR CLARITY FROM THE GERMAN TALKS HERE IN WHICH THE GERMAN SIDE MADE CLEAR THAT ANY GUARANTEES WOULD BE CLOSELY LINKED TO SALES OF INPUTS OFFERING THE HIGHEST AND MOST IMMEDIATE RETURN IN HARD CURRENCY EXPORTS. TO OUR KNOWLEDGE, HOWEVER, NO COUNTRY HAS MADE EVEN A GESTURE IN THE DIRECTION OF WITHHOLDING CREDITS FOR REASONS OF A COMMON POSITION ON WESTERN SANCTIONS, ALTHOUGH THE SUBJECT OF A HARMONIZED POSITION HAS COME UP IN NATO AMBASSADORS' MEETINGS AND THE GERMANS HAVE FORMALLY TOLD THE POLES THAT 100 MILLION DM IN HERMES GUARANTEES CAN BE EXTENDED AS SOON AS POLAND PUTS ITS FINANCIAL HOUSE IN ORDER.

HAVING MADE THIS OFFER, THE GERMANS WILL RESIST PRESSURE FROM US TO RESCIND IT.
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5. INDIA: SIKH TERRORISTS ARRESTED IN THE PUNJAB

Police arrested groups of alleged Sikh terrorists in two Punjabi towns June 13 and 14, according to Indian press reports. The Sikhs, who are believed responsible for past terrorist acts, reportedly were planning a series of attacks on political figures and policemen.

INR Comment: Although last week's demonstrations in the Punjab to commemorate the anniversary of the storming of the Golden Temple passed without major incident, the arrests show that further acts of Sikh terrorism in the Punjab are likely. (CONFIDENTIAL)

6. MOROCCO/WESTERN SAHARA: POLISARIO MAINTAINS PRESSURE ON BERM

Polisario units fired on positions along the Moroccan berm across the Algerian border south of the Moroccan city of Zaag for ten hours June 13, according to special intelligence. Moroccan units reported they could not respond effectively due to the extended front (about 80 miles) covered by their available artillery assets, and asked for reinforcement with additional artillery and ammunition.

INR Comment: We have no indication the Polisario penetrated the berm. Ongoing berm extension operations far to the south have denuded the Zaag area of troops and equipment, whereas the Polisario guerrillas are close to their main bases in Algeria. Lack of ammunition is a chronic Moroccan problem, due to budgetary constraints. (TOP SECRET UMBRA/NOFORN)

7. POLAND: INCHING TOWARD RESCHEDULING OFFICIAL DEBT

Foreign Minister Olszowski announced June 13 that Poland is likely to sign in late June the already-initialed agreement on rescheduling 1982-84 official debt, according to press reports. He optimistically linked the signing with obtaining new money from Paris Club members.

INR Comment: Despite the generous terms of the rescheduling agreement, Poland still faces at least a \$400 million financing gap this year. The Poles have delayed signing the agreement, but may now believe that more foot-dragging will not aid their IMF membership application or gain them new credits. (CONFIDENTIAL)

8. CHINA: MILITARY LEADERSHIP CHANGES STRENGTHEN DENG, HU YAOBANG

According to a Hong Kong newspaper, the central military commission has reduced China's military regions from eleven to seven, replacing four commanders and retaining three. Politburo member Li Desheng, in charge of the strategic northeast region for more than a decade, was replaced. Beijing region commander Qin Jiwei, a Politburo alternate, was retained.

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BY RW NARA DATE 11/29/17

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3. POLAND: ANOTHER PAYMENTS CRUNCH IN 1986

Poland will meet with its official creditors (Paris Club) on January 23-24 to discuss conditionality targets for the rescheduling of 1986 obligations. Rescheduling of previously rescheduled debt as well as original obligations will be necessary to close Poland's large financial gap--about \$3.8 billion. Official lenders are pressing for comparable treatment with commercial banks--which have already rescheduled maturities through 1987--but face fresh Polish calls for new money.

* * *

Poland's hard-currency debt obligations may total \$5.9 billion in 1986, [redacted] leaving a \$3.8 billion gap. The gap could grow if terms of trade or domestic conditions worsen.

3.3(b)(1)

Official creditors plan not to discuss terms of the 1986 rescheduling until the Poles consult with the commercial banks on an appropriate division of debt relief between the banks and governments. The banks received prompt payments through 1985, while official creditors agreed to defer for three months a \$510 million payment due on December 31.

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In addition, the Paris Club will probably seek a burden-sharing formula which divides Poland's limited debt-service payments with non-Paris Club official creditors--including the USSR, Hungary, Libya, and Iran.

3.3(b)(1)

IMF membership. Poland should rejoin the IMF and World Bank in late March or April. Poland's quota--i.e., its ability to draw on Fund resources--apparently will be less than the Poles had hoped but will still be sizable. Even so, membership in the Fund and the World Bank is not likely to raise significantly Western confidence in the Polish economy.

Economic reform. Perhaps of greatest concern to Western lenders is whether the Jaruzelski government is willing and able to implement a serious market-oriented reform--especially given the continuing tension between the regime and important elements of society. Even if an IMF agreement is struck and performance criteria are met by 1987, the magnitude of Poland's economic problems ensures a lengthy period of IMF supervision and Western skepticism about sustained economic growth.

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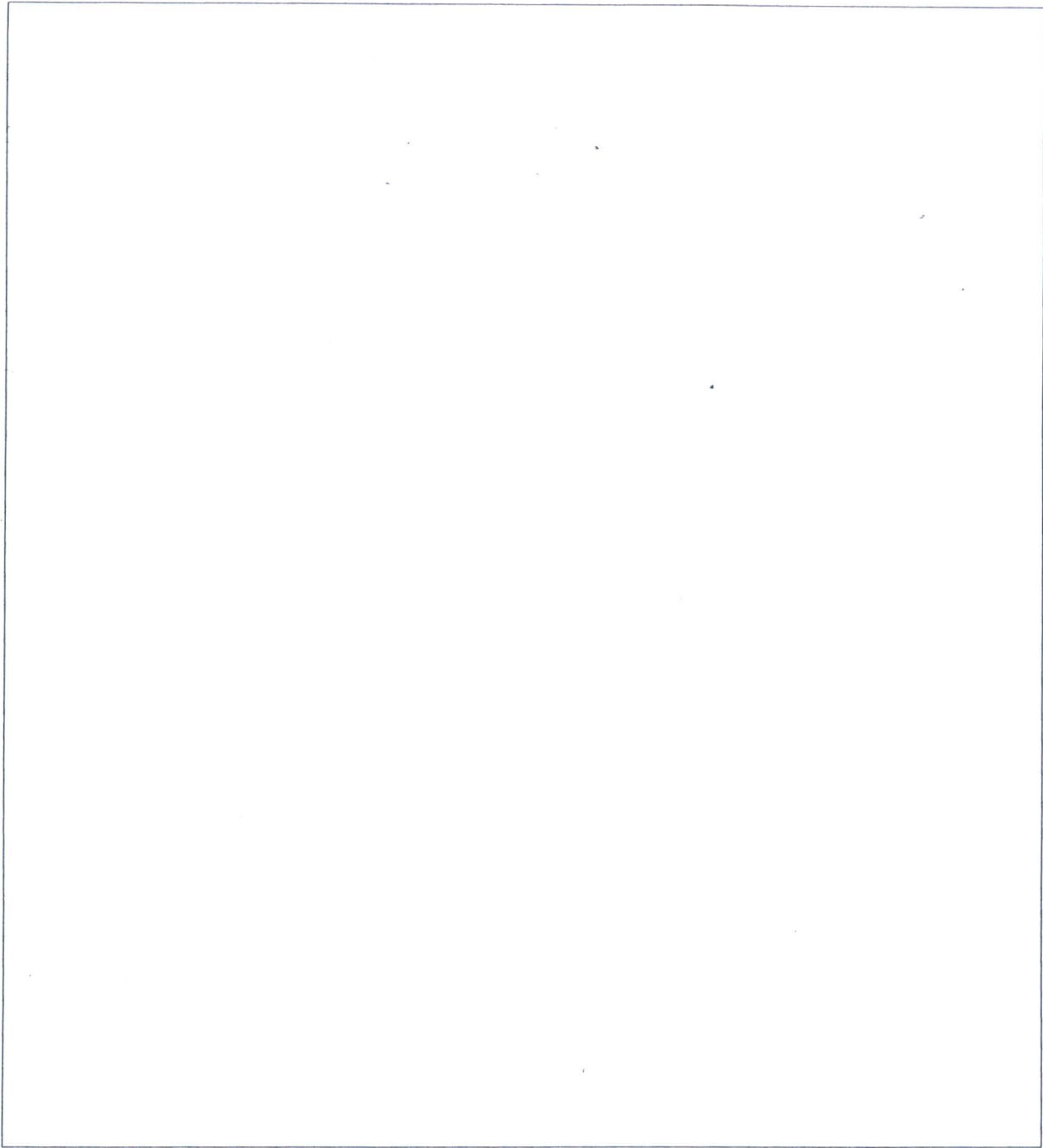
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3. POLAND: OBTAINING NEW DEBT RELIEF?

Poland will meet with its official creditors (Paris Club) on October 23 to discuss mounting arrears on official debt. Poland's inability to service its debt leaves the Club little choice but to revise earlier rescheduling agreements. But Western banks and other lenders may delay providing their fair share of new debt relief until Poland negotiates a stand-by program with the IMF.

* * *

Hard-currency debt obligations falling due in 1986 total \$2.8 billion, according to Polish data (see table). At best, a projected trade surplus and other flows of funds may cover \$2 billion, leaving an \$800-million gap. The Poles hope to reschedule \$600 million and cover the remaining \$200 million by drawing down short-term credits.

The Paris Club strategy. In July, Western governments had rejected Poland's request to reopen the 1986 agreement initialed in March and to defer \$600 million in debt payments. Instead, they advised Poland to seek debt relief, comparable to that already provided by the Club, from commercial banks and from the USSR and other bloc creditors.

On September 9, the banks signed an agreement worked out in June to reschedule \$1.7 billion--about 95 percent of principal due in 1986-87. Unlike Western governments, however, the banks refused to reschedule interest payments. Poland apparently has not sought any additional debt relief from the USSR or other CEMA lenders, which continue to press Poland to reduce its 5.6-billion-ruble trade deficit (some \$6.7 billion).

Paris Club reversing itself? Poland's failure to spread the burden of additional debt relief evenhandedly among non-Club lenders has recently induced some Club members to support reopening previous reschedulings. In particular, the FRG wants to regularize the Polish payments situation in order to grant some modest new trade credits. Other members see little choice but to revise past agreements in light of Poland's poor trade results so far this year.

The IMF role. The banks and other lenders may continue to reject Polish appeals for additional debt relief until the regime negotiates a stand-by program with the IMF. The IMF board had its first Article IV review of Poland on October 16. The Poles are now expected to approach the Fund to begin discussions on a stand-by.

Negotiations are likely to last well into 1987, with the Fund providing only a small part of the \$1 billion Poland wants from it during the year.

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POLISH HARD-CURRENCY DEBT OBLIGATIONS IN 1986
(in millions of US dollars)

<u>CREDITOR</u>	<u>AMOUNT DUE</u>		Total
	Capital	Interest	
<u>Governments</u>			
--1981 Rescheduling	469	179	648
--1982-84 Rescheduling ¹	528	38	566
--1985 Rescheduling		217	217
--Subtotal	<u>997</u>	<u>434</u>	<u>1,431</u>
<u>Commercial Banks</u>			
--1986-87 Rescheduling ²	<u>71</u>	<u>592</u>	<u>663</u>
<u>Others</u>			
--Socialist and CEMA banks ³	120	213	333
--Other creditors ⁴	293	108	401
--Subtotal	<u>413</u>	<u>321</u>	<u>734</u>
TOTAL	<u>1,481</u>	<u>1,347</u>	<u>2,828</u>

1. According to the agreed minute initialed on March 8, 1986.

2. According to the Memorandum of Understanding signed on September 9, 1986.

3. Socialist banks include primarily Soviet and Hungarian banks and Polish banks abroad. CEMA banks include the International Bank for Economic Cooperation and the International Investment Bank.

4. Including primarily the Libyan and Iranian central banks and short-term commercial credits.

Based on official Polish reference materials.

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Central Intelligence Agency

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POLAND

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Washington, D.C. 20505

DIRECTORATE OF INTELLIGENCE

16 October 1986

Poland: Limited Options in the Debt Dilemma

Summary

Poland's recovery from its economic crisis of the early 1980s has stalled, and prospects for sustained improvement over last year's disappointing performance appear slim for the rest of the decade. As a result, Warsaw, Western creditors, and the USSR will find no escape from the dilemma posed by Poland's economic weaknesses:

- o Failure to give the workers some say in determining their political destiny or to meet consumer demands with increased supplies will leave the Jaruzelski regime saddled with a sullen and unproductive labor force. Although the regime's use of force and intimidation may maintain a superficial calm, continued economic problems will erode the more enduring political stability that the regime is seeking.
- o Even under optimistic assumptions about Poland's hard currency trade performance, Warsaw will make little progress in meeting its financial obligations. Western creditors face more years of debt reschedulings, missed payments, and pleas for new credits from the Poles.

This memorandum was prepared by [redacted]

[redacted]
Yosinski, East European Division, Office of European Analysis and was requested by Harvey Shapiro, Deputy Director/Bureau of East-West Trade. Comments and questions are welcome and should be addressed to [redacted] Acting Chief, East European Division on [redacted]

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BY RW NARA DATE 4/11/16

o The USSR will have to continue providing substantial assistance if it wants to stave off economic decline in Poland.

Warsaw and its Western creditors may consider three options for dealing with the debt dilemma:

- o Poland's strategy is to rely on relatively fast economic growth to expand exports. We judge this to be infeasible because import requirements would grow faster than Polish projections and faster than both overall GNP and exports. The faster the overall economic growth rate, the lower the hard currency surplus.
- o Austerity, economic growth of about 1 percent per year, would yield a growing hard currency surplus as hard currency import requirements decline with constant exports. The austerity scenario could yield a \$3.5 billion surplus by 1990 under favorable conditions while the rapid growth scenario based on Warsaw's Recovery Program would yield a \$1.8 billion hard currency surplus.
- o Targeting new credits to specific export-generating projects, although a positive step, would not solve the debt problem because the number of potential projects is limited and the most marketable export products would likely have a high import content.

Warsaw is unlikely to adopt the reforms and austerity measures needed to address its debt problem as long as it perceives the the fruits of economic improvements will go only to foreign creditors -- whether in the West or the USSR -- and bypass both the Polish government and people. The Poles might take stronger actions to boost hard currency surpluses if a payments plan allowed Warsaw to keep some portion of the increased surplus. A simple payments plan that would serve both Warsaw's and the creditors' interests would include a rising annual base payment and a fixed share of any net hard currency earnings above the base payment. Creditors would receive some increase in cash flow without depriving the Poles of an incentive to improve trade performance. []

Scope Note

The analysis in this typescript is based on an econometric model [redacted]

[redacted] POLGNP determines the resource costs and, thus, the feasibility of various levels of Polish economic performance -- with special attention to the ability of the economy to reduce its dependence on imports. The model is designed to project the effects of technological adjustments and structural shifts in the economy on requirements for the factors of production -- capital, labor, energy, and imports. The model can then measure the trade-offs between domestic production, soft currency imports, and hard currency imports. [redacted]

Growing Out of the Debt Problem

Warsaw's strategy for dealing with its debt problem is to rely on relatively fast economic growth to expand exports. The blueprint for this strategy is contained in the "Program for Improving the State of Poland's Economy" that the Poles gave to Western creditor governments in 1984. The program projects annual increases in GNP of nearly 4 percent during 1986-90. It emphasizes growth in investment and exports but allows for a modest increase in per capita consumption as well. The key provisions of this program -- with growth rates scaled back -- have been incorporated into Poland's 1986-90 economic plan. [redacted]

Our analysis using the POLGNP econometric model indicates that Poland cannot grow out of its debt problems. In our view, Polish planners have underestimated popular pressures for increases in consumption, the amount of investment needed to modernize the capital stock, and the economy's need for energy and high-quality materials. The program rests on implausibly large gains in productivity of capital, labor, energy, and imports to enable the economy to boost output at the rates projected with comparatively small growth of inputs. [redacted]

Our model indicates that moderately fast economic growth would require a much higher level of imports than Warsaw projects. Whereas the Recovery Program calls for hard currency imports to grow only 4.5 percent and for soft currency imports to increase by 3.5 percent annually to achieve the growth targets for 1986-90, we estimate these requirements to increase by 7.5 and 6.5 percent, respectively. Under the Recovery Program's growth targets, our model projects that:

- o The hard currency trade surplus would increase from \$1.1 billion in 1985 to only \$1.8 billion by 1990, short of the Poles' goal of a \$2.1 to 2.7 billion surplus. This would be insufficient to cover even interest payments on Poland's debt and restore at least minimum creditworthiness with the West.
- o Poland's soft currency deficit would rise from approximately 650 million rubles in 1985 to 1.1 billion rubles by 1990. This would run counter to the goal of balanced soft currency trade by 1988 and a surplus by 1990 that was set in the Polish-Soviet trade protocol for 1986-90.

Thus, we do not believe that rapid economic growth can generate the trade surpluses needed to deal with Poland's debt problem. The Poles will not be able to meet their growth targets unless Western creditors and the Soviets temper their demands for net resource flows from Poland. [redacted]

Moderate Austerity

Our model's analysis indicates that with economic growth averaging 1 to 2 percent annually between now and 1990, the hard currency surplus could approach \$3.5 billion by 1990 -- nearly double the \$1.8 billion surplus of the faster growth scenario. * The improved trade balance results from a 6 to 7 percent annual reduction in hard currency import requirements under the austerity scenario compared to a 7.5 percent annual rate of increase with the growth scenario. This would be sufficient to halt the growth of the debt by covering interest payments but not enough for debt repayments. This seems the maximum amount of debt service payments Western creditors can hope for. From the Polish perspective, growth of 1 to 2 percent annually would prevent deterioration in the standard of living. [redacted]

Creditor efforts to extract more payments through greater austerity would slow GNP growth below 1 percent but would add progressively less to the trade surplus because savings on imports would diminish. If creditors are willing to accept less, Polish growth could rise above 1 to 2 percent. The hard currency surplus would contract rapidly, however, because import needs would rise much faster than GNP. [redacted]

The Soviets' Dilemma Under Austerity

Our research with the POLGNP model reveals a fundamental difference in the contribution of nonsocialist and socialist imports to the Polish economy. Whereas imports from the West are necessary for economic growth, imports from the Soviet Union and other socialist trading partners are essential for maintenance of the level of Polish GNP. With minimal growth in the Polish economy, imports from the West could drop 6 to 7 percent per year through import substitution. Socialist imports, on the other hand, would continue to inch up 1 to 2 percent per year. [redacted]

* This outcome rests on very favorable assumptions for Poland, including improvements in capital productivity beyond those expected given past performance, no labor unrest, no bad harvests, no problems in marketing exports, and no further deterioration in terms of trade.

Despite the goals of the 1986-90 Polish-Soviet trade protocols that call for balanced Polish-Soviet trade by 1988, the USSR probably cannot stem -- much less reverse -- the net flow of resources to Poland without risking serious damage to the Polish economy. Furthermore, slow growth could even widen Warsaw's deficit with the USSR by limiting Poland's capacity to expand soft currency exports while soft currency import needs would continue to rise. Cutting back deliveries to Poland would not benefit the USSR because it would depress Polish export capacity and could well risk economic collapse. Even if Moscow can force the Poles to redirect some exports from the West to the USSR, the Soviets probably will continue putting more into Poland than they will get back. []

Targeting Specific Export Possibilities

Some Western creditors have proposed targeting new credits to specific export-generating projects as a strategy for increasing Poland's debt repayment capacity. This approach, however, faces a number of obstacles:

- o The number of potential projects is limited, so the strategy will not solve the overall debt problem.
- o Products with the best prospects for sales in the West will themselves probably require a high level of hard currency imports in production, reducing the net hard currency earnings (see figure 1).
- o Polish estimates of new credit requirements to produce exports probably omit indirect import content. Indirect import content concerns domestically produced inputs which themselves require imported inputs for their production. For example, the meat processing industry may use domestic livestock directly yet be indirectly dependent on imports if that livestock is fed imported feed and supplements. Including indirect inputs can double the imports required to generate a given product (see figure 2).
- o Import requirements increase rapidly as rates of sector capacity utilization rise because high-cost import-dependent plants will be brought on line to meet the additional demand. Furthermore, straining the capacity of individual sectors will increase the need for new investment. Investment in plant and equipment, in turn has a very high import content (see appendix 1) Thus, efforts to generate exports will contribute the most to net hard currency earnings if the overall economy is growing very slowly.

Figure 1 Import Content of Exports Assuming Healthy Economic Growth and High Capacity Utilization Rates

(Import Content Measured in Domestic Zlotys as Percent
of Value of Exports in Domestic Zlotys)

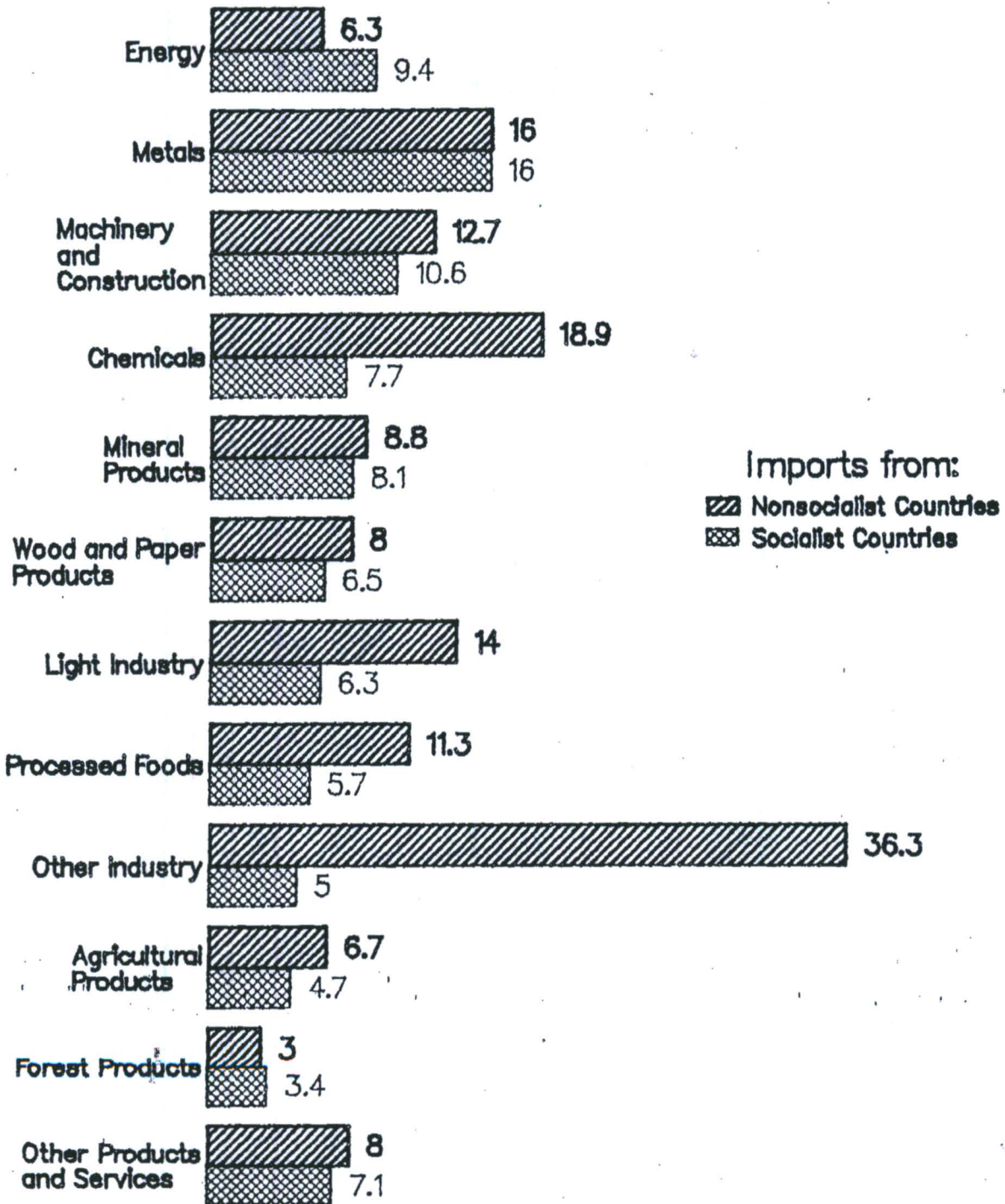
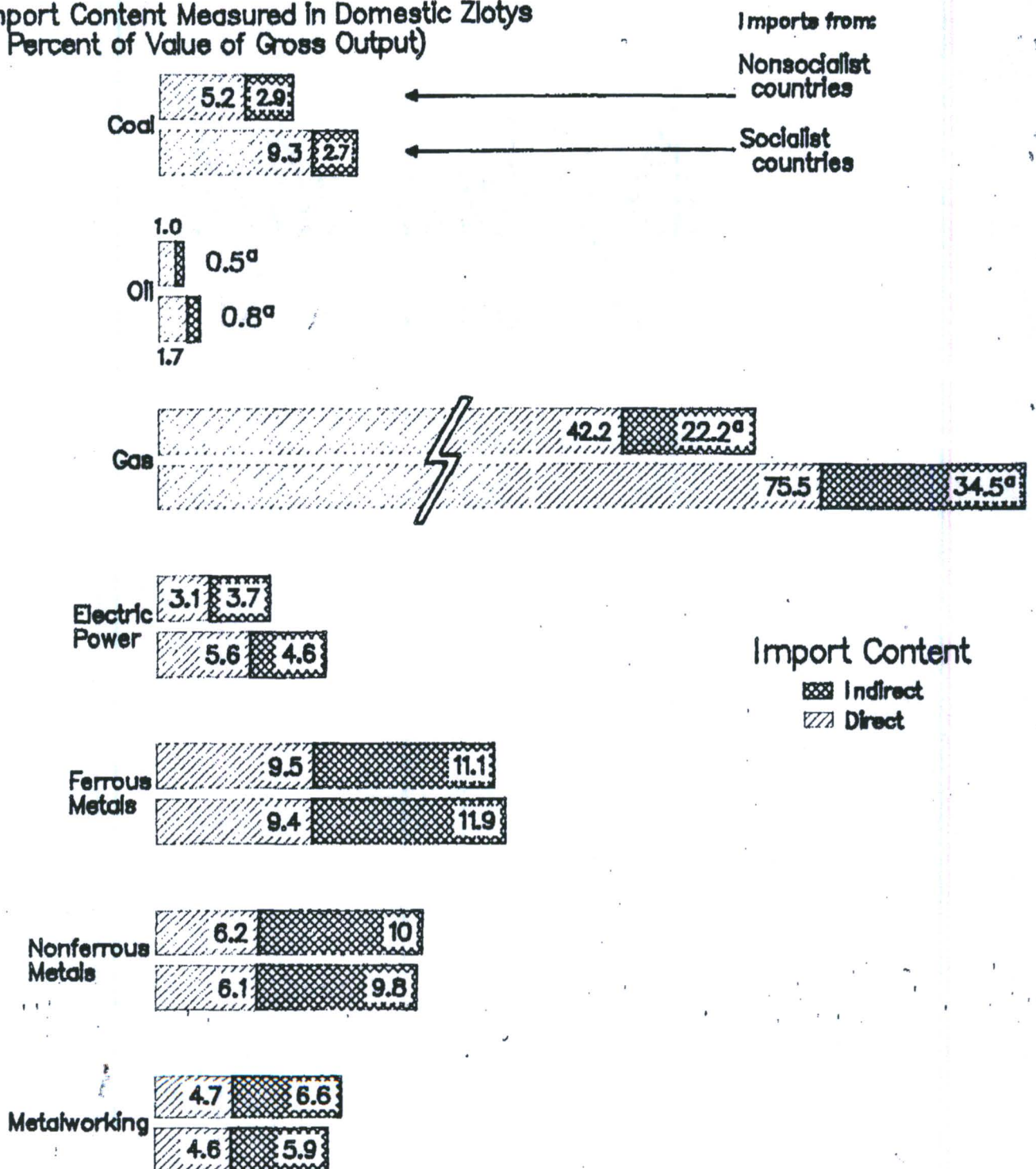


Figure 2
Import Content of Domestic Production by Sector Assuming
Healthy Economic Growth and High Capacity Utilization Rates

(Import Content Measured in Domestic Zlotys
as Percent of Value of Gross Output)



^aPoland's tiny oil and gas production industry is very import-dependent. For these calculations the joint exploration, drilling, and production costs were attributed to oil and gas in proportion to the production of each. Since the wells have yielded mostly gas, gas bears most of the import costs in our calculations.

Figure 2

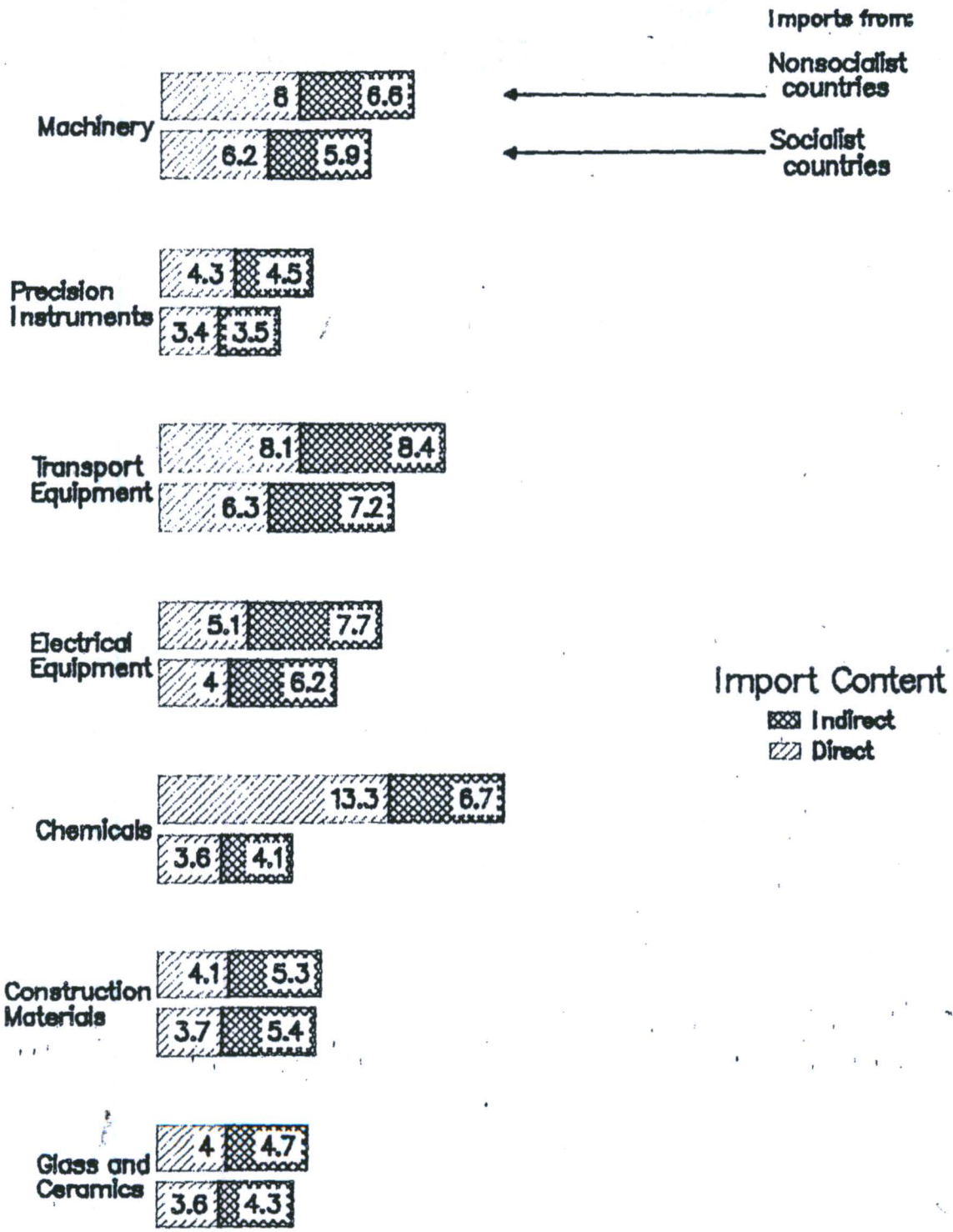


Figure 2

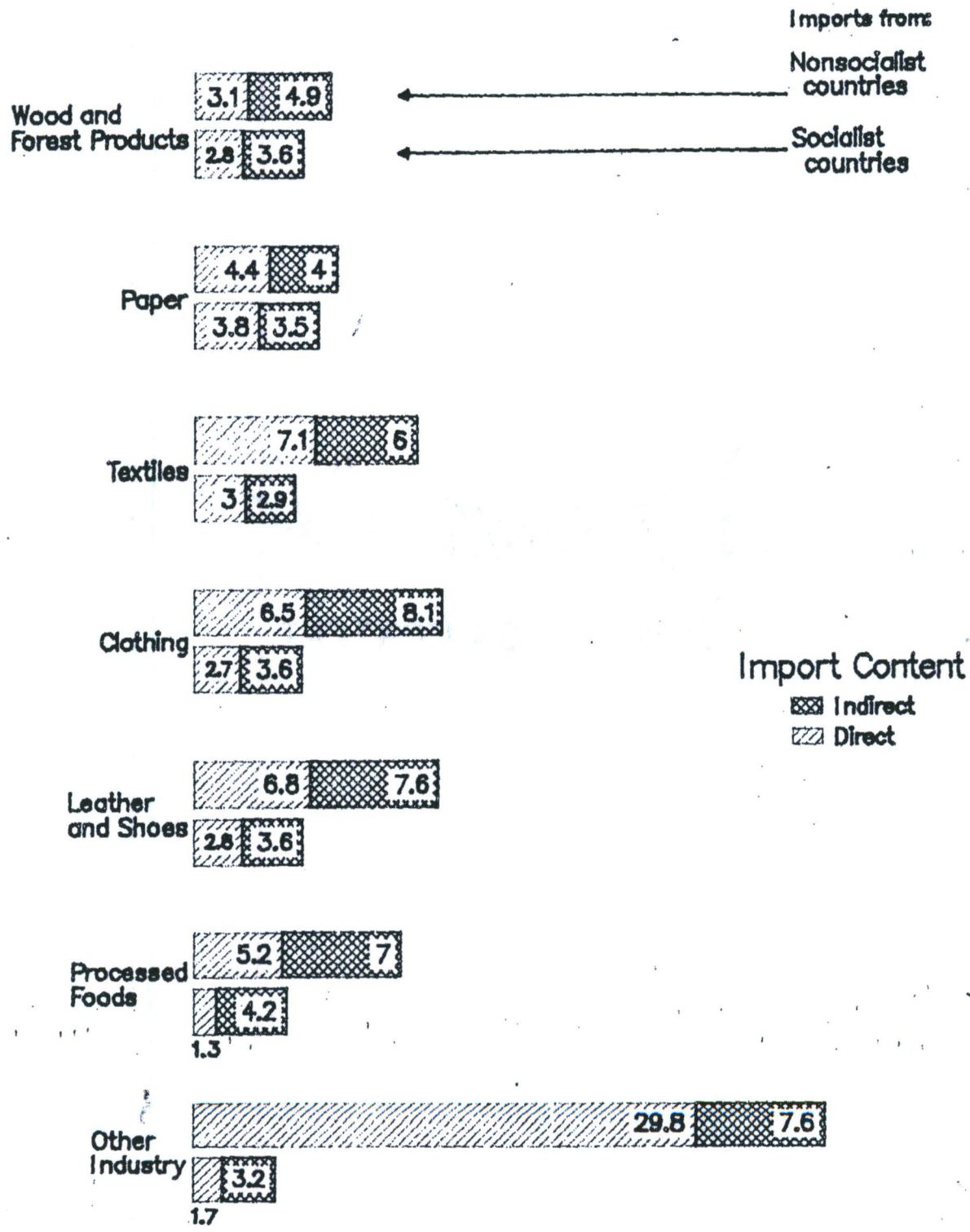


Figure 2

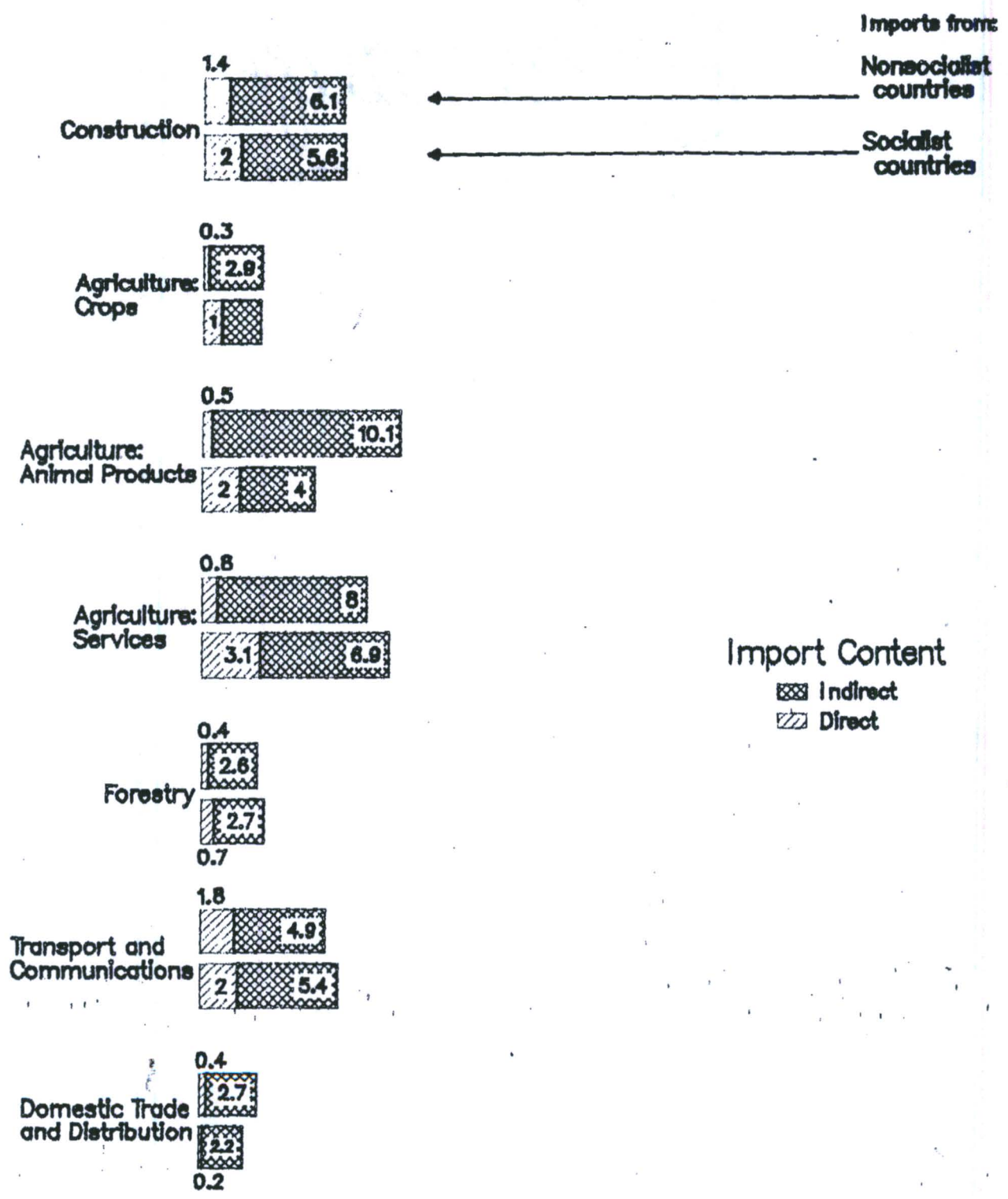
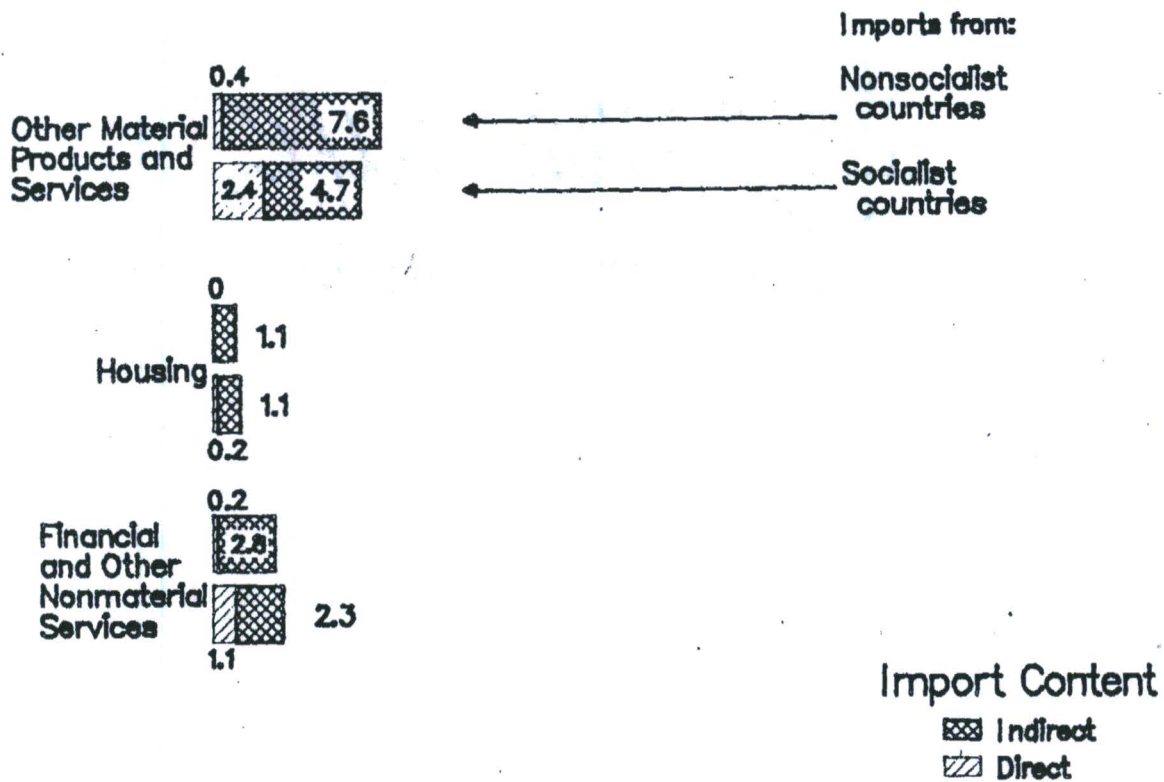


Figure 2



- o Exports with high hard currency import content are chemicals, metals, machinery, light industry, and processed foods. Yet machinery and processed foods, especially meat, are slated by the Poles for increased export over the next several years.
- o Import content also varies substantially within each category. For example, within processed foods, grain alcohol, wine, beer, and tobacco have very low import content. Sugar, fish, meat, and dairy products, on the other hand, have a very high import content. The high import content of "other industry" originates in processed animal fodder, feed, and supplements which require substantial imports. [redacted]

Extraction of Debt Payments from the Poles

After the 1983-84 recovery of economic growth, Polish net hard currency earnings -- and hence debt servicing -- have been disappointing although still positive. The much touted reforms have done little to improve efficiency or reduce dependence on hard currency imports. Warsaw's apparent strategy is to delay facing the debt problem as long as possible, minimize current payments, and delay payment of arrearages until creditors have little choice but to grant new reschedulings (see appendix 2) The Poles may hope that new credits will eventually be made available or solution of other debtor countries' problems will provide a palatable precedent for solution of the Polish problem. [redacted]

Warsaw is unlikely to adopt the reforms and austerity measures needed to address its debt problem as long as it perceives that the fruits of economic improvements will go only to foreign creditors -- whether in the West or the USSR -- and bypass both the Polish government and people. The Poles, however, might take stronger actions to boost hard currency earnings if creditors guaranteed Warsaw some portion of that increase. Such an incentive would require that terms be set according to the capacity of the economy to generate net hard currency earnings, rather than to the schedule of payments coming due. [redacted]

A payments plan that would serve both Warsaw's and the creditors' interests would include a base payment that would rise each year and a fixed share of any net hard currency earnings above that needed to cover the base payment. For example, a base payment might be set at \$1 billion in 1987, rising 10 percent every year thereafter. Warsaw would allocate to additional debt service, say, 25 percent of all net hard currency earnings

exceeding the base payment while retaining the remainder. For this approach to serve Western creditor interests, Warsaw would also have to show that additional export capacity is not being used to reduce its ruble deficit. If Western creditors did not enforce such a condition, the gains from the extra hard currency resources that Warsaw is allowed to retain would accrue at least partially to the Soviet Union rather than to the Polish economy.

[redacted]

Such an agreement could prove attractive to the Poles. First, it gives Warsaw a chance to retain at least part of any gains in net hard currency earnings. Second, it may help the Poles convince Moscow to maintain some net resource flow into Poland, since Warsaw could claim that it will retain much of that flow and not use it to support exports to repay Western creditors.

[redacted]

Warsaw will, of course, negotiate to minimize both the base payment and the share of net hard currency earnings above the base paid to creditors. Creditor negotiators can trade off the two types of obligations -- a higher base payment in return for a lower share of the net surplus in excess of the base payment or vice versa. The base payment is a fixed obligation while the share portion is a bet on Poland's ability to improve its net hard currency earnings in the future. The potential trade-offs between fixed payment and share of net earnings provide a wide range of alternatives within which agreement might be reached -- much wider than if only a fixed payment or only a fixed share were considered.

Appendix 1: Import Content of Domestic Final Uses

Figure 3 indicates the degree to which Poland can adjust its import requirements by changing the mix of personal consumption, investment, and government spending -- even without undergoing any technological adjustments. Any shift of personal consumption expenditures away from food toward other consumption dramatically reduces imports from nonsocialist countries. The maximum effect comes from a shift toward housing where management, maintenance, and repair have virtually no direct import content and only miniscule indirect import content. (1) Housing, though, is considered "unproductive" in Marxist economic systems and is usually neglected; yet, it is one area where welfare can be enhanced and work incentives increased with almost no increase in imports. []

A shift in personal consumption expenditures away from food and toward other (nonhousing) goods and services reduces the overall import content of the expenditures by nearly 16 percent. (2)

It also replaces nonsocialist imports with socialist imports. []

[]

1 Housing here refers to the consumption of housing services and the current expenses for housing. It does not refer to the value or import content of housing construction, which is included in investment.

2 See Figure 3. The first set of bars shows the import content of personal consumption expenditures on food: 36.7 percent for imports from nonsocialist countries and 24.2 percent for imports from socialist countries for a total of $36.7 + 24.2 = 60.9$ percent. The third set of bars, personal consumption expenditures on other things besides food and housing, indicates an import content of 13.9 percent for imports from nonsocialist countries and 37.5 percent for imports from socialist countries for a total import content of 51.4 percent. If 100 zlotys of personal consumption expenditures is shifted from food to other, the import content of that expenditure drops from 60.9 zlotys to 51.4 zlotys or by 9.5 zlotys. This reduction is 15.6 percent of 60.9 zlotys.

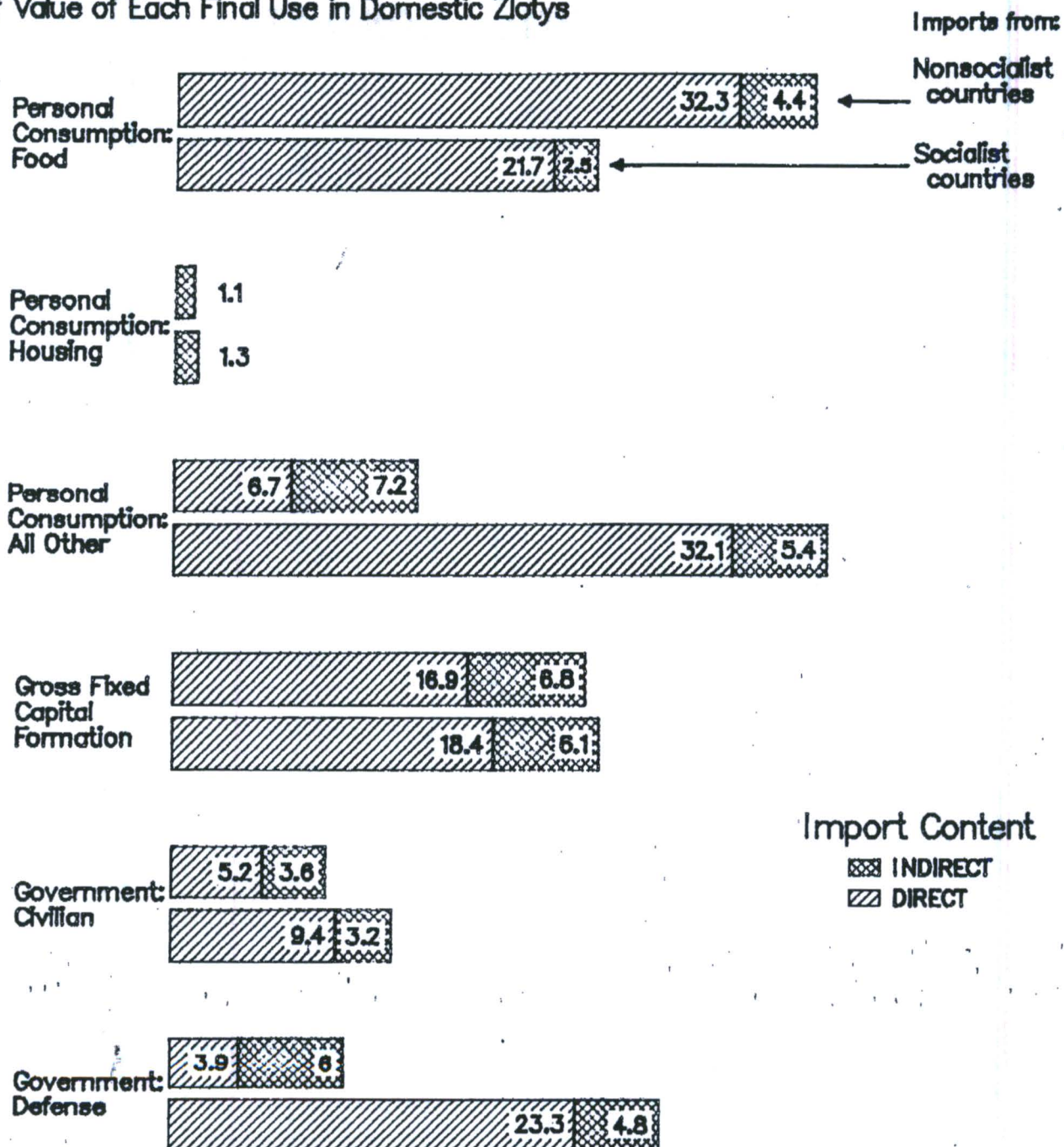
Investment in Poland is highly import dependent. With virtually no limits on imports, almost half(3) of every investment zloty would go directly or indirectly for imports almost evenly split between socialist and nonsocialist imports. Reductions in investment result in immediate and substantial reductions in imports. [redacted]

Government activities are much less import intensive than other final uses with the exception of defense spending where procurement involves substantial imports from other socialist countries. [redacted]

3 See Figure 3. The fourth set of bars indicates the import content of investment. Imports from nonsocialist countries comprise 23.7 percent of each investment zloty. Imports from socialist countries account for 24.5 percent. Adding the two numbers together yields a total investment content of $23.7 + 24.5 = 48.2$ percent or nearly half.

Figure 3
Import Content of Domestic Final Uses Assuming Healthy Economic Growth, High Capacity Utilization Rates, and No Financial Constraints on Imports

(Import Content Measured in Domestic Zlotys as Percent of Value of Each Final Use in Domestic Zlotys)



Appendix 2: Current Economic Concerns

Economic Growth GNP grew 1.6 percent in 1985, down from 3.8 percent in 1984 and 4.9 percent in 1983...Indicates that recovery from 1980-81 crisis is stalling...slower growth likely to continue in 1986...foreign trade, construction, personal income growth cited as problem areas. [redacted]

1986-90 Plan Calls for net material product to increase 3 to 3.5 percent per year through 1990, industrial production to increase 3 percent annually, agricultural production to increase 1.1 percent, consumption to increase by 2.2 to 2.9 percent...Capital spending set to increase 24 percent over 1981-85 total...Growth plans assume significant reduction of energy and raw material consumption...Stagnant coal production, rising energy demand may lead to energy shortages in the next few years...Aging capital stock will require higher investment rates and imports of investment goods than Warsaw can achieve. [redacted]

Living Standards Food supplies have improved since 1981 with only meat and chocolate still rationed...Nominal incomes continue to rise faster than 18.2 percent annual measured inflation rate...Many consumer goods still in short supply indicating hidden inflation...Thriving underground economy cannot meet growing demands...Worsening environmental problems could lead to reduced public health and slower industrial development...Environmental issues could spawn increased demonstrations. [redacted]

Economic Reform Leadership renewed calls for economic reform at Party Congress in June...Currently undertaking cadre review to oust reform opponents...Some high level personnel shifts have been made but bureaucratic and conservative resistance continues to limit reform implementation...Workers may distrust reforms as well, fearing unemployment, lower wages...Consumer austerity measures threaten to erode labor productivity, spark strikes or protests...Significant improvement of efficiency unlikely in near future. [redacted]

Trade Performance Poland unlikely to meet projected hard currency trade surplus for 1986...Hard currency surplus narrowed to \$430 million in first half of 1986 as exports declined 3 percent and imports increased 3.2 percent...Trade deficit with USSR continues to widen as imports surge by more than 10 percent...suggests Poles will be unable to balance trade with USSR by 1988. [redacted]

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Debt Policies Warsaw claims commitment to repaying debts, but not at the expense of living standards...Signed 1986-87 rescheduling agreement with commercial creditors in September...1986 government agreement initialed in March...Poles cite higher growth, higher export growth rate as only solution to worsening debt problem...Warsaw claims it cannot meet obligations under current rescheduling agreements without new credits. [redacted]

IMF Poland was readmitted to the IMF in late May 1986...membership quota is 680 million SDR...Membership may improve commercial and government creditors' assessment of Polish creditworthiness. Poles unlikely to receive IMF credits until Article IV consultations and negotiation of economic adjustment program are completed, probably sometime in mid-1987. [redacted]

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