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POLAND: Financial Outlook

Poland's financial situation since the imposition of martial law has deteriorated further and now has come down to default, continued stalemate with the banks, or delayed rescheduling. None of these outcomes will do much either to damage Warsaw's already shattered hard currency trade and financial relations or to restore its creditworthiness. Prospects remain poor for surmounting the financial hurdles that prevent imports of the raw materials, spare parts, and semimanufactured goods necessary for economic recovery. The economic outlook, therefore, is for continued stagnation and falling standards of living.

Warsaw has notified the banks that the interest due last year will be paid up by Monday, paving the way for signature by March of the agreement rescheduling Poland's obligations for 1981 to private creditors. Bankers generally are confident that the Poles will keep their promise, but \$200 million remained unpaid at the end of January. To be paid on time, interest payments will have to be made faster than they have been in the past six weeks.

Even if Warsaw fails to meet the deadline, the banks still may not call default. Creditors have held off through many months of Polish moratorium, arrearages, missed deadlines, economic slump, political turmoil, and now martial law.

The banks would prefer to keep the trickle of interest payments flowing and to avoid writing off large loans. The banks hope that Moscow will provide the money, but Polish officials claim that they expect no further Soviet help.

The likelihood that Poland will be declared in default will increase, however, if the impasse continues on rescheduling payments due in 1981, while Poland falls further behind in its payments due this year. Any of the 501 banks with which Warsaw is behind in its interest and principal payments could declare Poland in default.

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Creditor governments could take similar action on several grounds:

- In some cases, Warsaw apparently has not paid the 10 percent of principal and interest due in 1981 that was not covered by the agreement rescheduling obligations for official creditors.
- Overdue payments already are building this year on government-guaranteed credits.
- The imposition of martial law makes the regime vulnerable to a provision that allows the Western creditors to abrogate the rescheduling agreement under exceptional circumstances.

Consequences of Default

Legal default would prompt a scramble by private creditors for Poland's assets in the West, the value of which would offset only a fraction of Poland's hard currency debt. The impact on foreign trade would be limited, because it dropped substantially in 1981 and has fallen further since martial law was declared.

Although the immediate additional damage would be small, being declared in default probably would make it more difficult for Poland to reestablish its creditworthiness and delay access to new loans. The stigma of default would be difficult to overcome, and suits and claims could tie up Polish financial and commercial relations for some time.

Impasse Without Default

If the impasse continues beyond next week without a declaration of default, Warsaw would still have to place an extremely high priority on paying banks on 1981 interest rather than buying imports. With reserves depleted and export revenues reduced to a trickle, there are few funds left for imports.

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If Poland manages to pay interest and other required fees it will have cleared the immediate financial hurdle. The completion then of the rescheduling agreement would be the first major economic agreement with the West since martial law. The Poles unrealistically hope that banks would then restore short-term credit lines, allowing some expansion of trade.

Warsaw's Financial Strategy

Even with a private debt relief agreement Poland would have to tackle the massive burden of some \$10 billion in payments due in 1982. This year Warsaw owes \$5 billion in principal to Western governments and banks, and another \$1.8 billion to non-Western creditors. Interest charges are estimated at \$3.3 billion.

The Polish Government apparently has made no payments due this year, concentrating instead on meeting obligations for 1981. With no debt relief arranged, Poland is falling behind in its payments to all creditors at the rate of \$800 million per month.

The Poles are likely to request a moratorium on debt service for 1982 and then pay those creditors most likely to declare default or to extend new credits. Highest priority will be given to paying the \$2.5 billion in interest to private banks. The Poles and their private creditors also probably will urge governments to open negotiations for debt relief on guaranteed obligations due to be paid this year or at least ask official creditors not to declare default.

As long as nearly all Western government credits remain blocked by sanctions, Warsaw will not be able to repeat the tactic it employed last year, using commodity credits extended by Western governments to cover debt service. Even if Warsaw is able to join the IMF late this year, private bankers are unlikely to change their attitudes or to provide much immediate financial help. The Poles' recent announcement that they plan to accumulate a trade surplus of \$500 million for the first half of this year indicates that Warsaw is choosing to sacrifice imports to pay at least some debt service.

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