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INTERNATIONAL COMMERCIAL BANKS AND THEIR CROSS-BORDER  
LENDING TO GOVERNMENTS OF DEVELOPING COUNTRIES:  
A STUDY OF PERU, 1965-1976\*

\* The author, Mr. Robert Devlin, is a staff member of CEPAL. The views expressed here are those of the author and do not necessarily reflect those of CEPAL.

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### CORRIGENDUM

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IT IS SUGGESTED THAT THE MORE THAN CASUAL READER HEED THE FOOTNOTES OF THE STUDY SINCE MUCH QUALIFYING INFORMATION HAS BEEN PUT THERE TO AVOID BURDENING THE TEXT.

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ABBREVIATIONS

BCR	Banco Central de Reserva del Perú
BN	Banco de la Nación
CAF	Corporación Andina de Fomento
CEPAL	Economic Commission for Latin America
COFIDE	Corporación Financiera de Desarrollo
COTREX	Consejo de Transacciones Externas del Sector Público
DAC	Development Assistance Committee
DC	Developed Countries
IBRD	International Bank for Reconstruction Development (World Bank)
IDA	International Development Association
IDB	Inter-American Development Bank
IFC	International Finance Corporation
IMF	International Monetary Fund
INP	Instituto Nacional de Planificación
JUTREX	Junta de Transacciones Externas del Sector Privado
MEF	Ministerio de Economía y Finanzas
ODA	Overseas Development Assistance
OECD	Organization for Economic Cooperation and Development
USAID	United States Agency for International Development

EXPLANATORY NOTES

Three points (...) indicate that relevant data are not available or do not apply to the particular heading.

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## Chapter I

### SUMMARY AND CONCLUSIONS

#### I. SUMMARY

1. The decade of the 1970's has witnessed the emergence of private commercial banks as important actors in the external finance of developing countries. In the case of Latin America private banks have become the major source of finance, accounting for as much as two-thirds of total current account finance as recently as 1974. In the latter half of the 1960's the banks' share of total finance was only 12%.
2. Notwithstanding the important role of banks in the economic life of developing countries in general, and Latin America in particular, there is a most incredible dearth of specific information on the processes of lending by the banks and borrowing by the developing countries. Recent improvements in data collection have mostly involved very aggregate figures that tell little about how banks have lent and what their impact has been on the process of economic development; moreover, data collection and publication is more reflective of the needs of regulatory authorities in the center than the requirements of the developing countries.
3. The lack of insight into the process could be resolved if individual commercial banks made their loan portfolios more transparent. However, banks traditionally hide behind the veil of secrecy, making the detailed study of the experience of individual LDC borrowers the only reasonable alternative for breaching the gap in data and analysis.
4. This study concerning Peru represents an attempt to begin the employment of the latter strategy. The precise focus is on public sector medium and long term borrowing for the period 1965-1976. Data collection involved

aggregate loan flows from all sources and comprehensive loan-by-loan detail for all commercial bank transactions that were not related to national defense activities. Using data on commercial bank loans, profiles were created on individual commercial institutions for the purpose of analysis of their behavior. Data also were reaggregated to provide a more complete view of the nature of bank lending and its impact on the economic development of Peru.

#### Background on the borrower

5. During the period under study Peru had two governments with different economic philosophies. During 1965-1968 reigned a government which promoted industrialization and moderate social reform; however, it respected Peru's traditionally liberal economy based on the export of primary commodities and foreign investment. Thus, the government sector, while expanding rapidly with respect to its small size in the 1950's, remained basically supportive of the private sector. Introduction of a new government in late 1968 brought economic policies that showed a much more intensive nationalistic and developmental tone. The philosophy underlying the basic model was described as something that would bridge the gap between capitalism and communism. The state became the dominant entrepreneur in productive activities; foreign investment that was not compatible with national autonomy was dismissed from the country, and comprehensive socio-economic reforms were undertaken to enhance the well-being of the population.

6. Despite different orientations in economic policy, the factors behind a relatively high demand for foreign resources were similar for both governments.

- a) In both cases the public sector was expanding rapidly with respect to previous rates of growth. This was particularly true for the second government, which took control of wide segments of economic activity.

However, the domestic tax base severely lagged behind the expansion of activity, creating large deficits that for numerous reasons exceeded the capacity of domestic capital markets to finance them.

- b) There was a long term supply constraint for exports, coupled with ever growing pressures to import. The export constraint reflected a combination of laxness, bad luck and long gestation periods and/or delays on investments in the export sector. The demand for imports stemmed from rapid growth of investment (especially public) and consumption, overvalued exchange rates, dismal domestic food production and speculation.
- c) The public sector was relatively inexperienced vis-a-vis the ever-growing responsibilities placed on it. This meant that foreign contractors, imports and finance easily penetrated national investment schemes and that there was little effective discipline and/or control with regard to debt contraction. This created debt service problems which generated their own demand for foreign exchange.

7. The post-1968 government experienced several unique factors that inflated its demand for resources. One was comprehensive subsidies on basic consumer items, many of which were imported. Another was the ecological disappearance of the anchovy, a major export item. And perhaps most importantly, there were anticipated (and ultimately exaggerated) receipts from exports of newly found petroleum in the Peruvian jungle. One suspects that authorities either consciously or unconsciously mortgaged future petroleum receipts for present-day consumption and investment. Unfortunately, actual production fell far short of expectations.

8. Many of the above factors of demand for foreign finance stemmed from structural weaknesses in the economy that went unrepaired for prolonged periods.

For each government these problems culminated in economic crisis. The first government had its crisis in 1967-1968 and the second entered into open crisis in late 1975.

#### Behavior of the Suppliers of Foreign Finance

9. Despite the similarities in the factors of demand for foreign resources, the response from the supply side was rather unique for each government. The only common factor was boycotts from one or more official sources of finance.

10. The government in power in the 1960's faced varying credit freezes from U.S. AID, then a major source of concessionary finance, because of an investment dispute with a U.S. based transnational enterprise, the International Petroleum Corporation. This fact, coupled with the taxing analytical requirements of multilateral finance, caused the government to become highly dependent on private suppliers' credits. As a result its debt was already "commercialized" as early as 1965. As for commercial banks, they played a minor role, but were important at the margin due to the emergency finance that they provided to the government during 1967-1968. Banks also may have been indirectly present to the extent that they discounted and picked up promissory notes held by suppliers.

11. The government installed in late 1968 encountered a financial boycott due to its program of nationalizing foreign firms with compensation that was less than adequate in the opinion of the companies and their home governments. Important sources of bilateral finance were cut off and leverage was used to freeze aid from multilateral agencies. Peru's commercial bankers also were very reserved, lending only for purposes of refinance, and then due to threats of non-payment. Given the difficult economic environment in 1968-69 it is hard to determine whether the bankers' attitude was due to objective economic circumstances or participation in the boycott.

12. In 1972 Peru once again began to have access to foreign credit. The renewed access stemmed from several factors. First, Peru's deep resolve to overcome the boycott caused it to successfully sustain growth and reforms in the face of a hostile external environment, thereby making the punitive measures increasingly counterproductive. Second, there recently had been a discovery of oil in the Amazon, making Peru potentially an important strategic element in the oil procurement strategy of the center. Third, Peru began to diversify its external economic relations to incorporate partners with a neutral or favorable view on its economic policies. Fourth, and most importantly, structural changes in world banking in the early 1970's made commercial institutions abandon their traditionally conservative attitude on LDC finance in favor of an aggressive strategy for expansion of lending to developing countries. Peru eventually got caught up in the process, and banks were increasingly more eager to extend no-questions-asked finance to the government. A seemingly unlimited desire on the part of banks to expand their assets in LDCs, coupled with the government's inflated demand for foreign finance, created conditions where Peru accumulated enough commercial bank debt to make it one of the most important LDC clients of the banks.

13. The banks remained eager lenders to Peru up until late 1975 when a new cautious attitude was adopted. On the one hand, banks in general had become more cautious lenders due to a series of major bank failures in mid-1974 and criticism from home governments to the effect that banks had over-lent to LDCs. On the other hand, the structural weaknesses underlying Peru's demand for external finance had been intensifying, as was the burden of its debt. Moreover, anticipated receipts from petroleum had not lived up to original expectations. By 1976, bankers were very reluctantly financing Peru's balance of payments, and terms and conditions were relatively onerous. Thereafter, relations with the bankers became even more tense and ultimately creditors forced the government to take recourse to the IMF. Ensuing harsh stabilization programs generated heavy social costs for a country already characterized by severe poverty.

The Nature of Bank Lending: 1965-1970

14. In the period 1965-1970 a handful of large internationally experienced U.S. banks virtually controlled the government's access to foreign commercial bank credit. Peru's major bank at this time probably was Manufacturers Hanover, both because of the volume of credit extended and the fact that it arranged several relatively large multi-institutional loans for the first government in order to help it overcome its financial difficulties in 1967-1968. Other major lenders were Bankers Trust, Bank of America, Chase Manhattan, Citicorp and Continental Illinois. All together, there were only 27 lending banks in the period.

15. Most loans in 1965-1970 were financed out of the headquarters of the banks, both because the absolute volume of lending was small enough not to require special funding from abroad, and because loans to LDCs were uncommon enough to merit the attention of the very top executives of the banks. Reflecting the sourcing of loans, interest costs were based on a floating domestic prime rate. (Often the variability of the floating rate was assuaged by a floor and ceiling base rate.) Maturities rarely exceeded 5 years, which was the norm for international credit at this time. Flat fees on loans were rare.

16. Most commercial bank loans were formally designated for purposes of refinance. Banks refinanced suppliers which were reluctant or unable to lengthen their loan commitments and also official agencies which for political reasons were withholding credit from the government. Banks also constantly refinanced their own credit, especially in the crisis of 1967-1968 and then again under pressures of non-payment by the military government in 1969-1970.

17. Banks refinanced loans in the difficult economic period of 1967-1970, but credits were characterized by very short overall maturities (5 years), very short grace periods (sometimes less than a year), and rather onerous interest margins (1.75 or more).



18. Bank lending in the period almost always was very conditional. Commercial security arrangements such as escrow accounts were most common on transactions with decentralized government agencies. With the appearance of economic stress after 1966, refinance credits carried political-economic conditionality. When the government was under IMF scrutiny in 1967-1969, credits were tied to IMF standby accords and carried debt restrictions very similar to those applied by the IMF itself. When the government managed to avoid the IMF, as was the case in late 1969 and in 1970, banks reluctantly agreed to refinance, but also applied conditionality that was uniquely designed by them. The conditionality basically involved precise debt restrictions which gave the government little room for new debt contraction in the first half of the seventies.

The nature of commercial bank lending: 1971-1976

19. In 1971 commercial banks still were restrictive lenders to Peru. However, in the following year there began a process that involved a massive change in relations with the world banking community. Not only was there a phenomenal rise in the volume of lending, but also a tremendous diversification of sources. The total number of private creditors rose from just 27 in the sixties to 167 in the seventies. Major lenders at the institutional level were Citicorp., Wells Fargo, Manufacturers Hanover, Bank of America and Chase Manhattan, all with the exception of Wells Fargo, from the same club of major international lenders in the sixties. However, unlike the previous period when a few major lenders accounted for almost all the lending in absolute terms, in 1971-1976 they accounted for a minority of credit flows. A large mass of newcomers to international lending (of which Wells Fargo was one) that at the institutional level mostly were of intermediate or minor importance as individual lenders, as a whole accounted for the vast majority of credit extended to the government.

20. Not only were there many new institutions lending to Peru, but there was much greater dispersion in terms of the geographic origin and size of the institutions. In the sixties an overwhelming part of all commercial credit came from a handful of large internationally experienced U.S. banks. While U.S. institutions were still the dominant source of finance in the seventies, lending was shared among a very large number of banks. Moreover, important lending came from Japan and Europe as well. Most newcomers in the seventies were of varying degrees of size and often had little international lending experience.

21. The very significant dispersion in the sources of lending could suggest a greater degree of independence for the borrower. There is no doubt that there was more plurality in sources lending with respect to the 1960's. However, in the 1970's nearly 80% of all credit was extended in the form of syndicated loans, which were organized and administered by a lead bank. And just 5 lead banks—Citicorp, Wells Fargo, Manufacturers Hanover, Bank of Tokyo and Dresdner Bank—accounted for roughly three-fourths of the credit mobilized in syndication. Thus with the new mechanism for international lending—the syndicated loan—came a new form of power. While many new banks lent to Peru, a handful of institutions again had a considerable degree of control over the access to foreign credit. Moreover, the situation for Peru was merely a more severe form of a similar concentration at the level of international syndication.

22. Given the very large volume of credit to Peru, most banks had to seek offshore finance. (This was particularly true for U.S. banks which faced home country capital controls.) Thus while headquarters still remained the main source of loans, London, the Bahamas, Luxembourg and other offshore centers became important sources of funding. Another reason for sourcing loans abroad, especially with regard to tax havens like the Bahamas, was to enhance income from foreign transactions.

23. In the seventies, as in the sixties, U.S. dollars were by far the most common currency for loans. However, in the former period there was significant use of other currencies such as the yen and D-mark.

24. Reflecting the importance of offshore funding, almost all loans were based on the floating London Interbank Offer Rate. Accelerating world inflation caused the disappearance of the floor and/or ceiling base interest rate arrangements that had accompanied many floating rate loans of the sixties.

25. When Peru first gained access to considerable amounts of commercial bank loans in 1972, the terms of credit were very onerous. Margins over the libor were well in excess of 2% and maturities did not extend beyond 5 years. In contrast, established developing country borrowers like Brazil and Mexico were taking complete advantage of the bankers' eagerness to lend and were negotiating margins of something near 1.5% over libor and maturities of up to 10 years. Peru's more onerous terms reflected bankers continued uncertainty about the reform government, the economy, and perhaps to a lesser extent, the authorities' inexperience in negotiating with commercial bankers.

26. As international lending terms became increasingly more favorable for LDCs in general (a borrower's market), and as the banks became ever more interested in Peru, the terms of credit underwent massive transformation. By 1974 Peru was able to negotiate margins only slightly above one percent and maturities were up to 10 years. These conditions were only moderately less favorable than those offered to prime developing country borrowers like Brazil and Mexico.

27. In 1975, reflecting a turn to generally tight borrowing conditions (a lender's market), the terms of credit hardened for Peru about in line with most LDC borrowers. But in 1976, when bankers were openly concerned about the Peruvian economic situation, the country's average terms underwent serious

deterioration vis-a-vis other borrowers. By the end of 1976 borrowing conditions had turned full circle and reflected the onerous levels of 1972.

28. In the seventies fees and penalties became a very common part of commercial bank loans. Nearly nine-tenths of the value of lending in the period carried flat front end fees of one kind or another, at an average cost of 0.77% of the face value of the loans. Also, nearly two-thirds of the loans carried prepayment penalties, at an average cost of over 1% (flat) on the amount to be prepaid.

29. The generalized appearance of fees in the 1970's could be attributed to the emergence of syndicated loans as the major mechanism for the extension of credit. Banks were attracted to syndication because each individual institution could commit a relatively small amount of funds and thereby minimize risk. But fees often were a major inducement for lead banks to initiate syndication of a loan and also were an important inducement to participants. Reflecting the need to attract banks at the margin, syndicated credits generally had higher interest rates and fees than single bank loans and carried much higher pre-payment penalties. Notwithstanding their higher costs, syndicated credits appear to have been more favorable to the borrower than single bank loans because of both longer maturities and the much greater amount of resources that could be raised on any one transaction.

30. In the seventies, most commercial bank required the government to waive its sovereign immunity and to submit to foreign courts in the case of disputes. However, in order not to run counter to the Peruvian Constitution, which prohibits the government to submit to foreign jurisdiction, a loophole always was incorporated into contracts, allowing for possible local jurisdiction over the agreement.

31. Refinance operations continued to be the most important form of credit transaction carried out by the commercial banks. Banks refinanced their own debt, but also that of other private and official sources. This reflects a government policy of almost continued refinance of its external obligations. In 1971-1972 refinance was motivated by the burden of debt service payments. But in 1973-1974 the government refinanced basically to take advantage of the more favorable lending terms offered by the banks in this period. In 1975-1976 refinance again was motivated by debt service problems. In the latter year Peru arranged an historic 400 million refinance loan with its major private creditors. The operation was notable not only because of the size of the transaction, but also because the banks agreed to help Peru avoid an IMF stabilization program.

32. While refinance credits continued to be the major type of credit, the new style of world banking in the early 1970's was reflected in a significant diversification of lending activities. A very large percentage of the credit was of free disposition, i.e., the banks provided the funds with no strings attached whatsoever. There also was a very significant amount of project lending. And interestingly, the banks provided considerable amounts of credit to help the government compensate foreign firms that were nationalized in the reform program.

33. Most of the loans of free disposition were extended in 1973. This reflects the fact that the banks were very eager to lend to Peru at a time when major projects were still at a planning stage. Peru also was eager to establish itself as a major client. The objectives of the two parties were best achieved through the extension of credit that was not tied to any real activities.

34. Unlike the sixties, the banks' role in project lending was significant. The sectors where bank project loans were most heavily concentrated were oil development and manufacturing, in that order. Over a quarter of the resources were used for local costs. In most projects bank loans complemented other sources of finance like suppliers' credits and bilateral loans. In other words, banks were one layer in a multilayered financial package. However, significantly, commercial banks were very important in the successful financing of some projects of high national priority like the transandean oil pipeline and the Cerro Verde I copper mine.

35. The nationalization credits were extended in a form of solidarity between banks and home country investors. They were valuable to the government in as much as the loans permitted the authorities to settle prolonged disputes with foreign investors and their home governments. U.S. and Swiss banks—investors were the key actors in this type of credit. One historic credit arranged by Morgan Guaranty in 1974 was part of a package agreement with the U.S. government to end an investment dispute (and sanctions) that arose in late 1968 over the nationalization of U.S. based enterprises.

36. As for the terms of the credit, the different types of loans carried costs which were broadly similar to global averages. The clear exception to this was nationalization credits which carried relatively more favorable terms with regard to interest rate, maturities, fees and prepayment penalties. The more favorable conditions reflect the special nature of the credit as a form of bank—investor solidarity.

37. In the period 1972—1975 banks—in contrast to the 1960's—were virtually unconditional lenders to the government. The earlier heavily conditioned loans of the sixties were prepaid by new (and cheaper) unconditioned credits. Banks showed little interest in securing loans with anything more than a general government guarantee. What was financed, how it was financed, and the ultimate purpose of finance appeared to matter little to the banks.

38. The permissive environment of 1972-1975 changed radically in 1976. As noted before, banks were generally more cautious lenders because of factors external to Peru. However, the country's economic difficulties generated special concern among its private creditors and loans once again were heavily scrutinized. When Peru requested a large refinance credit from the banks in 1976 the immediate reaction was to condition any new credit by an IMF standby agreement, as had been done with developing countries in the 1960's. But the government insisted that it would not submit to the traditionally harsh IMF, and after hard negotiations, and strong reluctance on the part of some banks, commercial creditors agreed to extend refinance loans to the government. Banks joined together in a collusive fashion into national groups—U.S., Canadian, Japanese, European, etc.—, to form large syndicated credits worth nearly 400 million dollars all carrying almost identical terms and conditions.

39. In the negotiations for refinance of the debt, banks displayed an open willingness to protect the interests of TNCs. At least implicitly loans were conditioned by the requirement that the government settle investment disputes with two foreign firms. This conditionality was a radical departure from the behavior of the early seventies when banks lent to the government even in the face of prolonged disputes with many firms. On at least one other occasion after 1976 the banks attempted to condition finance by the treatment of a TNC.

40. When the banks agreed to refinance the government's commercial debt in the absence of the IMF, they did so fully aware of the fact that their credit completely dwarfed all other sources, including the IMF. Banks clearly had the leverage to influence government policy and this was exploited, as manifest in their agreement to monitor a government-designed stabilization program that was introduced by authorities as an inducement to have the banks refinance the

debt without the IMF. The banks split the loan into two tranches, with disbursement of the second one contingent upon the success of the stabilization program.

41. The agreement of the banks to extend credit without the IMF was not new; in 1969-1971 commercial banks had provided heavily conditioned finance on their own. What was new was that bankers took it upon themselves to monitor the whole economy, not just a few parameters like external debt.

42. While some large banks technically had the ability to monitor the economy, and as a group banks enjoyed considerable leverage over government policy, the foray into IMF territory failed. Criticism of their decisions was strong, basically arising from concern about having private profit-making institutions monitoring the affairs of a sovereign government. Possibilities for conflicts of interest obviously loomed large. Also, the Peruvians were unable to muster the political cohesion to make the hard economic decisions that bankers wanted so that foreign exchange could be squeezed from the economy for payment of debt.

43. With the stabilization plan failing, and criticism about their role in the economy mounting, commercial banks abandoned the country, forcing government officials to run back and forth between its private creditors and the IMF in search of a solution to their problems. The path was conflictive and the economy had to undergo severe shocks and social disruption. Not until 1979, when commercial debt was refinanced and official debt rescheduled, was some resemblance of order established. But the economy remained flat and social-political tensions were high. Commercial bankers also maintained a very cautious attitude towards new lending to the government. Moreover, the economic prospects for first half of the eighties remained clouded by (i) another bulge in debt service due to the short term nature of relief provided by creditors; (ii) a dismal world economy and (iii) the failure of the international community to develop an adequate official mechanism for transfer of resources from surplus to deficit countries.



The Differential Behavior of the Banks

44. Analysis showed that banks indeed behaved differently and are not a homogeneous group.

45. In 1965-1970 lending to the government was dominated by a few large internationally experienced U.S. banks. The posture of the banks was generally conservative as exposure was restricted and lending was conditional. However, in the early seventies there appeared many new lenders eager to expand their international portfolios. Both because of the crowded nature of markets in the industrialized markets, and the relatively lower rates of return to be found there, these banks focused on developing countries as a way of satisfying their ambitions for earnings growth. Their behavior displayed an aggressive character with regard to amounts extended, the terms offered, types of loans and conditions. Peru's traditional creditors of the sixties maintained a more conservative posture in this environment. Some, interested in maintaining their market position, followed the trends generated by the newcomers, while other traditional lenders assumed a more rigid posture and resisted them.

46. The aggressive lenders of the early seventies were characterized by a willingness to extend large amounts of unprotected credit without conditions. They also were likely to be more willing to extend loans of free disposition and refinance than their more conservative counterparts. These institutions also were inclined to finance activities in non-commercial areas such as social infrastructure. And up until 1975 the aggressive lenders continuously undercut the prevailing market terms for loans to Peru, thereby helping to steadily reduce interest margins and lengthen maturities.

47. By 1975 the world's commercial banking community had turned relatively conservative in its posture vis-a-vis the third world. Most of the aggressive lenders of the early seventies retrenched and/or became conservative due to fear about the stability of international finance and the massive debt accumulation

of LDC borrowers. Market trends once again came under the influence of the big international money center banks which had controlled credit flows in the sixties. Nevertheless, within the confines of a generally more conservative lending environment, some international banks behaved in ways which were more flexible than other institutions.

48. An attempt was made to classify banks according to their behavior with regard to Peru. This could be done only in a limited and tentative way due to the fact that few banks individually undertook extensive lending to the government. Moreover, some banks showed clear markings of aggressive behavior, while others were definitely conservative in their actions; but still other banks acted in ways which sometimes were conservative or aggressive, depending upon the time and circumstances.

49. From the standpoint of national origin, generally aggressive behavior was found in Japanese banks, U.S. (regional) banks, Italian banks and consortia. Meanwhile, generally conservative behavior was found in British, Swiss and French banks. German institutions also on balance might be considered to have been conservative. Other national groups showed more mixed behavior, being conservative or aggressive depending on the particular focus of action.

50. When banks are viewed from the standpoint of size, generally there were no clear-cut behavioral patterns. It is interesting to note though that aggressive behavior often was seen in the smallest banks. This can be explained in part by the fact that consortia fell into this latter category.

51. Moving to the level of individual institutions, one of the most aggressive lenders was Wells Fargo, which came from nowhere to become a major creditor of the government. Dresdner Bank, American Express International, Bank of Tokyo, Banca Commerciale Italiana, Bancal Tristate Corp. and Crocker National Bank were among the institutions that displayed a generally aggressive behavior. Openly conservative positions were seen in Chemical Bank, Bankers Trust, Morgan Guaranty,

Continental Illinois, Charter New York Corp. First Chicago, First National Bank of Boston and the National Detroit Corp. Some European banks like Schroders, National and Commercial Banking, Credit Lyonnais, Banque Francais du Commerce Exterieur, Banque de l'Indochine et de Suez, Amro Bank, Algemene Bank Nederland, Banque Worms, to mention just some, also showed generally conservative behavior towards Peru. Other banks like Citicorp, Bank of America, Lloyds Bank, Chase Manhattan, Manufacturers Hanover, and Bank of Nova Scotia showed behavior with varying degrees of aggressiveness and conservativeness depending upon the circumstances.

52. With regard to the relative commitments of the banks (authorizations as a percent of total assets), it was found that Peru generally was a very minor element in the overall portfolio of the banks. However, within this context, in the 1970's consortium banks assumed by far the highest relative commitments. Among regular banks, Wells Fargo, followed by American Express International and Bancal Tristate Corp., carried the highest relative commitments in Peru. In general, Peru's major lenders of the sixties showed very similar relative commitments throughout the 12 years. Exceptions were Bankers Trust, Continental Illinois, and to a lesser extent Manufacturers Hanover, which experienced notable retrenchment of their relative commitments in the period 1971-1976. Intermediate lenders of the 1960's such as First National Bank of Boston, Charter New York Corporation, and National Detroit Corporation also underwent a possible withdrawal of commitments to Peru in the seventies.

53. Some banks which had maintained or increased their relative commitments in the seventies, nevertheless can still be classified as having had a restrictive attitude on exposure in Peru. Morgan Guaranty appeared cautious and kept a low profile until it decided in 1974 to take the symbolic role of heading the large syndicated credit to the government that was part of a settlement of an investment

dispute with the U.S. Chemical Bank had an openly restrictive attitude on the government and did not really initiate lending to the public sector until it participated in the above mentioned syndicate with Morgan Guaranty. First Chicago also appears to have held back its exposure in Peru, entering the market only after the settlement of investment disputes with the U.S.

54. Empirical tests for the period 1972-1976 showed that as a rule banks discriminated risk through loan volume and not through the price of credit. While relative loan commitments among institutions showed great variation over time there was practically no significant divergence by individual banks (and groups of banks) from the general market's interest margins and maturities for Peru. Thus over time individual banks generally could not resist market trends nor reflect differential risk considerations in prices.

55. Some limited exceptions were found to paragraph 54. Empirical tests gave reason to suspect that commercial institutions whose size ranked them in the range of 47-91 on a world scale (1975) consistently pursued a pricing policy on the high side of the market terms. Bankers Trust appears to have had a deliberately cautious policy and provided maturities that were significantly shorter than the market average, while Dai-Ichi Kangyo Bank appeared to extend significantly longer than average maturities. In addition, a miscellaneous category of banks that incorporated institutions from countries generally outside the mainstream of international finance also showed a tendency to offer maturities significantly longer than the market average. Lastly, the Banque Commerciale pour l'Europe du Nord consistently charged significantly higher than average margins on its loans; however, this may have been offset by significantly longer than average maturities.

56. While few banks were able to diverge significantly from general market forces over time, some institutions clearly created inflection points in trends. The key bank in this regard was Wells Fargo. In 1972-1974 it repeatedly headed syndicates—heavily supported by Japanese institutions—that undercut

prevailing market trends. This was quickly copied by other banks, thereby markedly lowering the average cost of Peru's credit. To a lesser extent Dresdner Bank played a similar role. Banks which often supported the new trends were Bank of Tokyo and Crocker National Bank.

57. As part of traditional risk consideration commercial banks have preferred to finance income generating projects and have been less enthusiastic about refinance, balance of payments support and loans of free disposition. Sectoral preference has been for income generating primary activities. However, in the seventies most aggressive lenders abandoned this tradition and revealed little preference for sectors or types of loans. Big experienced international money center banks also showed little preference in this regard.

58. When banks were aggregated into country groups revealed preferences were discerned. The traditionally conservative preferences with regard to sectors and types of loans were found in British, German and Swiss banks, and to a lesser extent in French and Canadian institutions. The more bold non-traditional behavior was found in Japanese, Italian and American banks, as well as consortia. A miscellaneous group of banks from countries generally outside the mainstream of international finance also acted outside traditional behavior.

59. There was not a clear-cut functional relationship between revealed preferences for sectors/types of loans and the size of the banking institutions. However, it is interesting to note that many intermediate sized banks showed revealed preferences for traditional behavior, while small banks did not.

60. Banks most inclined to protect their loans with guarantees of home country export credit agencies were French and British institutions. The group of banks from countries outside the mainstream of international finance also had a high proportion of its lending to Peru covered by guarantees. Banks which appeared to lend to Peru with little or no guarantees from home country governments were the U.S., Japanese, German, Italian, Canadian and Swiss institutions. At the level of individual institution, some of the banks with a high proclivity

to protect their loans with home country guarantees were National and Commercial Banking Group, Credit Lyonnais, Banque Francais du Commerce Exterieur, Banque de l'Indochine et de Suez, Amro Bank Algemene Bank Nederland, Banque Worms, and Banco do Brasil.

61. When banks were grouped according to size, there was some evidence that the frequency of use of home country guarantees increased as the size of the bank decreased.

66. As for the behavior of lead banks in syndicated credits, it was found that the aggressive newcomers—e.g. Wells Fargo—employed strategies that were different from the big internationally established money center banks. First, the former gained mandates for syndication through offers to undercut prevailing market terms. Second, it established working relationships with a wide variety of newcomers that were willing to price cut as well. Working relationships reflected themselves in relatively large clusters of banks that repeatedly participated in syndicates led by the newcomer. Internationally established banks like Citicorp took less recourse to price cutting and had only a reduced number of working relationships, which often involved other big internationally established banks.

63. There was some evidence that banks with operations in Peru via branches or subsidiaries occasionally altered the pattern of their foreign currency lending to the government out of concern for protecting local business interests. However, there were no conclusive patterns established in this regard, making one suspect that most protective lending was done by the local operation itself and in local currency.

64. With the restrictive environment in international markets after 1974 and open economic crisis in Peru in the post-1975 period, the government encountered a generally reserved banking community. However, some banks took more flexible positions in negotiations than others. Many aggressive newcomers

of the early 70's with significant exposure in Peru—e.g. Crocker National and Bancal Tristate—simply retrenched and even did not participate in general refinance accords arranged by the banks in 1976. Other banks maintained their interface with the government, but took the position of hardline adversaries with regard to the authorities efforts to avoid the IMF and assuage the social costs of adjustment. Among the banks in this second group would fall Morgan Guaranty, Bankers Trust, and Continental Illinois. Chase Manhattan also would fall there, especially because it continuously conditioned its cooperation by how well authorities treated the Southern Peru Copper Corp. Another group of banks took a softer and relatively more flexible position (within a commercial context) in negotiations with the government. Dresdner Bank and Bank of Nova Scotia stand out in this regard. One could also place Credit Lyonnais, and Manufacturers Hanover in the group of "soft-line" banks. Despite a noticeable hardening of Citibank's position in 1977, it too should be considered to have had a rather flexible attitude in negotiations during the economic crisis.

65. If behavior in the post 1975 crisis were based on national origin, one would have to say that the most flexible vis-a-vis the Peruvian position were the European banks. The hard-line adversaries were mostly U.S. institutions, which incidently, were easily the most exposed in Peru. The Japanese did not appear to take a strong position, but rather followed bargaining trends which were usually dominated by the U.S. banks.

IMPACT OF COMMERCIAL BANK LENDING ON THE ECONOMIC DEVELOPMENT OF PERU

Positive aspects

66. In the period 1965-1968 banks were not a major source of finance for the government. However, at the margin they provided important resources that bridged the gap in fiscal and foreign exchange resources during 1966-1968.

67. Beginning in 1972 the banks provided much external savings and played a crucial role in the development of Peru, both in absolute and relative terms.

68. The entrance of new commercial lenders that year provided Peru with a way of breaking the grip of the financial boycott instituted by hegemonic powers in the center and which maybe enjoyed the support of Peru's traditional commercial lenders, who in 1969-1971 extended loans in a very restricted fashion, i.e. only for refinance and then on very onerous terms and with conditionality restricting future debt contraction.

69. From 1972, not only did the volume of bank credit increase dramatically, but competition for Peru's business created an environment where lending was totally unconditional and no questions were asked about the use of credit. Even in the more restricted environment of the post 1974 period, banks displayed flexibility by agreeing in 1976 to Peru's request for refinance of its debt without the interference of an IMF standby agreement.

70. With virtual stagnation in export growth in the seventies, commercial bank loans were the single key element in support of a rapidly growing capacity to import foreign goods and services in 1972-1975. This growth in import capacity was accompanied by unprecedented expansion of domestic consumption and investment, simultaneously. The cushion provided by imports permitted domestic demand to expand at margins in excess of domestic product that were large with respect to previous trends in Peru and with respect to actual trends in Latin America.



Accompanying growth in domestic demand were significant reductions in unemployment and growth in real wages.

71. Commercial banks also played a very important role in public finance in 1972-1975. Overall, in the period government deficits were very large and banks were a major source of finance. More specifically, by continuously refinancing the government's external debt, resources were freed for investment and consumption. A large mass of free disposition credits enabled the government to build up reserves or employ as it wished. And while banks were not overwhelmingly involved in project finance, they supported ventures of high national priority which were not easily financed such as the transandean oil pipeline and the Cerro Verde copper mine. Moreover, banks regularly covered local costs of projects. Considerable finance also was extended to cover compensation for nationalized foreign firms, thereby helping to diffuse investment disputes.

#### The negative aspects

72. When taken from another angle, many aspects of the banks' involvement in the economy can be viewed as being less fortunate.

73. One of the major preoccupations about bank involvement in the Peruvian economy is that their finance may have lulled public authorities into a false sense of security. In 1969-1971, the government used deep resolve and discipline to overcome a full scale external economic boycott; despite a hostile environment authorities managed to achieve more than respectable rates of growth, reduced unemployment, increases in real wages, etc., all while radically reforming relations with foreign and domestic private capital. (Catchup from the 1967-68 crisis was only a small element in this performance.) However, beginning in 1972—which corresponds to the period when banks entered the

economy en masse—the economic discipline of regime began to unravel. With a carte blanche from commercial lenders Peru found it could import without concern for exports; invest without concern for import content or an adequate mix of gestation periods; consume without concern for local production; and spend without concern for local tax effort. In this permissive environment, the economy's dependence on external finance and banks became paramount. A program originally designed to eliminate dependence on foreign capital instead evolved in such a way as to trade foreign firms for foreign banks. The new type of interface with foreign capital was complicated and the economy clearly became as vulnerable as ever to outside influences.

74. Had the banks continued to display unlimited willingness to bankroll Peru's economy in a standoffish manner the vulnerability would be a non-issue. However, there was a general retrenchment in world banking in 1975; as bankers became more reticent to finance and as the terms of loans became more onerous, the veil of finance became more transparent, showing behind it a very structurally weak economy. In 1976 the bankers panicked and attempted to force Peru into an IMF stabilization program. But, then, seeing Peru's resistance and recognizing their own leverage, the banks experimented with explicit balance of payments support on their own. Moreover, no longer were they standoffish in their behavior; not only were banks formally monitoring the political economy of the government, but they also began to protect the interests of their TNC clients. Thus banks once again became interventionist.

75. While commercial banks became interventionist, they also showed a low threshold for tolerating the problems associated with adjustments in developing countries. They provided Peru unquestioned finance in the seventies, notwithstanding economic policies that promoted ever more inflated reliance on foreign resources. If the banks were aware of underlying trends—as they should have been—then they too must have been awaiting the long term payouts on investments in petroleum, mining, etc., to realize themselves.

If they were not aware of trends, then their lending behavior must be deemed to have been reckless. But in either case, their tacit support of government policies in the first half of the seventies would lead one to ideally expect the banks to have borne the consequences of their decisions and have helped Peru overcome the difficulties without grave social costs. As it was, as soon as it became apparent that the momentum of past policies—which the banks unquestionably supported—could not be broken easily and that the mixture of politics and economics was not ripe for harsh adjustment, the bankers lost confidence and held back finance until Peru submitted to the tough requirements of the IMF.

76. Banks thus proved to be an ephemeral source of finance for an LDC unable to make quick and hard decisions about economic adjustments. Things, of course, might have evolved differently had Peru displayed restraint and screened the overtures of commercial lenders for credit. But even if this had been so commercial finance still would have proved inadequate from the standpoint of providing appropriate maturities for development. For the period 1971-1976, Peru's commercial maturities averaged just 7 years, suitable for only the most commercial of ventures. Social infrastructure can sometimes take up to a generation to payout and therefore needs much longer maturities than commercial banks could offer. Even in the commercial sphere 7 year maturities may be too short because many projects involve infant industries that can have payouts that are much more extended than identical activities in the industrialized countries. This is aside from prolongation of payouts due to mistakes or the unforeseen events—such as falls in export prices—that are very common to the experience of LDCs.

77. The lack of symmetry between the long run requirements of development and the short to medium term nature of commercial bank finance places clear obstacles in the way of broad-based socio-economic development. Policy makers, of course, can confront the problem in a variety of ways. But in order to illustrate the gravity of the matter for a country that is heavily indebted to commercial banks, one can

simplify and reduce policy options to basically two: (i) focus development strategies on activities with high short term private commercial rates of return and wait for social development to "trickle down" to the population or (ii) seek balanced socio-economic development today and hope that banks refinance their short maturities.

78. Option one might prove attractive to conservative financial managers, but unfortunately experience has shown that "trickle down" strategies can be perverse, acting merely as an excuse for unnecessary postponement of social reform and reasonably balanced income distribution. By the same token they have been associated with regimes that exclude large segments of society from political participation.

79. It has already been seen that banks have indeed refinanced, if not reluctantly, making option two technically feasible. However, refinance is a terribly awkward way to accommodate the long gestation period of development. A borrower becomes very vulnerable to the volatile lending terms in commercial markets. If refinance is sought in a borrower's market, such as 1972-1974, the results can be attractive with new credits carrying low margins and longer maturities. However, if refinance takes place in a lender's market, as in 1975-76, the results can be counterproductive to development. Not only might access to credit be difficult, but interest margins will be distressingly high and maturities uncommonly short. This causes bulges in debt service payments, complicates debt management and generates more requirements for refinance. In this type of environment debt service can prove to be more burdensome, making bankers concerned about the country and thereby further aggravate borrowing conditions. As government authorities become preoccupied about the bankers' view of their country's creditworthiness, economic policy can drift away from broad-based socio-economic development strategies into a more narrow approach stressing ventures with high short term private rates of return and an excessively liquid external payments sector.

80. If the need to refinance occurs under conditions of open economic duress, as in the case of Peru in 1976, the results can be disastrous to development. Banks, seeking to squeeze out foreign exchange for debt service, become interventionist. <sup>1/</sup> This can take place directly through the placement of requirements on government policy or indirectly by forcing authorities to submit to IMF scrutiny. Moreover, any relief provided by the banks is very short term in nature, with onerous terms and accompanied by considerable social costs and setbacks to the process of development.

## II. CONCLUSIONS AND RECOMMENDATIONS

There are three broad conclusions that can be drawn from analysis in the study, each of which leads to suggestions for future action.

1. Banks behave differently and therefore more institutional analysis of commercial lenders is needed

In the seventies relations between commercial banks and developing countries underwent fundamental change. But banks did not act as a homogeneous group; rather in many important ways they displayed distinct modes of behavior. In the bargaining environment it is important for developing country borrowers to be aware of these distinctions so that they can tailor their interface with commercial institutions in a way which is supportive of national development objectives. However, there is little institutional analysis available on the behavior of specific lenders, making it difficult for new borrowers to map out ex ante strategies for negotiations with individual institutions. Under present circumstances only with a long accumulation of experience can borrowers begin to differentiate the behavior of banks; however, the "learning by doing" mode can be difficult and full of unnecessary and costly pitfalls. Also, resulting evaluations of the banks can be more informal than systematic.

To overcome these problems, researchers must make a greater effort to analyse the institutional behavior of commercial lenders. 2/ As long as banks remain reticent about revealing the exact nature of their interface with LDCs, the most productive way to go about this would seem to be detailed case studies such as this one, which, in a cumulative way, would reveal ever more about the behavior of specific institutions. Indeed, an international organization such as the U.N. Centre on Transnational Corporations or the World Bank could set up a reporting system whereby developing countries would provide detailed information (ideally copies of credit agreements) on their individual transactions with commercial banks. Using this data the organization in turn could make a systematic analysis of the evolving behavior of individual banks both with regard to individual borrowers and groups of borrowers. The findings could be disseminated to governments participating in the system, providing a view on banks that is more extensive than that available to any single borrower. 3/ Such an arrangement would allow countries to effectively interchange views and experiences concerning specific lenders and permit them to adjust their negotiations with creditors accordingly. The interchange of information among borrowers about banks also would counterbalance the advantages of bankers who are constantly interchanging information about countries.

Of course, initially there may be resistance to such a system since borrowers can be very protective about data concerning their activities with commercial banks. Thus some work will have to be done to overcome this problem. The advantages of such a system will have to be demonstrated to developing countries and confidentiality on individual transactions will have to be ensured. Notwithstanding these obstacles, a dialogue with developing country governments on this matter should be undertaken as soon as possible.

2. An unregulated international banking system often experiences supply led-expansion, requiring borrowers to show restraint in the face of bankers' overtures

In the early seventies world liquidity and an unregulated eurocurrency market fostered clear supply-led expansion of lending. After a brief period of retrenchment in 1975-1977, banks once again, under pressures of liquidity, began actively soliciting clients in developing countries. Since banks often can show little self-restraint, then borrowers must be prepared to do so. This suggests that countries should carefully control their interface with foreign finance in general and commercial finance in particular; that foreign finance should be used only as a complement to a vigorous national effort to generate resources for development and, when foreign resources are used, care should be taken to ensure that the nature of deployment is consistent with the cost and maturities of the credit. Restraint and sagacious deployment is particularly important for small and medium sized economies where offers of commercial credit can easily exceed the real capacity of the economy to match commercial funds with appropriately commercial activities.

3. Commercial banks are not an appropriate primary conduit of external finance for developing countries and comprehensive reform of the present situation is urgently needed 4/

Even if a country displays appropriate restraint and sagacious management in its relations with commercial banks, its development is still handicapped by the severe qualitative drawbacks associated with commercial bank finance.

The basic underlying problem is that commercial banks are not appropriate primary conduits of development finance. Private commercial banks, as their name implies, are not development institutions and their private commercial time and risk preferences make it difficult for them to accommodate the broad socio-

economic goals of development, which are long term in nature and are based on social rates of return. There are several factors which seriously restrict the behavior of banks.

First they are profit oriented institutions which operate on the basis of private rates of return. They can internalize social rates of return on their lending only to the extent that the latter enhances the former; moreover, the gestation period for such a feedback process tends to be rather long term in nature.

Second, a great deal of bankers' resources come from call or short term time deposits. The short term deposit base places a limit on the degree to which banks can prudently mismatch maturities, i. e., lend long on short funds. Thus, the nature of the resource base gives these institutions only a short to medium term time horizon with regard to lending.

Third, as bankers will readily admit, they have a special concern for minimizing risk and avoiding losses. This orientation is partly a function of tradition, but also reflects the reality that banks operate on other people's money and must ensure the safety of deposits if access to resources is to be maintained. This leads to a conservative view of life where "caution and prudence" are the watchwords for lending operations. When viewing prospective loans to developing countries, bankers naturally are primarily interested in the prospects for repayment. It is not surprising then that liquidity indicators (as opposed to development indicators) dominate creditworthiness criteria; good management is synonymous with ensurance of liquidity to service debts, even if this means deflation of the local economy to free foreign exchange.

Thus, the inability of commercial banks to satisfy the requirements of economic development stems to a large degree from their institutional makeup. For banks to radically alter their behavior would be inconsistent with their structure and basic commercial goals. What is needed, then, is some examination of the alternatives to a commercial bank-dominated external development finance.



### Exploring the alternatives

One has just seen some drawbacks that might be associated with having commercial banks at the forefront of the allocation of resources to developing countries like Peru. Unfortunately, in economics diagnosis is easier than prescription, leaving for the remaining part of the chapter the difficult task of suggesting alternatives.

### The international division of labor for development finance

In general it appears that what is needed is some rethinking about the current division of labor for development finance. There are many sources of finance and each one usually is especially capable of performing certain tasks.

Looking first at commercial banks. They are especially good at financing trade. They have a world-wide network of branches and correspondents with which to follow trade flows. Decisions on finance can be made quickly because of the familiarity among clients. Assessment of risk does not have to be terribly sophisticated, because much of the finance is self-liquidating and the tenor of agreements is on the short side; this, incidentally, is compatible with both the limited risk assessing ability of most commercial banks and the short-medium term deposit base of these institutions.

Banks also are exceptionally suited to finance highly profitable commercial ventures with a quick payout, say between 5 and 7 years. Another area which appears suitable is the finance of working capital, i. e., the pure need for short term liquidity.

Just as banks are exceptionally suited for the above tasks, they are inferior at others. One area where banks display severe limitations is in the provision of finance for ventures with a long payout. Social infrastructure requires maturities far beyond the reach of banks, and not surprisingly, these institutions themselves sometimes are chary about lending in this area.

But many commercial ventures also may be out of the reach of banks, particularly those that involve infant industries and are capital intensive.

Banks also cannot adequately fill liquidity needs when illiquidity is due to structural imbalances (real or financial) in the economy. So if balance of payments or fiscal difficulties stem from something other than a temporary exogenous factor (e.g., a fall in the price of a major export commodity) banks are an inferior source of finance. In these circumstances—which are very common to developing countries—if bank extends "no-questions-asked" finance they become a permissive influence that hides the need for changes in structure and policy. Peru up to 1975 fell victim to an overly cooperative banking community. On the other hand, if banks attempt to induce changes in policy and structure they become interventionist. Because of their private commercial character when they lock horns with sovereign governments they are open to charges of conflicts of interest and political subversion. To this must be added the fact that the maturities that they can offer under the risk associated with restructuring may simply be inadequate for the circumstances. Thus, when banks enter into finance of structural balance of payments problems they enter into a "no win" situation.

Who then are the experts in those areas where commercial banks appear to face constraints? They are multilateral agencies and private bond markets.

Multilateral agencies—i.e., the World Bank, Inter-American Development Bank (IDB), etc.—display great virtue with regard to some of the special needs of developing countries.

First they have highly trained professional staffs which have a wealth of experience with regard to the problems confronting developing countries. They can help in project preparation; troubleshoot where problems arise and help in follow-up evaluation. Thus, they are interested in the success of the project and not just its finance and repayment. These personnel also are capable of collaborating with authorities in the formulation of global policy for development.

Second, and more importantly, multilateral agencies are not commercial institutions and therefore can assume time and risk preferences that are compatible with the far reaching needs of development. Thus, multilateral agencies can and do lend to countries which display liquidity and political conditions that simply would unnerve a private banker. Moreover, their special character enables these agencies to support repayment periods of up to 25 years or more, which is the type of finance that can smoothly promote the broad-based socio-economic change that is integral to the process of development. Implicit in this capability is a willingness to finance projects with a basic needs character, and to encourage this type of development as well.

Third, unlike commercial banks where developing countries have no influence over policy, multilateral agencies incorporate developing countries as voting members and provide opportunities for them to influence events. Nor is this virtue negated by the fact that LDCs are a minority voting block. Indeed, as long as industrialized countries contribute to the bulk of finance, the credibility of multilateral agencies is best maintained if they have technical control over decision making. But LDCs, acting together, can provide an effective lobby for pressuring the industrialized countries to adopt policies favorable to their needs. Also LDCs can improve their voice in policy to the extent that they insure maximum representation on the staffs of multilateral agencies, sponsoring individuals for their technical competence and not for their domestic political connections.

The above is not to suggest that multilateral institutions are perfect. The quality of their finance undoubtedly can be improved. The IMF would appear to be in need of the greatest amount of reform. 5/ For example, better articulation between the Fund and the World Bank is appropriate so that standby programs can take on a longer term character and facilitate real structural—as opposed to just monetary/financial—change. In line with much longer standby

agreements, conditionality could be moderated to take into greater account domestic political and social objectives and the need to avoid reductions of employment and per capita income in poor countries. And in order to facilitate more disbursements and greater flexibility in development there is great need for significant program lending by development institutions like the World Bank and IDB. One could go on about where changes are desirable. Fortunately, unlike commercial banks whose actions are constrained by the commercial interests of their stockholders and the rules of prudent banking, the policy frontiers of multilateral institutions are only limited by the courage and imagination of policy makers in the industrialized countries.

As for private bond markets, they afford developing countries the opportunity to acquire funds on terms considerably longer than those usually offered by commercial banks. Also, their interest rates are generally fixed through the life of the maturities, providing LDCs a predictable cost that can be neatly incorporated into planning strategies. Another consideration is that bond markets are really standoffish and remote in the sense that borrower and lender never meet each other. Their major drawback is that investors tend to be rather skittish and therefore access may be somewhat unreliable.

There are two other important specialists in the international financial area that are worthy of mention: commercial suppliers and bilateral government agencies. Both usually are associated with "vested interest" finance, i. e., finance itself is only a means to a broader objective. The conditions of finance sometimes can be attractive, although this is offset by their being tied to particular goods or political positions. Nevertheless, sometimes the interests of the borrower may overlap with that of the lender, making for a mutually beneficial transaction. It is in these circumstances that suppliers and governments have an important role to play in the division of labor for development finance.

Can the division of labor be made to work?

One has just seen what may be considered to be a reasonable division of labor for finance based on an existing infrastructure. Unfortunately, some actors in the global division of labor have had their activities restricted for one reason or another, creating a vacuum that has been filled in an ad hoc fashion by commercial banks, which in contrast have been able to expand almost without limits on a base of surging world liquidity and an unregulated eurocurrency market. The problem, as has been seen, is that banks cannot properly assume their new role. The question is how can the imbalance in the sources of finance be rectified.

Since any fundamental alteration of the workings of the division of labor for development finance would require at least a medium term period to realize itself, one can look first to immediate solutions that involve adjustments to the present situation and then follow with a longer view involving a more comprehensive reordering of relationships.

Immediate adjustments in the present system

In the short term the goal must be to make the best of an unsatisfactory situation, i. e. , to try to assuage some of the sharper edges of bank lending behavior. The scope of change, however, can only be very limited because many of the problems are intrinsic to the institution of private commercial banking itself. Also, change is handicapped by the fact that there are hundreds of banks operating internationally, with no central control over their liquidity or behavior. Nevertheless, some action can be taken to alleviate the situation without violating the boundaries of prudent banking.

As a general rule commercial banks might take greater care to operate in areas where they are institutionally most comfortable in the long run and

therefore reduce the possibilities of radical alteration of behavior that is disruptive to market stability and the development of developing country borrowers.

In this spirit, banks could consider concentrating their lending in traditional areas of competence, i.e., commercial ventures that require working capital or investment finance. Moreover, banks could avoid lending to commercial ventures merely on the basis of a government guarantee; rather, it might be advisable to coldly evaluate ventures on commercial (and not political) grounds with a view to assessing the real repayment prospects of the venture itself. When ventures are commercially evaluated by the banks, they actually would be doing borrowers a favor if they held back finance from an activity that could not support repayment on its own. In other words, banks should cease to treat governments as if they had some type of fail safe repayment mechanism; lending for commercial ventures should conform to the same standards that would apply to any commercial entity.

Following the above prescription, commercial banks should avoid direct balance of payments finance. Experience has shown that banks are incapable of absorbing the political-economic shocks that often accompany an LDC adjustment process; they also are not suited to be involved in public macro-economic policy making. So why enter terrain that ultimately may require a quick and disruptive retreat? Banks would find it less necessary to enter into balance of payments support if countries were more comfortable with the IMF; thus this latter institution should for once and for all moderate its conditionality and adopt a more pluralistic methodology for tackling the adjustment problem. Medium term program lending from the World Bank and IDB also would help banks avoid direct balance of payments finance.

Commercial banks of course will frequently be asked to refinance, which is indirect balance of payments support. And refinance should be considered a

natural way to assuage repayment difficulties and borrowers should not be "punished" through higher than average interest margins and shorter than average maturities. It should be remembered that the real capacity of almost all borrowers to meet their debt service hinges on the refinance and rollover process; since most developing countries run heavy deficits on current transactions debt is almost always repaid with new debt. Thus, to weigh a weakened borrower down with onerous interest margins and short maturities actually may increase the risk of non-payment rather than reduce it. In the case where a developing country is facing internal structural difficulties and bunched maturities banks could cease to be reluctant to enter into rescheduling agreements. A medium term rescheduling of principal could be viewed as a routine way to provide relief and reduce risks of non-payment. If interest payments are kept current, as they should be, banks would encounter extra bookkeeping work, but not necessarily losses of income.

Commercial banks also could take a broader view on prepayment strategies. In the end prepayment can help a country assuage the effects of the constantly changing terms on commercial markets and therefore really enhance capacity to repay debt and contract new debt. Thus, placing heavy prepayment penalties on credits with relatively favorable terms to the banks might be counterproductive to all concerned.

There are three other specific areas where banks could consider altering their behavior:

- a) One is that banks might seek more long term funds so as to reduce their dependency on short term deposits and thereby prudently lengthen maturities. Some banks like Citicorp have already attempted to do this, but hopefully the strategy will become more intensive and generalized in the world banking community.

- b) Banks might reconsider the need to act as world policemen for TNCs. When a TNC invests in a country (and banks help them) all parties take calculated risks based on the returns to capital. Thus lending to an LDC government should be viewed as a separate business transaction and should not be linked to the fortunes of a locally based TNC. In the early seventies banks showed that there does not have to be a connection between a government's treatment of foreign investment and successful business relations between them and a government. So why renew the ancient practice of fronting for TNCs?
- c) Banks could avoid offending the sensibilities of developing countries borrowers through demands to waive sovereign immunity and local jurisdiction over loan agreements. As an alternative to the traditional practice, one could see greater employment of international arbitration as a way to satisfy a bank's requirements for security and a government's desire to avoid an alien country's legal system.

#### More fundamental changes

The above proposals could provide short term relief to developing countries. But to rectify the imbalance in the division of labor of development finance there is a clear need to begin work to drastically increase the resource flows coming from the real specialists in development finance, i.e., official agencies and long term capital markets.

Multilateral agencies have suffered from a lack of an automatic funding mechanism, aid weariness, and a general ideological shift away from multilateralism. In an age of fiscal deficits and tax revolts new contributions to development institutions have become unfashionable; perhaps one reason for the industrialized countries' complacency about the role of their banks in development



finance is that it simply is less of a fiscal burden to have private commercial banks channeling resources to developing countries. Indeed, to the extent that bank earnings are taxed by the center's governments there actually may be fiscal gains in the present situation.

What one needs to counter this trend is a campaign to educate the public in the need for massive resource transfers on more reasonable terms to developing countries. And this can be viewed as simply enlightened self-interest. While commercial bank financing appears on the surface to be working smoothly, the inferior quality of the finance, coupled with other well known maladies of the international economy, may be generating underlying social and economic tensions that could make for a more difficult world in the 1980's. Moreover, transfers to the periphery usually come back to the center in the form of purchases for import, creating new business and jobs for industrialized nations.

There has been no lack of proposals for massive transfers; they range from the Mexican government's Long Term Recycling Facility to Venezuela's (Ronald Müller's) global Marshall Plan. They all are characterized by sophisticated mechanisms to provide long term finance to developing countries. Multilateral agencies are seen to be the manager of funds. The major obstacle to the programs seems to be the generation of resources.

It therefore may be worthwhile to briefly review some tentative ideas on how resources could be generated, concentrating on the need for automatic funding.

One possibility is to assign to the World Bank and IMF a more direct role in transferring savings from surplus countries to deficit developing country governments. Many have complained about the lack of symmetry in pressures on countries to adjust their balance of payments; deficit countries must undergo

vigorous IMF programs while surplus countries suffer at worst moral suasion. Why not arrange for surplus countries to place 50% of their annual surplus (after adjustment for coverage of "normal" capital outflows) on deposit with the aforementioned institutions? A commercial interest rate could be paid for the deposits. Withdrawals would not be permitted until a surplus country's "non-deposited" surplus fell to some critical level—say the equivalent of 3 months' imports and then withdrawals would still be staged to the trends in the country's balance of payments. Since surpluses tend to accumulate in certain industrialized countries and some OPEC countries, the fund would be continuously renewed. The special character of developing institutions will allow them to mismatch maturities and transfer these resources to the periphery on appropriate terms. Admittedly, unless the surplus is taxed this proposal would place only mild additional pressure on surplus countries since access is maintained to surplus receipts; its chief value is that it would allow more resources to be channeled through development agencies.

Ways also need to be explored on how to bring permanent increases in the capital base of international agencies, which will facilitate their ability to capture funds on international capital markets. One measure might be to channel allocations of SDRs to subscriptions of capital in these institutions. Inviting the centrally planned economies to play a more active role in development finance also would increase available resources and provide more ideological plurality in the international financial scene. Industrialized countries and OPEC also could consider directly guaranteeing bond issues of multilateral agencies, thereby facilitating greater leverage over the existing capital base.

Less certain are the possibilities to raise capital contributions via taxes in industrialized countries. The constraints are more political than real, however, as ample room exists for new revenue. Emergency economic development

taxes on luxury consumption, i. e., cigarettes, liquor, oversized cars, second homes, luxury restaurants, etc., could undoubtedly painlessly produce considerable annual contributions. The problem in this approach is that small interest groups may be able to resist the introduction of what otherwise are rational measures.

Another scheme that enjoys some support is co-financing between commercial banks and development institutions. In this way banks would come under the umbrella of multilateralism and effectively expand resources being channeled through development agencies. Banks participating in co-financing would presumably offer slightly lower interest rates and somewhat longer maturities. The value of the scheme is that it requires no real change in the existing financial system. The disadvantage is that it could be construed as a substitute for increasing the capital base of multilateral agencies. It also could further erode the plurality in the sources of finance and "cartelize" development finance.

In exploring the resource problem, it also might be useful to question the current practice of having multilateral institutions charge all developing countries the same rate of interest on regular (e. g., non-IDA) loans. In order to stretch development funds to the greatest degree possible, one might consider tiering interest rates to the level of development of the country. Lower income countries could continue to receive absolutely concessionary rates. On the other hand, upper income countries are not interested in aid but rather longer maturities and could be charged commercial rates of interest. Furthermore, rates to upper income countries could continue to be fixed, but with provision for periodic adjustment on old loans should they become uncommercial over the medium term. Even with commercial rates there could be some cost savings on loans; with greater access to multilateral finance there might be less need to maintain large amounts of borrowed international reserves; many of the fees and ancillary charges of loan syndication would be eliminated and prepayment could be effected without penalty.

Turning to international bond markets, they have not been a dynamic source of funds for developing countries since the great financial collapse of the late 1920's. Industrialized countries have placed great administrative barriers in the way of LDC bond issues, creating a two tier system whereby rich countries tap eurobonds and poor countries eurocredits. This is distressing because bond markets can be a very suitable way to finance development, and while they cannot substitute for a dynamic multilateral development finance, they certainly can take some pressure of these institutions. Undoubtedly, rich countries should reconsider their policies in this area. Also mechanisms might be explored for having industrialized countries guarantee bond issues of developing countries.

As for bilateral finance, this has no doubt slipped because of aid weariness. It might be difficult to stimulate this source of finance, although schemes that are designed actually to restrict funding, such as the Gentlemen's Agreement among OECD export credit agencies, could merit reconsideration, at least with regard to finance for LDCs.

One cannot help but think after reviewing proposals for transfers and some possibilities to finance them that current problems are of a political rather than an economic nature. There are a multitude of technical ways to enhance the functioning of the international division of labor for development finance. The obstacle is to develop the political will to implement them. Many may feel that any massive reordering at this time runs counter to political realities and it is therefore best to accept, with perhaps some minor modifications the present system. However, in closing, one should remember that reality is to some degree fungible and with due willpower and courage one can improve upon the present transfer mechanism, which has evolved in an ad-hoc fashion and is less than adequate for the promotion of broad-based socio-economic development. Hard core realists who may be skeptical of change should perhaps ponder on the fact that those who are excessively realistic can be the most unrealistic of all.

Chapter 1

FOOTNOTES

1. Banks also can be interventionist when there is no debt crisis. See the case of Brazil in Devlin (1979).
2. The United Nations Centre on Transnational Corporations in New York has wisely initiated some ground-breaking studies on the behavior of international commercial banks.
3. In the case of Peru the World Bank's tabulation of publicized eurocurrency credits provides only a partial view of transactions with commercial banks. The data also provide only limited information on a syndicate, the conditions of the agreement, and the specific role of each bank in the operation.
4. Much of this section is based on excerpts from the author's paper cited in footnote 2.
5. For a in-depth critique of the Fund's stabilization policies see United Nations.

Chapter 2

Introduction and methodological notes

1. Introduction

The decade of the 1970's has witnessed the emergence of private international commercial banks as important participants in the external finance of developing countries. In 1970 banks accounted for roughly 19% of the total current account financing (including reserve accumulation) of the non-oil exporting developing countries, most of which was short term (maturities of less than one year) in nature. However, by 1974, the banks generated 33% of this finance, with the bulk of/transactions falling into the medium to long run (1-5 and over 5 years, respectively) category. With some increase in lending by official agencies in the post-oil crisis period, coupled with<sup>a</sup> moderation of current account deficits in the period 1976-1978, the banks' participation slipped back somewhat to between 25% and 30% of the total. Again medium to long term transactions predominated.<sup>1/</sup>

While commercial bank finance has become important to LDCs taken as a whole, it is in<sup>the</sup> upper income developing countries like those of Latin America where much of the lending has been concentrated. As seen in table 2.1 Latin America accounted for nearly two-thirds of the gross indebtedness of non-oil exporting developing countries to commercial banks and almost all the indebtedness on a net basis. While a great portion of this debt is carried by superborrowers like Brazil and Mexico, other countries like Peru, Chile, Argentina, Panama have become important clients of international banks as well.

Table 2.1

INDEBTEDNESS OF NON-OIL DEVELOPING COUNTRIES TO PRIVATE  
COMMERCIAL BANKS, END DECEMBER 1977 <sup>a/</sup>

(billions of dollars)

	Developing countries				Total	World
	Latin America <sup>b/</sup>	Middle East <sup>c/</sup>	Africa	Asia <sup>d/</sup>		
Gross	71.1	1.9	14.0	21.6	108.6	657.3
Net <sup>e/</sup>	36.2	-7.1	3.0	-1.2	30.9	658.3

- <sup>a/</sup> Includes short term debt  
<sup>b/</sup> Excludes Caribbean area and Panama  
<sup>c/</sup> Excludes Israel and residual estimate  
<sup>d/</sup> Excludes Hong-Kong and Singapore  
<sup>e/</sup> Debt less deposits in the banks.

Source: Bank for International Settlements, Forty-Eighth Annual Report, Basle, 12 June 1978, pp. 94-95.

Likewise, the relative weight of banks in the structure of Latin America's external finance also has become considerable. In 1966-1970, the average net contribution of banks to the current account finance of Latin America was only slightly greater than 12% of the total; however, by 1974 the banks accounted for more than two-thirds of net flows, and in 1976, despite new lending by international organizations (e.g. IMF oil facility), their contribution still was near 50%.<sup>2/</sup>

Thus there is little doubt that private commercial banks have become a force to be reckoned with in the external finance of the region. And their importance must not be taken as a mere passive element in finance. As pointed out by Barnett and Müller: "... banks can exert considerable power over underdeveloped countries that are poor in foreign exchange because they control the faucets from which dollars flow"<sup>3/</sup>

Sadly, while banks' power over the affairs of many LDCs has been growing rapidly as a result of their control over foreign financial flows, there is an incredible dearth of information with regard to the specific nature of bank lending to LDCs and the impact that this has had on the development of the periphery. What improvements that have been made in collecting data on the subject have been for very recent periods and have involved a high degree of aggregation that reflects the needs of regulatory authorities in the center rather than the requirements of developing countries. Thus, available data reveal little about the evolution of the borrowing and lending processes, the underlying factors and actors, and the precise implications that all this has had for developing country borrowers.



Because of the problem of a lack of information, or excessive aggregation of data, analysis of the phenomenon of bank lending to LDCs has been mostly limited to generalization, with little consideration as to whether events have differed among lending institutions and borrowing countries. The only studies that have penetrated somewhat the veil of aggregation have been those by Wellons and Sánchez Aguilar.<sup>4/</sup> The former gives a good orientation to the general institutional process of lending and complements this with some perspicacious, but very brief, analysis of the cases of a number of LDC borrowers (of which Peru is not one). The latter analyzes the lending of U.S. banks to Mexico in the early 1970's. Both studies have made a valuable contribution to the enhancement of understanding of bank involvement in the external finance of LDC's; however, the scope and depth of analysis are severely handicapped by an obvious data constraint.

## 2. Goals of the study

The basic general goal of the study is to begin to break the above-mentioned analytical bottleneck concerning the lending and borrowing processes that have generated LDC commercial debt. A more penetrating view is sought of the phenomena in order to enhance decision making capacity of LDC governments with regard the contraction of commercial loans.

As for the commercial banks, an objective is to gain a more comprehensive view of the nature of their lending activities in general. The analysis also is undertaken to show that banks cannot be treated as a homogeneous group; that while showing common characteristic and

motivations, they also have distinct modes of behavior. The different modes of behavior mean that some banks would be more important to the government than others and that there would be variable relations with individual banks, both at points in time and inter-temporaneously. And, of course, some behavior could be deemed as being more favorable to the borrower than others.

As for borrowers, the goal of the study is to ascertain the motivations (over time) behind the contraction of loans from banks and assess the impact that commercial loans have had on both the macro and micro aspects of economic development.

### 3. The general methodology

One way of approaching the subject would be to have individual banks provide detailed information on their portfolios and their lending to individual LDC's. However banks are notorious for their use of the protective shield of confidentiality, making it difficult for even home country governments of the banks to secure disaggregated data on lending operations. In view of this, an alternative would be to go directly to borrowing countries for data that will reveal the behaviour of banks and their impact on development. However, this represents a formidable task, requiring one to systematically dig deeply into raw data in the field for a number of selected countries, and then reaggregate this information in a manner which promotes a better understanding of the lending by banks and their influence on developing countries. Notwithstanding those obstacles the latter option represents the basic methodology of this study. However, given the complexity of the matter and given limited resources it was decided to initiate the project in one country and follow up with more case studies later, adjusting them to the findings of the initial effort.

It was deemed impractical to begin the project with a superborrower such as Brazil or Mexico because of the fear that disaggregation of such voluminous lending by banks might create an unwieldy data base for launching an initial case study. Peru finally was selected as the first case due to the fact that, while still a major client of the banks, it offered prospects of a more manageable data base. Also, the country has had a very interesting recent economic history. In order to capture a more than contemporary view of bank lending, it was decided to have analysis begin in 1965, thus incorporating at least 5 years of activity that would reflect the traditionally conservative relationship between these institutions and LDCs. The 1970's, of course, would reflect the new style of world banking that made developing countries acceptable, if not very attractive, clients for loans. The year 1976 was used as the cut-off date for the study, because as will be seen, it represents the last year in which Peru enjoyed general acceptability among the world's commercial bankers.

Another decision was to focus only on medium and long term lending to the public sector, or lending with guarantees by the public sector. Short term lending is qualitatively different than medium and long term transactions and data collection for the former would have been even more difficult than that for the latter. Meanwhile, the vast majority of medium-long term lending by commercial banks to Peru has been through the public sector, making the study of government loans practical from the standpoint of comprehensive coverage.

Since the study was entering virgin territory, Cepal prepared a project manual before initiating field research. The manual, entitled

Project Manual and Methodological Guidelines for a Study on the Role of Transnational Banks in the External Finance of Peru,<sup>5/</sup> provided the objectives and hypotheses underlying the study, predesigned data sheets to be filled out during the process of data collection, and tentative modes for the processing and analysis of the data. The manual made clear that the methodology would be a holistic one, attempting to understand phenomena as related to both lender and borrower. Thus the study's shifting focus between the banks and the public sector.

Field research was undertaken and the public sector was combed for data covering the 12-year period. While seeking aggregated data for financial flows from all sources, the most disaggregated data possible were sought on individual commercial bank loans, using table format 21 of the aforementioned Project Manual as the guide for its collection. The goal was to collect comprehensive data on every individual commercial loan to the public sector, but purposely excluding credits related to national defense.<sup>6/</sup> The basic goal was realized, as a comprehensive data base was generated. However, not having perfect information, and given the disperse nature of the Peruvian public sector, no guarantee can be made that the data are a perfect image of the defined universe. But if they are not identical to the universe, they are certainly a very close approximation of it.

After collecting data on individual bank loans information was cross-checked for consistency and accuracy. Profiles were then developed on individual commercial lenders, incorporating all the comprehensive information from table format 21 of the Manual. Once profiles were prepared, analysis was performed on individual banks, data permitting.

Data also were rebuilt into new forms of aggregation which shed light in varying degrees of generality on lending behavior and its impact on the borrower.

The results of the process of disaggregation and deliberate reaggregation provided a new and unusually comprehensive view of bank lending to a developing country. The results of this and other analysis are found throughout the rest of the study.

4. Some specific aspects of the methodology

There are some other specific aspects of the methodology which should be brought to the reader's attention. They are as follows:

- a) subsidiaries of banks were incorporated into the parent where ownership was more than 50%;
- b) when loans were syndicated credits, the syndicate itself was broken down with relevant information being placed into the profiles of the respective banks;
- c) non-dollar loans were converted into U.S. dollars at the rates of exchange prevailing at the time of authorization;<sup>2/</sup>
- d) split interest rates were averaged, weighted by the number of years (or alternatively the amounts on which) each rate prevailed;
- e) fees and penalties that changed value over the life of the loan were averaged in a way similar to (d); and
- f) in re-aggregation, quantifiable terms and conditions of the loans usually were weighted by the value of individual credits.

5. The format of the study

Chapter 3 and 4 focus on borrowers and lenders, respectively.

Chapter 3 is a brief account of the evolution of the political economy of Peru over the last 12 years, with a view to explicating those factors that influenced its demand for foreign resources and also those that may have conditioned the response of foreign suppliers of finance. Chapter 4, focuses on the actual response of the supply side over the 12 years, and the factors underlying this response. Here general commercial bank finance is viewed against the finance supplied by other sources of credit.

Chapter 5 and 6 represent a detailed analysis of the nature of commercial lending over the 12 years. The former chapter, through an inter-temporal comparison, analyzes how lending changed radically between the 1960's and 1970's with regard to actors, types of finance and the terms and conditions of credit. The latter chapter expands on the nature of lending by analyzing in detail one of the major mechanisms behind the expansion of bank lending to LDCs: the syndicated credit. The chapter deals with how syndication has evolved with regard to Peru, the major actors and strategies behind this type of operation.

Chapter 7 focuses specifically on the banks and attempts to discern differential behavior among individual commercial institutions and groups of institutions, as it has applied to Peru. The focus is on such things as relative commitments to Peru, costs of credit, preferences for types of loans and sectors, behavior of banks with local operations in Peru, etc.

Chapter 8 focuses on the impact of bank lending on the economic development of Peru. Analysis focuses on specific issues such as the nature of support of public investment and conditionality, as well as an overall evaluation of both the positive and negative aspects of bank involvement in the economy.

The last chapter, nine, is a brief descriptive update of events which will take the reader from the last year of analysis - 1976 - through the difficult period of 1977-1979.

The study also contains a statistical appendix and an annex which provides brief descriptive profiles on the role of some key banks in lending to the government over the period 1965-1976.

6. Some final considerations

First, the findings of this study must be considered as being specific to Peru. However, data often are suggestive of broader phenomena, inevitably bringing forth generalizations. Any generalizations brought up in the study are mostly tentative in nature and should be treated as hypotheses awaiting further testing. Hence the need for more case studies on the borrowing of LDCs.

Second, it was almost impossible to get partial, let alone perfect information, on the strategies and motivations of all the individual lending institutions. As noted earlier, data on banks are sparse and lack precision. Thus, as the reader will note, there often is no alternative but to conjecture about the factors underlying behavior of individual institutions or groups of institutions. This suggests the need to combine case studies such as this one with follow-up interviews with bankers on why they behaved the way they did in certain circumstances.

Third, every attempt has been made to ensure accuracy. However, both the large scope of the study and the attempt to bring analysis down to highly disaggregated levels generates greater than normal risks of errors in fact. Readers of the draft document would be doing a great service, then, if any perceived errors are brought to the attention of the author.

Footnotes

Chapter 2

1. Data are from Watson, table 2, pp. 12-13.
2. See Massad and Zahler, table 1, p. 4.
3. Barnet and Müller, p. 142.
4. See Wellons (1977) and Sánchez Aguilar.
5. See Devlin (February 1978).
6. The only area where national defense loans are incorporated into the data base is in the aggregated global lending data presented in Chapter 4.
7. The borrower's definition of authorization was employed. It was found that in many cases that the borrower's date of authorization of a loan could be as much as three months after a commercial bank's date of authorization.



### CHAPTER 3

#### The public sector and its demand for external resources

While it is beyond the scope of this study to attempt a detailed historical evaluation of the Peruvian economy,<sup>1/</sup> an effort will be made to highlight those events and factors that were decisive in the public sector's recourse to external finance. Material in this chapter is presented on two levels.

On one plane, the chapter is designed to provide the reader with key background information on the political economy of Peru over the 12 years under analysis here. This material, which is of necessity descriptive, constructs a local scenario that will be supportive of later analysis of bank lending. The focus, of course, is on those domestic economic and political events that influenced Peru's demand for external finance in general and bank finance in particular. Care also is taken to incorporate local events that may have affected, either positively or negatively, foreign lenders' willingness to extend finance to the government. (The actual response of the supply side is for reasons of exposition reserved for chapter 4, however.) These domestic events behind recourse to external finance are treated in chronological fashion, using 1965 as the point of departure.

On a second plane the chapter attempts to complement the chronological description of key events with some analytical view of just what factors were behind Peru's need for external finance. The analytical element is incorporated in two ways. Those factors of demand that are

peculiar to a particular point in time are woven into the description of the political economy of Peru. Meanwhile, those factors which are more generalized, or common to the 12 years, are brought into focus in an analytical overview that closes the chapter. This overview also will serve as a form of summary to the admittedly broad time span covered in the descriptive survey.

I. A synthetic review of Peru's political economy, 1965-1976

In a simple framework, it can be said that the public sector's requirements for foreign finance are closely linked to the fiscal budgetary operations of the government and the behavior of the country's balance of payments.

In the first instance, external borrowing may be needed to help support fiscal expenditure. The nature of this support can vary according to circumstances.

A budget may be in perfect equilibrium yet be in need of foreign finance. This / <sup>occurs</sup> because almost all budgets have a foreign component and foreign currency income may fall short of foreign currency expenditures. If a government wants to avoid drawing down on its international reserves, external borrowing may be its alternative.

But foreign borrowing more often is associated with deficit finance. Given a desired level of expenditure and a given level of tax revenue, a government has several options in terms of financing the gap between income and budgetted outlays. One is that it can borrow in the domestic financial market. There are often severe limitations to this approach, however, since developing country capital markets are notoriously very thin and therefore full domestic finance of a large deficit may

prove to be highly disruptive to the whole economy, or simply impossible to realize at all. An alternative form of finance is to create the resources by taking recourse to the Central Bank's printing press. But this easy route to finance is also a very dangerous one because of its severe impact on inflation. Finally, if there is a ready access to private capital markets abroad, a government may opt to cover the fiscal gap through foreign borrowing. Because of interest differentials between home and foreign capital markets, the latter option may be attractive even if domestic finance is available to cover the fiscal deficit.

In practice governments use all three methods of finance, with their respective importance varying with the size of the deficit to be financed, and the nature of access to financial capital at both home and abroad. But when domestic capital markets are small and the financial need large, the real options sometimes are between emissions and foreign borrowing. The latter is usually considered to be the more prudent source of finance, although feasibility depends on the willing hand of foreign financiers.

It also is important to point out that deficits can sometimes be more apparent than real. This occurs when deficits are a manifestation of lagging tax effort. Thus, foreign borrowing and/or emissions can simply be an expedient measure to avoid the hard realities of a need for greater restraint in spending and/or more intense tax effort.

With regard to the balance of payments, it is the public sector's responsibility to guaranty the "money-ness" of the local currency through

its transformation into needed foreign exchange. In a developing country, current account transactions usually do not balance, requiring some form of external finance. Furthermore, there usually are requirements to finance debt service payments and capital outflows generated by nationals and foreign residents. Some of the need for finance can be covered autonomously as importers (including those of the public sector) often bring foreign credit to bear on their transactions; as foreigners are likely to be making some new investments in the country and national capital may be repatriated. However, more likely than not the net effect will be an unfinanced gap that the public sector will have to fill either indirectly, through a general program of borrowing, or directly through compensatory balance of payments loans or draw-downs of official reserves. In addition to financing the external gap, a government also may borrow simply to build up foreign exchange reserves, which are looked upon as a form of security by international creditors.

The actual amount of finance required to support the balance of payments depends on many factors. The country's export vocation, income and price elasticities of demand for imports, terms of trade, level of factor payments, swings in private capital movements, etc., all are determinants. Some elements of the balance of payments performance are out of the governments control, e.g., external prices and natural events - weather, ecological changes, etc. - that can alter the exportable surplus or change import requirements. On the other hand, the government has policy instruments at its disposal that can influence the requirements

for external finance. These go from the style of development that is officially promoted, down to demand management, exchange rate regimes, tariff levels, fiscal incentives and disincentives, policies towards foreign investors, etc. Some policy measures can have an immediate impact on the external sector, e.g. import quotas, while others take longer to work their way through the system, e.g., export incentives. But timely policy measures are crucial to balance of payments management. And while foreign finance is useful to bridge financial gaps and time lags associated with policy instruments, it also can become an opiate that hides the need to introduce corrective measures. Thus, if a borrower lacks discipline, easy access to foreign finance can actually be permissive, promoting widening of external gaps, mounting external debt, and later problems if an adequate flow of finance cannot be maintained.

It is within this general framework that one can view the Peruvian experience with banks. Thus the following account of the political economy of the public sector and demand for foreign resources will tend to revolve around the fiscal accounts and the balance of payments, although other areas will be incorporated where they are deemed to be significant.

A. 1965-1966: The seeds of crisis

The study on commercial bank lending to Peru begins at a time when the economic program of Peru's newly elected administration was in full gear. The government, which came into office in mid-1963, was reformist in character and its program mirrored the principles of the Alliance for Progress, as expressed in the Charter of Punta del Este.<sup>2/</sup> Policy was oriented to pursuing the industrialization process (via import substitution) that began in earnest in the late 50s and which was progressively changing the structure of an economy that traditionally had been dependent on primary commodity exports generated by the investments of foreigners and members of the national oligarchy.<sup>3/</sup> But at the same time authorities also gave attention to programs of a social nature, especially in the areas of education and moderate land reform,

that were designed to calm peasant unrest and narrow a gap between rich and poor that was perhaps nowhere greater in Latin America.<sup>4/</sup>

Activist government policy was something of a novelty for Peru, where the public sector by tradition was relatively small<sup>5/</sup> and where the economy had long operated in a laissez faire environment.<sup>6/</sup> Partly as a consequence of this, the public sector was not as sophisticated as its counterpart in some other Latin American countries and there were few mechanisms for the control and coordination of an ambitious program. Nevertheless, government expanded rapidly as reflected in the fact that outlays (exclusive of amortization) more than doubled over 1963-1965; <sup>7/</sup> even in real terms growth was substantial, roughly estimated at more than 50%.<sup>8/</sup> In expanding authorities were careful, however, to respect traditional boundaries of activity as public investment was largely confined to infrastructure (especially roads), leaving unchallenged the private sector's domination of productive activities. Moreover, direct foreign investment continued to be the explicit cornerstone for financing productive capital formation.<sup>9/</sup>

By 1965 there were some signs of strain in the economy. The fiscal accounts were moving into increasing disequilibrium - after having been practically in balance in 1962-1963,<sup>10/</sup> and inflation was on the rise (see tables 3.1 and 3.2). Also, as the export boom of the early 60's receded, so did the relatively high rate of growth achieved during the period. On the other hand, imports accelerated. External prices for imports were very much higher this year. Moreover, volume was fueled by an increasingly overvalued exchange rate,<sup>11/</sup> stagnant food production, public investment and renewed vigor in the private sector. As a result, the trade balance, which had tended toward

Table 3.1

## PERU: GROSS NATIONAL PRODUCT AND CONSUMER PRICES

(Rates of growth)

	Average 1961-1964	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976
GDP in 1970 prices (soles) <u>a/</u>	6.9	4.8	5.7	1.6	0.7	4.4	9.1	5.1	5.8	6.2	6.9	3.3	3.0
Consumer prices <u>b/</u>	7.1	16.1	9.2	9.8	19.0	6.3	4.9	6.9	7.1	9.5	16.9	23.6	33.5

Source: GDP: CEPAL on the basis of official data; consumer prices: IMF, International Financial Statistics, May, 1978, vol. XXXI, No 5.

a/ Market prices.

b/ Annual average.



Table 3.2  
PERU: SUMMARY OF CENTRAL GOVERNMENT REVENUE AND EXPENDITURE

(Billions of soles)

	Average 1962-1964	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976
Current income	11.9	17.4	20.3	23.7	30.2	34.0	38.8	41.4	45.6	53.4	68.6	87.9	111.4
Current expenditure	10.9	16.3	19.5	23.6	27.2	28.0	32.2	37.0	42.3	52.0	62.4	90.5	122.7
Savings	1.0	1.1	0.8	0.1	3.0	6.0	6.6	4.4	3.3	1.4	6.2	-2.6	-11.3
Capital expenditure	2.5	5.2	5.9	6.3	6.1	6.4	9.9	12.5	14.1	15.4	20.2	28.0	37.1
Amortization	...	1.3	1.6	1.8	3.6	4.0	5.8	8.1	9.0	15.8	16.1	12.9	16.1
Overall expenditure	...	22.8	27.0	31.7	36.9	38.4	47.9	57.6	65.4	83.2	98.7	131.4	175.9
Deficit	...	-5.4	-6.7	-8.0	-6.7	-4.4	-9.1	-16.2	-19.8	-29.8	-30.1	-43.5	-64.5
Memorandum													
Items:													
<u>As percentage of gdp</u>													
1. Current income	14.2	15.1	14.8	15.1	16.2	16.3	16.1	15.7	15.5	14.9	15.3	15.8	14.5
2. Current expenditure	13.1	14.2	14.3	15.0	14.6	13.4	13.4	14.0	14.4	14.5	13.9	16.3	15.9
3. Capital expenditure	2.6	4.5	4.3	4.0	3.3	3.1	4.1	4.7	4.8	4.3	4.5	5.3	4.8
4. Total expenditure excluding amortization	16.0	18.7	18.6	19.1	17.9	16.5	17.5	18.7	19.1	18.8	18.5	21.3	20.8
5. Total expenditure including amortization	...	19.8	19.7	20.2	19.8	18.4	19.9	21.8	22.2	23.2	22.1	23.7	22.9
6. Deficit	...	4.7	4.9	5.1	3.6	2.1	3.8	6.1	6.7	8.3	6.7	7.8	8.4
<u>As percentage of expenditure</u>													
Deficit	...	23.7	24.5	25.2	18.2	11.5	19.0	28.1	30.3	35.8	30.5	33.1	37.2

Source: Derived from data of the MEF and CEPAL.

equilibrium in the early 60s, recorded a sizeable deficit in 1965 and the current account needed considerably more finance than was customary for Peru (see table 3.3).

The weakening fiscal situation stemmed from the considerable growth of expenditures associated with the administration's reform program and the effects of domestic inflation, coupled with the fact that the national tax base was narrow and relatively inelastic. Moreover, taxes themselves were a sensitive political issue and an opposition Congress was little disposed to support needed tax reform.<sup>12/</sup>

Financing of the fiscal gap through the tapping of local savings was not easy, both because of the underdeveloped nature of national capital markets and public officials' lack of experience in the use of debt instruments. Thus, Central Bank primary emissions were a frequent source of finance,<sup>13/</sup> although recourse actually was minimized in 1965 due to a new awareness of the inflationary impact of such practices.<sup>14/</sup> Another important source of finance was relatively short term commercial borrowing abroad, which also conveniently helped to finance the external deficit.

Here one also should bring to the readers attention that by 1965 there were clear signs of growing apprehension about foreign direct investment, traditionally a prime component of the country's external finance. While foreign influence in the Peruvian economy had long been considerable and a source of concern for some sectors of the population,<sup>15/</sup> it had by now become a public issue largely because of a heating up of a long standing dispute with the International Petroleum Company (IPC), a subsidiary of Standard Oil of New Jersey,<sup>16/</sup> that raised passions about the role of expatriate capital in the economy.<sup>17/</sup> Indeed, the incumbent

Table 3.3

PERU: BALANCE OF PAYMENTS  
(millions of dollars)

	Average 1960-1964	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976
Exports goods and services	615	772	909	884	999	1 050	1 224	1 064	1 153	1 345	1 841	1 689	1 746
Imports goods and services	577	845	1 034	1 048	909	895	971	1 012	1 103	1 484	2 442	3 038	2 627
Trade balance	38	-73	-125	-164	90	155	253	52	50	-139	-601	-1 349	-881
Factor payments	-66	-91	-128	-147	-149	-185	-133	-125	-121	-163	-172	-242	-371
Profits	(-59)	(-62)	(-95)	(-98)	(-76)	(-113)	(-73)	(-50)	(-42)	(-80)	(-42)	(-15)	(-44)
Interest	(-7)	(-27)	(-33)	(-49)	(-73)	(-72)	(-60)	(-75)	(-74)	(-83)	(-130)	(-227)	(-327)
Current account	-22	-159	-246	-305	-53	-27	146	-69	-64	-299	-752	-1 574	-1 233
Balance of payments (- = surplus)	-23	-15	24	33	14	-37	-298	36	-12	-88	-408	497	321
Gross int. reserves a/	120	175	155	126	111	167	336	424	484	568	968	467	330
Memorandum items (rates of growth)													
1. Exports goods and services													
Current dollars	15.3	1.1	17.6	-2.8	13.0	5.1	16.6	-13.1	8.4	16.6	36.9	-8.3	3.4
1970 dollars	9.7	-2.8	2.4	1.5	11.1	-4.2	4.4	-8.7	7.9	-14.6	-3.2	-6.9	4.9
2. Imports goods and services													
Current dollars	13.6	23.0	22.4	1.4	-13.3	-1.5	8.5	4.2	9.0	34.6	64.6	24.4	-13.5
1970 dollars	12.2	9.1	17.7	2.5	-13.2	-1.6	5.5	0.2	2.4	19.6	32.7	11.4	-16.1
3. Terms of trade index (goods)	4.0	-11.2	11.1	-2.2	2.2	11.5	10.7	-9.4	-7.4	24.8	18.3	-15.1	-3.5
As percentage of GNP (current prices)													
4. Exports of goods and services	22.3	18.0	17.8	17.3	20.8	19.4	19.7	15.6	15.1	14.5	15.9	12.4	13.0
5. Imports of goods and services	20.9	19.7	20.3	20.5	18.9	16.6	15.6	14.8	14.5	16.0	21.1	22.3	19.6
6. Current account	-0.7	-3.7	-4.8	-6.0	-1.1	-0.5	2.3	-1.0	-0.8	-3.2	-6.5	-11.6	-9.2

Sources: CEPAL, on the basis of official data.

a/ IFF, International Financial Statistics, May 1978.

President ran on a platform that included a promise to resolve the dispute with the IPC,<sup>18/</sup> a promise that remained frustrated throughout his 5 years in office and ultimately contributed to a change in government. As will be seen soon, the issue of foreign investment eventually reached a peak in 1968, bringing about a radical change in relations with foreign capital.

Turning to 1966, there were more indications of deterioration in the financial situation.

In this year current expenditure growth continued to outstrip the generation of revenues, with a consequent sharp reduction in public savings (see table 3.2). Furthermore, the fiscal gap proved more difficult to finance, so that once again authorities returned to the Central Bank for assistance.<sup>19/</sup> Another major source of finance continued to be loans contracted abroad on relatively short terms.

The balance of payments also was under more pressure in 1966, notwithstanding a marked improvement in exports and the terms of trade. With imports continuing their rapid pace of growth, and an increasing proportion of exports receipts being drained away by profit remittances, the current account deficit rose by about 55%. This year, and unlike 1965, the deficit could only be partially financed abroad so that there was an 11% decline in gross international reserves (see table 3.3).

Few remedial measures were taken in 1966 to stem the tide as apparently the general public saw reasons to be optimistic about the government's economic and political prospects.<sup>20/</sup> About the only outward signs of concern was an intensification of the debate over tax reform and the renewal of an IMF stand by agreement for \$37.5 million in March. But perhaps as a sign of the general level of confidence, the credit - which would have been a first tranche - was not drawn upon during the year.

B. 1967-1968: A Financial Crisis

By 1967 there finally was a general awareness of a difficult situation. Concern was growing about the viability of the exchange rate, which had been stable since 1959. The fiscal situation by now was clearly grave, with public savings all but disappearing (see table 3.2) and financing becoming ever more difficult to realize. The balance of payments was in severe disarray; export earnings actually declined and the current account deficit was at record proportions and in deep need of finance (see table 3.3).

The government, facing a large fiscal gap, continued to do battle with Congress over tax reform, but to little avail. Import tariffs were increased early in the year; and while having little revenue effect, they did help to slow down imports.<sup>21/</sup> Budget financing was satisfied largely through emergency short term commercial loans.

In August, the government negotiated a new 42.5 million standby accord with the IMF. Being a first tranche credit, conditions were relatively moderate. Key elements of the agreement were expenditure cuts and restrictions on new debt with a maturity of less than 5 years.<sup>22/</sup> This latter measure was introduced because of what was seen to be the haphazard and uncoordinated nature of borrowing by government agencies,<sup>23/</sup> most of whom took ample recourse to commercial credit on relatively onerous terms.

The IMF accord was complemented by additional medium term commercial credit. Nevertheless, the overvalued exchange rate could not be supported (see table 3.4). The government, retreating from an adamant position taken earlier in the year against devaluation,<sup>24/</sup> had to make the unpopular decision to adjust

Table 3.4

PERU: APPARENT INTERNATIONAL PURCHASING POWER OF THE SOL

(1964 = 100)

Year	Soles per dollar	Index of exchange rate	Index of internal prices, Peru a/	Index of internal prices, United States b/	Index of parity 3/4	Relation of exchange rate to parity 2/5
	(1)	(2)	(3)	(4)	(5)	(6)
1964	26.8	100.0	100.0	100.0	100.0	100.0
1965	26.8	100.0	113.4	102.0	111.2	89.9
1966	26.8	100.0	127.3	105.5	120.7	82.9
1967	30.7	114.6	142.7	105.7	135.0	84.9
1968	38.7	144.4	168.2	108.3	155.3	93.0
1969	38.7	144.4	181.4	112.6	161.1	89.6
1970	38.7	144.4	193.4	116.6	165.9	87.0
1971	38.7	144.4	200.8	120.5	166.6	86.7
1972	38.7	144.4	210.8	125.9	167.4	86.3
1973	38.7	144.4	241.7	142.9	169.1	85.4
1974	38.7	144.4	281.8	169.1	166.6	86.7
1975	40.8	152.2	338.5	184.8	183.2	83.1
1976	57.5	214.6	455.2	193.3	235.5	91.1
1977	83.8	312.7	634.9	205.1	309.6	101.0

Source: Derived from data of CEPAL and I.M.F., International Financial Statistics, May 1978.

Note: This is a very rough and ready index which should be used only as an approximation of trends. The United States is Peru's major trading partner and its wholesale price index is used as a proxy for international prices.

a/ GDP deflator.

b/ Wholesale price index.

the Sol by 44% on September 1. Notwithstanding the devaluation and additional credit, the year ended with the public sector still in a precarious financial situation and international reserves down to the equivalent of less than one and one-half months' imports (see again table 3.3).

In 1968 problems once again intensified, complicated by what now was becoming a debt service problem on the numerous foreign loans contracted in earlier years (see table 3.5).<sup>25/</sup> The first half of the year was spent largely trying to convince Congress about the need for a tax reform. Meanwhile, economic growth slowed, inflation intensified and the internal and external finances were in chaos. Finally, in June 1968, Congress gave the President extraordinary powers (Emergency Law 17044), for a period of 60 days, to tackle the crisis. New tax measures were quickly introduced, bringing immediate revenue gains. Further budget cuts were undertaken. In order to counteract increasing foreign control of the banking system, local banks had to convert into two-thirds national ownership. External problems were confronted with a new IMF standby credit for 75 million dollars that was negotiated in September 1968. Under the standby agreement new debt was restricted; no loans were to be contracted with maturities between 181 days and 10 years and specified semi-annual limits were placed on loans with maturities between 10 and 15 years.<sup>26/</sup> Armed with the IMF credit, authorities also managed to arrange rescheduling/  
refinance accords with major foreign creditors.

The new measures brought desired results, but they came too late to save the government. Facing growing unpopularity over its economic policy, and embroiled in a scandal over its proposed settlement of the IPC dispute,<sup>27/</sup> the administration fell victim to a restless military who took over power in the name of a revolutionary government on October 3, 1968.

Table 3.5  
 PERU: EXTERNAL PUBLIC DEBT<sup>a/</sup>  
 (millions of dollars)

	Average 1960-1964	1965	1966	1967	1968	1969 <sup>b/</sup>	1970	1971	1972	1973	1974	1975	1976
Disbursed debt	218	385	535	635	744	875	945	997	1 121	1 491	2 182	3 066	3 641
Debt service	4.4	52	89	98	146	135	167	213	219	433	456	474	533
Amortization	37	37	68	66	103	89	121	156	164	352	338	283	299
Interest	7	15	21	32	43	46	46	57	55	81	118	191	234
<u>Memorandum items</u>													
1. Disbursed debt as percentage of GDP	7.9	9.0	10.5	12.4	15.5	16.2	15.2	14.6	14.7	16.1	18.9	22.5	27.2
2. Debt service as percentage of exports	7.2	6.7	9.8	11.1	14.6	12.9	13.6	20.0	19.0	32.2	24.8	28.1	30.5

Source: 1960-1968: Banco Interamericano de Desarrollo Deuda Pública Externa de los Países de América Latina, Washington, 1978; 1969-1976: CEPAL on the basis of official data.

<sup>a/</sup> Public and publically-guaranteed debt with a maturity of more than 1 year.

<sup>b/</sup> Data from 1969 onward are from a **different** source and therefore are not directly comparable with the earlier years.



C. 1969-1974: Consolidation of the Revolution

The new government declared itself dedicated to transforming an economy which was in chaos and under the control of powerful national and foreign groups.<sup>28/</sup> Its basic intentions were to reduce dependence upon foreign capital, carry through a radical land reform, and achieve a rapid rate of economic development based on export-led industrialization.<sup>29/</sup> The transformation was to take place "without chaos and without death",<sup>30/</sup> while the investment required for the restructuring of the economy was to come basically from internal as opposed to external resources.<sup>31/</sup>

1. Stabilization of the economy and subsequent expansion of investment

Given the precarious state of national finance, coupled with initially formal restrictions on foreign borrowing, the new government/had little choice but to maintain stabilization efforts. In mid-October 1968, the authorities informed the IMF that they were disposed to "continue and strengthen" the program under the new standby credit that was arranged in September by the previous government.

The stabilization effort continued through 1969-1970 and into 1971. During these years fiscal policy was orthodox, if not conservative. For 1969-1970 the current savings of the budget turned strongly positive (an average of 77% of capital expenditures), reflecting largely the effect of the full impact of the fiscal measures introduced in mid-1968. Meanwhile, investment expenditures by the public sector were

restrained (see table 3.6) even in the face of depressed private sector investment. These factors reflected themselves in a narrowing of the fiscal gap. Moreover, financing of the deficit was done principally through the use of domestic financial instruments; recourse to Central Bank financing was carefully avoided and there was little new external borrowing.<sup>32/</sup>

The balance of payments also showed remarkable improvement in this period. Reduced import requirements in 1969 and favorable world commodity prices in 1970 caused the current account to move close to balance in the former year and actually turn to a large surplus in the latter. Despite net outflows on the foreign investment account, the overall balance of payments was in surplus in both years, aided in 1970 by the legislated repatriation of foreign assets by residents to the tune of nearly 200 millions dollars. By the end of 1970 reserves had risen to 4 months' imports requirements (see table 3.3).

The stronger balance of payments position was fundamentally aided by some major refinancing of the external debt. In London in September 1968, the former civilian government had negotiated a formal multilateral refinance package of \$180 million, providing relief for 1968 and 1969.<sup>33/</sup> With large payments falling due in 1970 and 1971, foreign creditors were approached for another refinance operation in Brussels in November 1969, this time for \$90 million and covering 75% of the debt service payments scheduled for the next 2 years.<sup>34/</sup> It is significant to note that at the time the government made every effort to maintain cordial relations with the IMF,<sup>35/</sup> whose goodwill, as will be seen clearly in later chapters, was crucial to the arrangement of the refinance accords.

It is important to note that the government's stabilization efforts in the period were not accompanied by drastic reductions in economic growth. As can be seen in table 3.1, the regime reduced inflation and balanced the internal and external accounts, all while maintaining very respectable

Table 3.6  
PERU: PUBLIC SECTOR CAPITAL FORMATION AND FINANCE

Year	Fixed investment <sup>a/</sup>			Investment as percentage of GNP	Percentage financed internally	Percentage financed externally
	Central government	Public firms	Total			
Sales at 1970 prices (billions)						
1965	4.8	5.7	10.5	5.5	...	...
1966	6.3	6.4	12.6	6.2	...	...
1967	4.7	3.6	8.3	4.0	...	...
1968	3.5	4.1	7.7	3.6	56.5	43.5
1969	4.0	4.1	8.1	3.7	54.0	46.0
1970	6.4	4.5	10.9	4.6	64.6	35.4
1971	7.7	4.5	12.2	4.9	76.6	23.4
1972	8.2	5.3	13.4	5.1	77.8	22.1
1973	6.8	6.6	13.4	4.8	71.2	28.8
1974	9.0	14.6	23.5	7.7	53.2	46.8
1975	9.8	19.1	28.9	9.2	56.0	44.0
1976	9.5	17.8	27.3	8.4	59.6	40.4

Sources: Investment and GNP figures are from Cabieses and Otero, pp. 209 and 220 and are not directly comparable with data in table 1. Data for 1976 are estimated on the basis of data from the BCR (1976). Finance data are from the MEF.

<sup>a/</sup> May not sum properly due to rounding

By 1971 the revolutionary government had implemented most of its basic reforms (to be discussed momentarily) and its interests turned from stabilization to investment and industrialization. The government planned to raise the global investment coefficient from roughly 13% in 1970 to over 21% by 1975.<sup>36/</sup> Moreover, in contrast to the past, the State was to become a dominant factor in investment, with the programmed rate of growth for 1970-1975 being an average of 32% per annum in real terms, compared to less than 10% for the private sector; the governments' share of gross internal investment was to rise from 36% in 1970, to roughly 58% by 1975.<sup>37/</sup> Significantly, the nature of investment also would undergo radical change, as the State was to give a secondary role to its traditional area of responsibility, i.e., infrastructure, in favor of a new strategy, involving heavy investments in mining and manufacturing.<sup>38/</sup>

The nature of the industrialization program was not unsimilar to that of the previous government. Growth was to be stimulated by substitution of imports. In support of the strategy, tariff levels remained high, reinforced by the introduction of quotas, or absolute bans, on the import of products produced locally. While the State was in charge of most of the investment, the government nevertheless tried to stimulate private investment in industry through very liberal tax incentives and the attraction of a protected market.

Implementation of the plan saw government capital outlays in 1972 rise in real terms above the peak level achieved in 1966. But the investment program really did not take off until 1974 when investment expenditure nearly doubled the 1966 figures (see table 3.6). Overall, the public sector investment coefficient rose from 4.6% in 1970 to 7.7% in 1974,<sup>39/</sup> with a very high percentage being devoted to large projects in mining, oil exploration and intermediate goods manufacturing.<sup>40/</sup> Significantly, until 1974, external sources played a significantly smaller role in the finance of investment (see again / table 3.6), which was in keeping with earlier declarations of the government. At the same time, current outlays of the central government rose

rapidly (see table 3.2), with subsidies<sup>41/</sup> and interest payments growing in significance. The spectacular growth of the public sector that was brought on by this program reflects itself in the fact that by the end of 1974 the government was approaching control of roughly one-third of output and two-fifths of employment in the modern sector, one-half of all fixed capital formation, two-thirds of credit (excluding government finance) and nine-tenths of exports and one-half of imports.<sup>42/</sup>

The enormous expansion of the State in the economy during this period was contrasted by its relatively weak resources base. According to Fitzgerald, Peru's fiscal effort was not one of the more impressive ones in Latin America as a result of heavy tax exemptions for industrial promotion, frustration of tariff revenue through import controls on durable goods, and an unwillingness to irritate perceived areas of political support through tax reform.<sup>43/</sup> Indeed, the ability of the Central government to capture revenue actually declined steadily after 1970 with the concomitant erosion of government savings and considerable expansion of the overall deficit (see table 3.2).

The scarcity of resources was compounded by the fact that State enterprises - by 1974 carrying out the bulk of investment activity (see table 3.6) - were unable to generate savings because of the very long gestation period of their projects and/or policies of subsidized pricing.<sup>44/</sup>  
of late 1973  
After the oil crisis/the latter problem became severe as State prices were amply used to offset the effects of the higher external costs of food and petroleum.<sup>45/</sup>

Despite the resource bottleneck, the public sector had no difficulty financing its expenditures. The State, taking advantage of its greater control of domestic credit, took heavy recourse to internal credit and around 1972 foreign borrowing began to take on a higher profile as well.<sup>46/</sup> It also should be mentioned that around 1973 primary emissions of the Central Bank once again became a significant source of finance, and this eventually fueled inflation (see again table 3.1).

In 1971-1972, the balance of payments remained reasonably sound, in the former year because of continued restrictions on imports (which in both current and constant terms were still below the peak level of 1967) and in the latter because capital flows began to recover due to new foreign investment in mining and oil exploration as well as renewed recourse to foreign credit markets. As the investment program took off, and internal consumption expanded, imports began to accelerate, as reflected in a noticeable widening of the current account deficit in 1973. Rising consumption and investment, coupled with higher prices for food imports (which traditionally are of considerable volume) and petroleum, as well as a progressively overvalued Sol (see again table 3.4), caused foreign purchases to rise by nearly 65% in 1974. With factor payments also rising sharply, the current account deficit more than doubled, to represent roughly 40% of export earnings (see table 3.3). The disequilibrium in the current account was, however, totally masked by large inflows of foreign capital which generated an overall balance of payments surplus and permitted international reserves to reach record levels. The State, through foreign borrowing, accounted for most of these capital flows. Likewise the burden of external public debt was by now very significant (see table 3.5).

2. The reforms

As noted in previous paragraphs, the new revolutionary government was preoccupied with reforms in the years 1969-1974. Some of these reforms had a significant impact on the demand for foreign finance and on relations with foreign capital. The purpose of this section is not a comprehensive analysis of any or all of the reforms introduced by the government, but rather a summary of those measures that had some importance to the demand for foreign resources and/or could have conditioned the attitudes of foreign suppliers of finance. In this examination, special attention is given to reforms in the institutional control of foreign borrowing and the role of foreign capital, since these two measures had in their own way a very direct impact on the demand for foreign resources. As will be seen in chapter 4, the latter reform also had a profound impact on the supply of the external finance.



a) Agrarian reform

One of the basic and most far-reaching reforms was that applied to agriculture. Land reform had been a hot political issue throughout the 50's and 60's, with peasant frustrations ever increasing due to ineffectual reform programs.<sup>47/</sup> To diffuse peasant unrest and overcome a long history of near-stagnant agricultural output,<sup>48/</sup> the government in 1969 decreed a new land reform law. Almost immediately the country's coastal estates and large livestock operations in the Sierra were expropriated. All together, by the end of 1975 over 7 million hectares had been expropriated, 6 million hectares adjudicated, involving nearly 10,000 ranches and affecting 250,000 families.<sup>49/</sup> While the reform radically changed the pattern of ownership in the sector, it had little impact on production; although output did not fall below historical trends, it did not rise either, so that a high demand for food imports continued to weigh heavily on the balance of payments throughout the period.<sup>50/</sup>

b) Labor communities

In 1970, under a new industrial law, the government established what it termed industrial communities. Under this new regime a private industrial entity with 6 or more employees (or in cases where there were less than 6 employees, income greater than one million soles) had to provide 25% of its pre-tax profits to a workers' industrial community, 10% in the form of currency and 15% in shares of the firm. There were similar, but modified arrangements, for the mineral and fishing sectors.<sup>51/</sup>

The reform enabled workers to participate in profits, but more importantly, theoretically over some time they also could eventually gain control of the enterprise itself. (From the outset

they had a representative on the board of the firm). By mid-1974 some 3.700 firms in the industrial sectors had established an industrial community, covering around 245.000 workers.<sup>52/</sup>

The communities, while well-intentioned, undoubtedly had some undesirable side-effects. One was that given the industrial structure of Peru, 62% of the industrial work force (as opposed to only 40% of value-added) was not incorporated into the community concept.<sup>53/</sup> Another, which is more directly related to the focus of this study, is that owners of enterprises saw new investment as a way of postponing indefinitely the day in which workers could actually gain control of the firm. Thus incentive was given to new investment, and therefore imports, regardless of whether there was a real need for new capacity.

c) Institutional reforms

Right after the change in government in 1968, a series of institutional reforms were adopted, making a reorganized Ministry of Finance the focus of power for fiscal and monetary policy.<sup>54/</sup> The reforms themselves were quite comprehensive and therefore cannot be analyzed in any detail here;<sup>55/</sup> one can however, attempt to highlight those actions which had an impact on the demand for external finance.

First, in 1970, the government instituted full foreign exchange controls. These were complemented by the creation of new institutions to regulate exchange; the Consejo de Transacciones Externas del Sector Público (COTREX) was instituted to control the foreign exchange outlays of the State, while the Junta de Transacciones Externas del Sector Privado (JUTREX) was organized to elaborate an annual foreign exchange budget for the private sector, based on applications submitted by individual entities.<sup>56/</sup>

The government also was concerned about the casual nature of debt contraction in the 60's, such that it took steps to centralize control over borrowing activities. In 1969 the Comisión Permanente de Crédito Externo (Peruvian Commission on External Credit) - presided over by the Director General of Public Debt (an office in the Ministry of Finance) and made up of general managers of the BCR, BN, INP and the Coordinator of the Secretariat of the Annual Economic Plan - was created to formulate overall debt policy and approve all foreign credit operations of the State. 57/

The actual process of approval for credits was quite complicated and involved a multitude of government agencies. For instance, by 1970 project finance had to be approved by the Council of Ministers, be given a sectoral priority by the INP, meet with the approval of the Comisión Permanente de Crédito Externo, have its terms scrutinized and registered with the Directorate General of Public Debt, and be reviewed by the Counsel General and Controller General of the Ministry of Finance. Each approved credit also was accompanied by a Supreme Decree. 58/

Given the diverse levels of control over debt, it was decided in 1972 to establish the Comité Superior de Deuda Externa (Superior Committee on External Debt), headed by the Minister of Finance and incorporating the Chief of the INP, the Director General of Public Debt and the Presidents of the BN, BCR and COFIDE. Its task was to coordinate the various offices in the debt control system in order to insure that general guidelines on debt contraction were being followed; it also was responsible for authorizing an agency to initiate negotiations for foreign credit. 59/

In 1972 another major innovation in the debt control system was introduced, i.e., the centralization of credit negotiations. The BN became the bargaining agent of the Central Government and also assumed responsibility for the short term financial needs of State enterprises. Meanwhile, COFIDE was created to handle the medium/long term credit needs of public enterprises (and under certain circumstances that of private and quasi-private enterprises as well).<sup>60/</sup> Significantly, in late 1973 the control system for credit authorizations through both institutions was streamlined in order to increase the flow of finance for programmed investment.<sup>61/</sup>

How did the debt control system affect the demand for foreign credits? As Ugarteche points out in his study on the institutional control of foreign borrowing, the centralization of credit negotiations in the BN and COFIDE was an improvement over the old system whereby each public entity was basically on its own with regard to foreign credit agreements.<sup>62/</sup> These two agencies, and especially COFIDE, had staffs capable of enhancing the credibility of finance proposals and negotiating with creditors with a view to international market conditions (COFIDE maintains files on creditors). No doubt better terms were secured as a result of this system. However, the system apparently was not an effective filter for several reasons.

First, according to Ugarteche, while the planning institute continuously showed concern about debt service and management, there were no precise parameters or guidelines established on how much debt should actually be contracted and under what conditions ; nor, apparently, were precise policy/<sup>guide</sup>lines ever laid down by the

Comisión Permanente de Crédito Externo. <sup>63/</sup>

Second, the fact that there were no explicit debt guidelines established meant the project approval was carried out without any overall constraint on foreign finance which, as Fitzgerald observes, was permissive to designers "who want the 'best' equipment and rapid delivery" and who "tend to favor foreign suppliers". <sup>64/</sup> This was aggravated by the fact that planners themselves saw projects as a means of borrowing foreign exchange in general, thereby releasing indigenous resources for other purposes. <sup>65/</sup> The situation led to what Fitzgerald terms as a "haphazard" accumulation of debt. <sup>66/</sup>

Third, the system of project selection itself, was prone to outside pressures and ministerial rivalries. As Fitzgerald notes:

"... major projects tend to accumulate their own 'pressure groups' among the beneficiaries and also within the ~~administration, so that once underway to the feasibility stage they are very difficult to stop or modify.~~ In administrative terms, the problem is felt to lie in the fact that the projects reach the INP 'too late in life' and are difficult to stop, or where they blatantly fail to conform to development objectives, to reformulate without rejection". <sup>67/</sup>

Fourth, in practice these same pressures came into play when applications for foreign credit were being considered. With regard to the approval process Ugarteche concludes:

"Usually the pressures of Ministers for approval of projects in their ministerial portfolio resulted in the Superior Committee (of External Debt) only approving what was proposed. It is an ex-post approval of an agreement made previously by the Council of Ministers." <sup>68/</sup>

Moreover, Ugarteche points out that an inverted hierarchical relationship between the Comisión Superior de la Deuda Externa and the Comité Permanente de Crédito Externo did not help matters. The former, composed by ministers, provided the go-ahead to initiate

contacts for external credit, while that latter, composed of general managers of ministries, had to consider the appropriateness of the amounts and terms offered. Unfortunately, the members of the Comité were of insufficient rank to resist the pressures generated from the Ministers. 69/

From the above one can conclude that the reform generated the infrastructure to regulate the demand for foreign credit, but credit proposals were nevertheless able to fully penetrate the screen of control because of a lack of definition in financial policy and inadequate instruments to counteract the momentum generated by an ambitious development program. It was not until 1978 that most of these deficiencies were remedied. 70/

d) Reform of foreign capital

As was seen earlier Peru traditionally had geared its economic policy to the attraction of foreign investment. The strategy worked with great success, as the profile of foreign capital was indeed very high. By 1968 three-quarters of the mining sector, two-thirds of the sugar industry, half of the fishing and cotton and wool processing were under foreign control,<sup>71/</sup> not to mention roughly 60% of the banking system's resources and credit.<sup>72/</sup> Expatriate capital also had one-third of manufacturing (two-thirds of the 200 largest firms),<sup>73/</sup> and control of dominant enterprises in communications, power generation and trade.<sup>74/</sup> The exposure of the United States was particularly high, as its national firms accounted for over 80% of all direct foreign investment.<sup>75/</sup>

The new military regime was very concerned by what it saw to be excessive foreign control of the economy and therefore took steps that sharply altered the view on foreign capital. In some cases the role of foreign investment was modified directly, and in others it was changed indirectly as part of broader reforms. It is important that these changes be reviewed in some detail for several reasons. First, the change in "demand" for foreign investment altered not only investment flows, but also had repercussions on the whole nature of external finance. Second, treatment of foreign investment is theoretically an important factor in banks' evaluation of creditworthiness.<sup>76/</sup> Third, commercial banks - some of them important actors in this study - were both directly and indirectly caught up in the reform measures.

Not surprisingly, the first major action taken by the authorities was on the IPC. On October 9, 1969, 6 days after its installation in power, the government expropriated the IPC's oil fields and refinery in Talara. Later, in early 1969, it took over all other company assets, including its gasoline marketing network. Furthermore, no compensation was to be paid because of an alleged debt of nearly \$700 million dollars owed by the Company to Peru for oil extracted from the Talara fields over the previous 40-odd years.<sup>77/</sup> Meanwhile, the expropriated assets were turned over to the State petroleum entity which was reorganized and renamed PETROPERU.

It should be pointed out that in taking over the IPC's assets, authorities were quick to add that the action should not be construed as a general attack on foreign capital or private property, and <sup>that</sup> the government would support foreign investment which subjected itself to national laws and interests.<sup>78/</sup>

In 1969 the government displayed its rather unique view of foreign investment by actions taken in the mining sector. The sector was a United States enclave with U.S. firms - Cerro de Pasco, Southern Peru Copper Corp. and Marcona Mines being most important - controlling over 80% of the value of production. Meanwhile national interests controlled only 16% of output.<sup>79/</sup> In September it was decreed that mining concessions held by private corporations must be exploited or revert to the State. After waiting for proposals, early the next year 8 major concessions were taken over; Cerro de Pasco lost four concessions (including Tintaya); Anaconda, two (including Cerro Verde); American



Smelting, two (including Michiquillay) and Kaiser Aluminum, Charter Consolidated and NATOMAS one each.<sup>80/</sup> Also at the end of 1969 the government announced that the State would nationalize all marketing and refining of mineral products,<sup>81/</sup> which were later to be put in the hands of a new public enterprise called MINEROPERU. Simultaneously it signed a contract with Southern Peru for exploitation of the large Cujajone copper deposits,<sup>82/</sup> thereby giving a concrete example that Peru was still interested in foreign capital.

Another firm affected by reforms in 1969 was W.R. Grace. Having widespread holdings in Peru, it lost its two big sugar plantations (and refineries) as a result of the Agrarian Reform.<sup>83/</sup> As a reaction to the move, Grace took steps to divest itself of its operations. In the same year, ITT lost its local telephone company,<sup>84/</sup> and Peru enforced its sovereign control over maritime resources within 200 miles of the coast.

In 1970 a law was issued implementing Decision 24 of the Cartagena Agreement, which, among other things, placed limits on profit remittances by foreign firms. Also, in an attempt to rationalize the automobile industry, General Motors and Ford had their production licenses revoked in favor of new concessions to Japanese and European bidders.<sup>85/</sup>

further

It was in this year that Peru introduced / reform of the financial sector.<sup>86/</sup> Branches of foreign banks, which at this time were Citibank, Bank of America, Lloyds BOLSA, and Bank of Tokyo (Royal Bank of Canada had recently closed its office), were allowed to remain in Peru under restricted conditions; there was a minimum capital base, no time or

savings deposits were permitted and special lines of credit in foreign currency had to be made available to the government.<sup>87/</sup> Furthermore, foreigners were not allowed to own local banks or insurance companies; those who already had subsidiaries had to reduce their participation to below 20%.<sup>88/</sup> As a result of the law

Chase Manhattan decided to sell its 51% ownership in Banco Continental to the government. Meanwhile, Banca Commerciale Italiana had its participation (through the subsidiary SUDAMERIS) in the Banco de Credito reduced to below 20%. Likewise, Credit Lyonnaise had to reduce its participation in the Banco de Lima to conform with the new rule. Finally, the financially troubled Banco Internacional, of which Chemical Bank was a major shareholder, was taken over by the government.

In 1973, the government nationalized the fishing industry, financially troubled because of the disappearance of the anchovy. While the industry as a whole was largely national<sup>89/</sup>, a number of foreign firms, especially of U.S. origin (Ralston Purina, H.J. Heinz, CARGILL, GRACE) were affected. Also at the end of 1973, Cerro de Pasco, which had its cattle ranches expropriated in 1969, was subject to a complete nationalization. This had far reaching implications, because Cerro, in addition to having the largest mining operations,<sup>90/</sup> had interests in many other sectors of the economy.<sup>91/</sup>

In most cases the reforms were met by indignation on the part of foreign firms. Amicable agreements, however, were in some instances worked out relatively quickly, as is the case of ITT.<sup>92/</sup> Chase Manhattan

received a highly favorable settlement<sup>93/</sup> and also benefited from the Cuajone agreement, a project for which it was to be lead financier. On the other hand, compensation for IPC, GRACE, Cerro and some of the fishing firms were subjects of hot and long debate on which neither party could reach agreement. By mid-1973 the United States government was interested in clearing up all outstanding claims as soon as possible and therefore appointed James Green, a senior Vice President at Manufacturers Hanover Trust, as a special negotiator. By February 1974, a package deal was agreed to, involving: (a) payments to the United States Treasury of 76 million dollars, which would then be distributed to companies with claims by the United States State Department, and (b) the release of \$74 million in blocked company assets.<sup>94/</sup> Also implicit in the agreement was a large syndicated bank credit to the government of Peru, an operation which will be analysed in greater detail in chapter 5.

The examination of foreign capital reforms should not end without mentioning that aside from direct actions taken on capital of international banks, these institutions were also indirectly affected through their links with non-financial corporations <sup>that</sup> / were nationalized or Peruvianized. These links varied from ownership of stock of the company to interlocking directorates and extensive lending and deposit business with the parent or subsidiary. Table A 3.1 of the statistical appendix displays links between major banks and some of the foreign firms affected by the program of nationalizations.

3. The discovery of petroleum in the Amazon

Special attention has been given to this event because it was perhaps one of the most decisive factors in the response of both the demand and supply sides of external finance for Peru. The general highlights will be presented here, with later chapters analyzing its impact on bank lending.

When Peru nationalized the Talara oil fields, it faced a problem of deteriorating national petroleum production. Policy makers found that national output was at only about 70,000 B/D, with another 30,000 B/D being imported to cover requirements of local consumption. Nor were prospects good; this country, which was once self-sufficient in petroleum, faced the likelihood of national requirements reaching 180,000 by 1980.<sup>95/</sup>

Impressed by Texaco-Gulf's discovery of large deposits of petroleum in an Amazon region of Ecuador that was near the Peruvian border, officials immediately took steps to explore for similar possibilities in jungle territory which was basically adjacent to Ecuador's fields. In 1970 geological work was undertaken. Peru then invited foreign firms to join PETROPERU in the search, but under rather restrictive conditions for the time; instead of paying royalties or taxes, firms would have to explore at their own risk and any petroleum discovered would be split 50-50 with PETROPERU.<sup>96/</sup>

The first firm to accept these conditions, then termed the "Peruvian Model", was Occidental Petroleum, a maverick corporation, under the direction of Mr. Armand Hammer, that was known for dealing with governments that the 7 sisters thought wiser to avoid. Contracts were signed in June 1971.

By late 1971 PETROPERU's and Occidental's operations were fully underway and in November a well in the Trompeteros region struck oil at 2.000 B/D. Then another well was dug in the CAPIRONA region with similar success. A third was initiated at PAVAYACU and it too produced oil.<sup>97/</sup>

The results were truly promising; the traditional average ratio of success is 10 wells to one discovery while Peru was finding oil at a ratio of 1:1.<sup>98/</sup> Not surprisingly, euphoria broke out in Peru. By early 1972 papers were headlining articles to the effect that Peru had immense reserves equal to production in the United States of Russia.<sup>99/</sup> Petroleum officials expressed that the jungle "was floating on a sea of petroleum".<sup>100/</sup> Moreover, self sufficiency was forecast for late 1975 and export potential seemed bright; indeed a foreign geologist under contract to Petroperú went so far as to predict production of 10 million barrels a day by 1980.<sup>101/</sup>

After the initial finds, foreign petroleum firms, notwithstanding the stringent terms of the "Peruvian Model" contract, entered the jungle in droves. By 1974 16 foreign petroleum companies had signed contracts.<sup>102/</sup> Meanwhile, the United States consulting firms Scientific Software Corp. and De Golyer and Mac Naughton had estimated recoverable reserves at 547 million barrels in 1974.<sup>103/</sup>

By 1974 Peru had already formulated plans to transport the jungle petroleum to the coast via a 200.000 B/D transandean pipeline. Feasibility studies had been prepared by the Bechtel Group (at a cost of 700 thousand dollars) and a complex financing package (analysed in chapter 8), in which banks participated, was arranged by mid-year. When the pipeline was originally conceived in the early 70's, costs were estimated at 350 million dollars. However, escalations caused the actual price to prove to be nearly 800 million dollars.

D. 1975-1976: Crisis anew

In the last two years covered by this study, Peru once again enters into crisis, a crisis that perhaps was even graver than the one experienced in 1967-1968.

By 1975 the economic situation was showing open signs of strain. A deep recession in the Center was playing havoc on Peruvian exports, which had already been severely hurt by the disappearance of the anchovy and sluggish volume in mining. The adverse situation reflected itself in an absolute fall in both the unit price and volume of/ exports this year, further aggravating the long term decline in the export coefficient, which by this time had dropped to a level that was only somewhat more than half of the average for 1960-64 (see table 3.3). Meanwhile, imports, fueled by higher petroleum prices, the investment program, an overvalued exchange rate and subsidies on food, and oil, continued to grow rapidly. Coupled with a large deficit on non-factor services, the net effect of trends was an enormous rise in the current account deficit, which could not be covered by capital inflows, abundant as they were. Again, the State was a major conduit for capital flows via foreign borrowing, much of which was used simply to offset the substantial outgoing payments related to its heavy service of foreign debt (see table 3.5). The shortfall in finance caused gross international reserves to fall from nearly one billion dollars in 1974 to less than 500 million dollars in 1975, which was insufficient to cover 2 month's imports.

The central government's financial situation remained very precarious as well, with fiscal effort falling to one of its lowest points in recent history (see again table 3.2). At the same time, public enterprises continued to run large deficits. 104/ The financial gap had to be closed via heavy foreign borrowing, internal credit,

and primary Central Bank emissions. It is worth noting as well that in the midst of these problems the government took the surprise move of nationalizing Marcona Mines.

In August 1975 there was new leadership in the government. Aside from some price adjustments , however, economic corrective measures were not undertaken until late in the year. In September a new economic team was formed. This was quickly followed by a 16% devaluation, the first adjustment of the exchange rate in 8 years (see table 3.4).

The slowness of adjustment was perhaps attributable to the confidence that financial problems would be rectified by upcoming petroleum exports. However, by the end of 1975 even this prospect was turning dim. Just as the transandean oil pipeline was reaching 46% of completion, 10 of the foreign firms in the jungle terminated operations either due to dry holes or the finding of uncommercial deposits. 105/

The crisis deepened in 1976. In a historic multi-houred speech to the public in January 1976, the Minister of Finance clearly defined the nature of the crisis and introduced measures to reduce the cost of fiscal subsidies, raise revenues and close the external gap. 106/ This was followed up in June by a comprehensive stabilization program that, uniquely, did not involve the IMF.

Notwithstanding stabilization efforts, the banking case study closes with the economy in continued crisis; high inflation, low growth, impressive fiscal and external gaps, a burdensome external debt and a precariously low level of foreign exchange reserves. Furthermore, the prospects of a petroleum boom appeared ever more doubtful as during/year all but one of the remaining foreign oil companies closed down operations in the jungle due to unsuccessful explorations. By the end of 1976 the only foreign operating firm was Occidental Petroleum, which was producing the equivalent of 7.000 barrels a day in its block, along with PetroPeru, which generated another 3.000 barrels a day. By now the oil pipeline was 98% completed, but the immediate prospects were that the two companies would generate petroleum sufficient to barely satisfy half of the formal capacity of 200.000 barrels a day. 107/

In subsequent years, events were to become even more turbulent, but, unfortunately, this later period goes beyond the scope of the study. However, in order to provide continuity, Chapter 9 provides an update that will take the reader up through 1979.

## II. Analytical overview and summary

The previous pages have attempted to provide the reader with a brief account of those events and factors underlying the public sector's demand for external resources during 1965-1976. Given the breadth of the material, it might be useful to view factors of demand for the period as a whole.



One can use new loan commitments as a proxy for the public sector's effective demand - i.e., demand that is met by a full or partial response from the supply side - for external finance. This is done in table 3.7 which displays volume indexes for new loans contracted by the public sector during 1965-1976. Index A represents commitments deflated by an import price index and is therefore best suited for showing trends vis-a-vis the external sector, while index B deflates commitments by an index of local prices, adjusted for the nominal exchange rate, and therefore is best related to domestic finance. 108/

The data clearly show that the public sector made increasing commitments to foreign finance in the periods 1965-1967 and 1972-1976. Curiously, despite the very different orientation of public policy in the two periods, the factors behind demand were quite similar. At the risk of oversimplifying, the commonality of factors is presented below.

#### A. The fiscal dilemma

One factor of demand for foreign resources that pervades most of the period is severe disequilibrium in the fiscal accounts. On the one hand, there were almost continuous pressures to increase government expenditures, with the state taking on ever more importance in the economy. Starting from a low base of expenditure of 16% of GDP in the early 60's, outlays averaged nearly 19% of product in 1965-1967 and near 20% in 1971-1976. These figures are much higher if amortization of debt is included (see again table 3.2). The expanded expenditure in these years is counterposed by a completely flat revenue base that averaged only 15% of product. In 1976, income as a percentage of product actually was lower than in 1965.

Table 3.7

PERU: ANNUAL FOREIGN LOAN COMMITMENTS OF THE PUBLIC SECTOR

(1965 = 100)

	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976
Index A	100	328	147	115	86	128	162	288	471	519	307	442
Index B	100	222	180	117	81	119	144	256	440	509	321	543

Source: Derived from data in IMR, World Debt Tables and CEPAL.

Notes: Index A is an index of annual foreign loan commitments deflated by the index of import prices; index B is an index of annual loan commitments deflated by an index of domestic consumer prices adjusted for movements in the nominal rate of exchange of the Sol with the U.S. dollar.

Thus, one encounters the anomaly whereby the state sharply increased its participation, but did not give itself access to the domestic income needed to support its increased activity. The result, of course, was sizeable fiscal deficits to be financed. The disequilibrium was particularly severe in 1972-1976, when the deficits were consistently in excess of 6.5% of GDP. Only in 1968-1970, a period <sup>relative</sup> of/retrrenchment, was the fiscal situation reasonably balanced.

At least to some extent there were common reasons for fiscal difficulties. As just mentioned, government expenditure tended to expand vigorously, due to real activity, subsidies and inflation. On the other hand revenues were held back by <sup>an</sup>inelastic tax system and a perennial disinclination to raise tax pressure. Moreover, the flat revenue base was aggravated by an inclination to forego income because of desires to provide investment incentives to the private sector. Investment incentives, tariff reductions (and import restrictions in the post-1968 period) all were used extensively to promote industrialization. These same incentives, however, represented considerable foregone fiscal income.

In the years of sizeable deficits, local sources of finance were limited by either an inadequate amount of local savings and/or insufficient instruments for tapping these resources. There was a greater degree of success in using domestic savings after 1968 as the government had considerable control over the domestic financial system. However, except in 1968-1970, when there were reduced financial requirements, the domestic financial system still could not fully support the fiscal deficits.

As will be seen in the next chapter, there was ample access to foreign capital in 1965-1967 and 1972-1976. And, there was little hesitation in either period to use foreign finance to cover fiscal requirements. Central bank emissions also supplemented foreign resources.

Interestingly, both in the 60's and 70's, the government's external debt contraction may have lacked sufficient restraint, because of public sector expansion progressing more rapidly than the managerial skills of public servants. This problem was particularly severe in the 60's. In 1972-1976 there was much more formal control of the borrowing process, but the pressures of a very ambitious investment program, coupled with lack of definition in debt policy, contributed to the formal control system being overridden by other considerations.

In 1968-1971 there was little new foreign borrowing for fiscal purposes as finance requirements were much reduced and efforts were made to employ domestic resources to cover the fiscal gap. But as will be seen in the next chapter, the behavior of the budget and the mode of finance may very well have been related/<sup>in part</sup>to the fact that there was very limited access to foreign finance in these years.

B. The balance of payments dilemma

The balance of payments gap, or course, was not altogether unrelated to the fiscal situation. But there were nevertheless some unique factors at play.

Table 3.8 provides some data that permit one to pinpoint some common characteristics of the balance of payments performance during the period 1965-1976. As can be seen, the period of large

Table 3.8

## PERU: EXTERNAL BALANCE OF PAYMENTS DEFICIT TO BE FINANCED

(Millions of dollars)

	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976
Trade balance	-73	-125	-164	90	155	253	52	50	-139	-601	-1 349	-881
Direct foreign investment (DFI)	-53	-110	-165	-169	-179	-143	-108	-23	-10	16	301	126
Net investment	38	18	-18	-20	6	-70	-58	24	70	58	316	170
Remittances	-91	-128	-147	-149	-185	-73	-50	-47	-80	-42	-15	-44
Total debt service	-76	-68	-129	-232	-215	-252	-306	-318	-468	-529	-661	-989
Interest (net)	-29	-33	-49	-73	-72	-60	-75	-74	-84	-130	-227	-327
Amortization	-47	-35	-80	-159	-143	-192	-231	-244	-384	-399	-434	-662
Total deficit to be financed <sup>a/</sup>	-202	-303	-458	-311	-239	-142	-362	-291	-617	-1 114	-1 709	-1 744
<u>Memorandum items:</u>												
1. Total deficit as percentage of GNP	4.7	5.9	9.0	6.5	4.4	2.3	5.3	3.8	6.6	9.6	12.6	13.0
2. Total debt service and net DFI as percentage of exports	16.7	19.6	33.1	40.1	37.5	32.3	38.9	29.6	35.6	27.9	21.3	49.4

Sources: Derived from data of CEPAL.

<sup>a/</sup> Excludes from consideration short term capital movements and errors and omissions.

finance requirements (as a percent of product) were 1965-1968 and 1973-1976. In both periods a negative trade balance, followed by mounting debt service were prime factors behind a rising need for external finance. In 1965-1968 outflows on the direct foreign investment (DFI) account were even more important than debt service as a source of finance requirements. It also can be seen that in 1969-1972 DFI and debt service were a major burden on the balance of payments, but the trade account made a positive contribution to resource flows, creating less requirements for finance.

Looking first at the trade balance, one can see, by returning to table 3.3, that in periods of deficit there was usually relatively rapid growth of imports. External prices often were a factor behind growth, but in most years volume also was considerable. There were some common factors behind volume growth; stagnant local food production, public and private investment, subsidies on basic consumer items, tax and tariff reductions on capital goods, and very importantly, policies to provide artificial support for prolonged periods to a fixed exchange rate. But, perhaps the most important determinant of the trade deficit was the abissmal performance of exports. Throughout the 12 years there was a secular decline in the export coefficient so that by 1976 export volume, as a percentage of product was only 50% of the average for 1960-1964 (see table 3.9) In some years the erosion of export performance was hidden by favorable prices, but in the end the sluggish volume made the balance of payments very vulnerable. One cannot help but think that if there had been a more dynamic export sector, the crises of 1967-1968 and 1975-1976 might have been manageable.

TABLE 3.9

PERU: EXPENDITURES ON GROSS DOMESTIC PRODUCT, 1965-1976<sup>a/</sup><sup>b/</sup> As a Percentage of GDP in 1970 (local currency prices)

	1960-1964	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976
Consumption	76.5	79.9	79.9	81.0	81.6	82.6	83.0	82.4	82.5	86.2	87.9	89.5	88.1
Private	65.6	67.8	68.6	69.2	69.3	70.5	71.0	70.2	69.9	73.9	75.9	76.3	74.9
Public	10.9	12.1	11.3	11.8	12.3	12.1	12.0	12.2	12.6	12.3	12.0	13.2	13.2
Investment	16.4	16.8	19.5	18.6	13.1	13.0	12.9	15.3	14.5	16.0	19.5	20.8	17.9
(Gross fixed capital formation)	14.1	15.1	16.1	14.6	12.3	12.2	12.4	13.0	13.1	13.0	15.9	18.6	16.7
Exports G and S	23.1	21.0	20.4	20.4	22.5	20.6	19.7	17.2	17.5	14.1	12.7	11.5	11.7
Imports G and S	16.1	17.8	19.8	20.0	17.3	16.2	15.7	14.9	14.4	16.3	20.2	21.8	17.7
Gross domestic product	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: CEPAL on the basis of official data.

a/ At market prices.

b/ Calculated on the basis of unfounded data.

There were some common features behind the lagging export performance.

One factor was the long gestation period of mineral projects, coupled with an uncertain policy on the role of foreign private investment. There was significant new investment in minerals in the late 50's and the coming-on-stream of production helped to boost exports in the early 60's. Any prospects for new private foreign investment in the 60's, however, was dampened by the uncertainty surrounding the revision of the 1950 Mining Code and the renegotiation of the Toquepala contract. No sooner was the contractual problem resolved than a change in government occurred in 1968 with a radically new view on foreign investment being introduced. This further delayed any prospects of foreign investment in minerals. After several years of uncertainty, an agreement was reached for the Southern Peru Copper Corporation (US) to develop the Cuajone deposits and the government undertook the development of Cerro Verde and Michiquillay. But output from Cuajone and Cerro Verde, given lead times, could not come on stream until the latter half of the 1970's (development of Michiquillay had to be postponed indefinitely because of the 1975-1976 crisis).

Another crucial factor in the minerals sector was petroleum. As has been seen, there was great anticipation of oil exports giving massive support to the balance of payments. Undoubtedly, the government formulated its investment program, and the finance of it, on the basis of eventual receipts from the Amazon oil. However,



when an exportable surplus did not materialize as fast as originally expected, a gaping whole was left in the balance of payments.

Another crucial element to the poor export performance was a lack of export vocation in the industrial sector. Theoretically, the import substitution program also could have provided a base for industrial exports. But little attempt was made to encourage efficiency as no-questions-asked protection was provided to industrialists. The fixed exchange also worked against industrial exports. Nor was there really any serious program to promote such exports through instruments, such as subsidies, that would compensate the formal disincentives to selling abroad. 109/

Finally, there were some things out of the government's control. The loss of anchovies was an ecological phenomenon that eroded to a considerable degree the country's ability to generate foreign exchange. Also, it was unlikely that substantially increased output from export agriculture could be realized simultaneously with important agrarian reform measures.

Of course, except in the years of open external crisis the country was able to overcome the export bottleneck through foreign borrowing. But borrowing, along with occasionally buoyant world prices, may have generated a false sense of security with regard to external solvency and have dampened incentive to introduce corrective measures. Moreover, as borrowing accumulated debt itself created a demand for more borrowing to cover debt service payments. This latter demand by definition grew at an exponential rate.

Perhaps the most graphic summary of what happened to Peru is in the national accounts data presented in table 3.9. Here one sees that between 1965 and 1975 consumption rose from 80% to 90% of Gross Domestic Product; investment rose from 17% to 21% and imports rose from 18% to 22% of product. Simultaneously, exports fell from 21% of product to 12%. These somewhat striking trends were feasible of course, only because of massive foreign borrowing.

Footnotes

Chapter 3

1. This has been done well elsewhere. For a historical view covering 1880-1977 see Thorp and Bertram. For short term trends consult the annual Economic Survey of Latin America prepared by Cepal. Also see the annual Memoria of the Central Reserve Bank of Perú; the number issued for 1976 is particularly good. For analysis of economic trends in 1963-1968, see Kuczynski. For a view of events in 1968-1972 consult Quijano and the Central Reserve Bank of Peru (1972 and 1973). Analysis of the period 1968-1975 is found in Fitzgerald, Schydrowsky and Wicht, and Cepal (forthcoming). Authors Cabieses and Otero study the years 1965-1975. For analysis focussing on external debt during the military government see Ugarteche (forthcoming) and Reynolds.
2. See Levinson and De Onis, p. 148.
3. See Fitzgerald, p. 4.
4. See Hunt (1971), p. 377.
5. In 1960 government investment was equivalent to only 2% of GNP. See Cepal, Estudio Económico de América Latina 1965, p. 263. Also see Hunt (1971), p. 392 and Kuczynski, p. 13.
6. See Kuczynski, pp. 13-17.
7. See table 16 in Kuczynski
8. Calculated by using Kuczynski's data and deflating with the consumer price index.
9. This is very explicit in the Economic Plan for 1962-1971. See Ugarteche (1979), p. 5.

10. See Humberto Cabrera, pp. 25-26.
11. See Kuczynski, p. 130.
12. A familiar political slogan in Congress at this time was "No more taxes". See Kuczynski, p. 41.
13. Ibid., p. 98.
14. In that year the government was able to make ample use of public deposits such as those related to the social security system. See Kuczynski, pp. 98-99.
15. See Mariategui, pp. 3-21.
16. For the full history of the dispute, see Pino. Also see Kuczynski, Chapter 5.
17. In addition to the IPC dispute, which was being handled by the executive branch, Congress had put in motion measures to renegotiate the contract for the Toquepala copper mine of the Southern Perú Copper Corporation, a subsidiary of the American Smelting and Refining Company, Phelps Dodge, Newmont Mining and the Cerro Corporation. The highly liberal terms of the original contract were in concordance with a 1950 mining code. See Bossio Rotondo, pp. 132-136.
18. Kuczynski, p. 118.
19. Ibid., p. 96.
20. Ibid., pp. 102-105.
21. Ibid., p. 154.
22. Source: Field research of the author.
23. See Ugarteche (1979), Chapter 2.
24. Kuczynski, p. 153 and Pino, p. 131.

25. As another indication of the debt problem, it can be pointed out that by 1968, 65% of the external debt had to be paid within 5 years. See de la Melena (1976), p. 72.
26. No limits were placed on loans with a maturity of less than 181 days or more than 15 years. (Source: field research).
27. See Piñelo, pp. 140-145, for an account of events.
28. "Manifiesto del Gobierno Revolucionario de la Fuerza Armada", October 8, 1968. See Kerbusch, pp. 159-160.
29. Fitzgerald, p. 1.
30. (Author's translation). From Presidential message on the 149th anniversary of independence, Lima, July 28, 1970, as quoted in Willmore, p. 97.
31. Based on statement by Minister of Finance in the Joint Annual Discussion of the Board of Governors of the World Bank and IMF in September 1970 as quoted in Willmore, p. 101.
32. De la Melena (1973), p. 187. and Ugarteche (1978), pp. 60-61.
33. 120 million dollars came from the U.S. and Canada and 60 million dollars came from Japan and Europe. De la Melena (1973), pp. 199-200; (1976) p. 86.
34. Ibid.
35. The standby agreement expiring in 1969 was not renewed (Quijano, p. 28); however, close contact with the Fund was maintained through 1970 (Quijano, p. 102). Use of Fund resources was limited to finance with no conditionality.
36. Instituto Nacional de Planificación, pp. 19-20.
37. Ibid.

38. Ibid. p. 20.
39. Based on data in tables 1 and 11 of Cabieses and Otero, pp. 209 and 220, respectively.
40. In 1971-1972, 26% of all investment went to these sectors, while in 1973-1974 the figure was roughly 46%. See Fitzgerald, p. 88. For a summary list of some of the major projects, again see Fitzgerald, p. 87.
41. Much of the subsidy was for petroleum and food, the latter of which had to be imported in large quantities because of almost stagnant local production.
42. The figures themselves refer to 1974 and 1975. See Fitzgerald, pp. 41, 53 and 84.
43. Ibid., pp. 44-45.
44. Central Reserve Bank Memoria 1976, pp. 44-47.
45. Ibid.
46. Fitzgerald, p. 55, table 32.
47. Horton, p. vii.
48. Ibid., p. i; also see table on p. 8 for historical data on food production.
49. Brundenius, p. 19.
50. See table 2 on p. 210 of Cabieses and Otero. It should be noted that the fact that production did not fall below the pre-reform output trends was in itself a major achievement.
51. Cabieses, pp. 79-80 and Fitzgerald, p. 34.
52. See Fitzgerald, pp. 34-35.
53. Ibid., p. 34.
54. De la Melena (1973), p. 131.

55. See de la Melena (1973 and 1976) for an overall view of the reforms.
56. For a comprehensive view of how Jutrex and Cotrex functioned, see Ugarteche (1979), Chapter 3. For a more abbreviated view, see de la Melena (1973), pp. 212-215.
57. Ugarteche (1979), pp. 22-23.
58. Ibid., Appendix 2., p. 57.
59. De la Melena (1973), p. 211.
60. For a detailed view of how these two bodies functioned, see Ugarteche (1979), Chapter 4.
61. Ibid. and de la Melena (1973), p. 66.
62. Ugarteche (1979), Chapter 5.
63. Ibid., pp. 7-10 and Chapter 5.
64. Fitzgerald, p. 89.
65. Ibid.
66. Ibid.
67. Ibid., p. 85.
68. (Authors' translation) Ugarteche (1979), p. 48.
69. Ibid., p. 49.
70. See new policy guidelines set out in DL 22149 in Ugarteche (1979), p. 12.
71. Fitzgerald, p. 20.
72. Kuczynski, p. 239.
73. Brudenius, p. 77.
74. Fitzgerald, p. 20.
75. Nickson, p. 15. It should be noted that trade also was heavily geared towards the United States, with it being the market for roughly 40% of all exports and one-third of all imports.

76. See Friedman, p. 53.
77. Pinelo, p. 145.
78. See texts of Decree Law N24-17066 and "Manifiesto del Gobierno Revolucionario de la Fuerza Armada" of October 1968 as reproduced in Kerbusch, pp. 154-159.
79. Brundenius, p. 40.
80. Bosso Rotondo, p. 136.
81. Ibid., p. 134.
82. Ibid., p. 133.
83. See NACLA (March 1976), pp. 24-30.
84. Fitzgerald, p. 68.
85. For details on the government's actions to rationalize the industry see Hunt (1975), pp. 323-325.
86. The first reform law on the financial sector was introduced in the last days of power of the previous regime under the umbrella of the emergency law 17044 of June 1968. See Kuczynski pp. 230-243. The basic proposals of the law were implemented by the new regime, with modifications that basically made for more stringent application.
87. See DL 1835 in Ley de Bancos, p. 163.
88. Ibid., p. 28. The first version of the law which came out in June 1968 under emergency law 17044 required two-thirds national ownership.
89. The industry was 73% national in terms of ownership shares. Of the foreign held shares, the United States had 65%, England 6.6%, France 5.7%, Japan 4.7%, Switzerland 3.5%. See Ministry of Fishing, pp. 38 and 134.
90. Brundenis, p. 42.
91. See Malpica, p. 174.



92. Most of the compensation was paid in Soles and reinvested in a new Sheraton Hotel in Lima. See Hunt (1975), pp. 315-316.
93. Chase invested 1.7 million dollars in the bank in 1965; it received 6.3 million dollars in compensation, Ibid., p. 316 and NACLA (April 1976), p. 6.
94. NACLA (March 1976), pp. 29-30.
95. See La Crónica.
96. Medina (NQ16), p. 3 and Hunt (1975), pp. 335-336.
97. La Crónica, Overall, in its first 26 months of operation Occidental struck oil on the first 5 wildcat wells. PETROPERU had 3 successful wildcats strikes. See Hunt (1975), p. 336.
98. See COPE.
99. Medina (NQ18), p. 15.
100. (Author's translation), La Crónica.
101. Medina (NQ18), p. 15.
102. PETROPERU ← Memoria 1974, p. 21.
103. Ibid., p. 24.
104. See BCR (1976) p. 47.
105. Petroperú, Memoria 1975, pp. 23 and 45.
106. See Ministry of Economics and Finance (1976).
107. PetroPerú, Memoria 1976, pp. 23, 26, and 43.
108. Index B was also calculated by using<sup>u</sup> purchasing parity index, but the results were not unsimilar to the index in the table which uses a nominal exchange rate.
109. The formal export promotion program, CERTEX, apparently was not very effective. See Schydrowsky and Wicht, p. III. 28.

## Chapter 4

### The supply of external finance: an overview

The previous chapter reviewed the evolution of the public sector over the 12-year period 1965-1976 and some of the factors underlying its demand for external resources. The demand, of course, was conditioned by supply, and it is the task of this chapter to see how the various types of finance responded to the external needs of the government. The first part of the chapter will be an overview of the behavior of the supply side for the same 12-year period, taking into account the amounts authorized, the terms of finance, etc. The second part will go into more detail on the factors behind the response of the various sources of finance. Commercial banks will be part of the analysis; however, they will be treated in a general way, leaving a more detailed examination for subsequent chapters.

#### I. External finance: the structural shift to banks

As was pointed out earlier, the public sector's medium to long term external debt was not exceedingly large at the outset of the period under study; at 385 million dollars in 1965 it was equivalent to roughly 9% of the GNP. However, the debt had grown very rapidly, doubling with respect to 1960, and with most of the expansion having taken place from 1962.<sup>1/</sup> One can gain an idea of just what sources of finance were important to the government at this time by reviewing the composition of external public debt at the middle of the decade. Table 4.1 provides such a profile for Peru and Latin America as a whole.

Table 4.1

PERU AND LATIN AMERICA: DISTRIBUTION OF EXTERNAL PUBLIC  
DEBT ACCORDING TO SOURCES OF FINANCE,  
1965-1966 and 1975-1976<sup>a)</sup>  
(Percentage)

	Private				Official		<u>Total</u>
	<u>Bonds</u>	Suppliers	Banks	Others	Multilateral	Bilateral	
<u>1965-1966</u>							
Perú	5	40	8	3	23	21	100
Latin America	8	20	9	3	23	37	100
<u>1975-1976</u>							
Perú	-	11	45	3	11	30	100
Latin America	4	9	39	5	21	22	100

Source: InterAmerican Development Bank, External Public Debt of the Latin American Countries, Washington, D.C. 1978.

Note: Data are not compatible with figure 4.1 and table 3.5.

a) Disbursed and undisbursed debt with maturity of more than 1 year.

From the table it is clear that at the beginning of the period under study the primary sources of finance for Peru were private and commercial, accounting for 56% of all public obligations. In contrast, for Latin America as a whole private sources accounted for only 40% of region's debt. Thus Peru, despite being a relatively poor country, by the mid-60's already had an unusually "commercialized" external debt with the accompanying "hard" terms; more concessionary official finance played a secondary role, accounting for only 44% of all obligations. For Latin America, however, concessionary sources of finance dominated the financial scene, as displayed in their 60% participation in the region's external debt.

In the mid-60's most of Peru's private funds came from commercial suppliers who held some 40% of all obligations, a representation that was double the figure for the region. And significantly, at this time commercial banks were minor lenders to both the governments of Peru and the region.

Over the 12 years, for Peru private commercial sources of finance continued their dominant role; however, there was a radical structural shift in the individual sources of supply. As seen in table 4.1, by the end of the period commercial banks were holding 45% of the country's debt, while the suppliers' portion had shrunk to 11%. Overall, private sources accounted for nearly 60% of all outstanding obligations at the end of the period. Similarly, the participation of banks in the external debt of the region increased dramatically over the period. However, in contrast to Peru the use

of commercial banks was not at the expense of foreign suppliers, but rather official sources of finance. Also, the relative increase in the importance of the banks was less intense for the region than it was for the government of Peru.

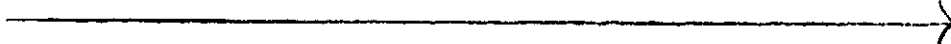
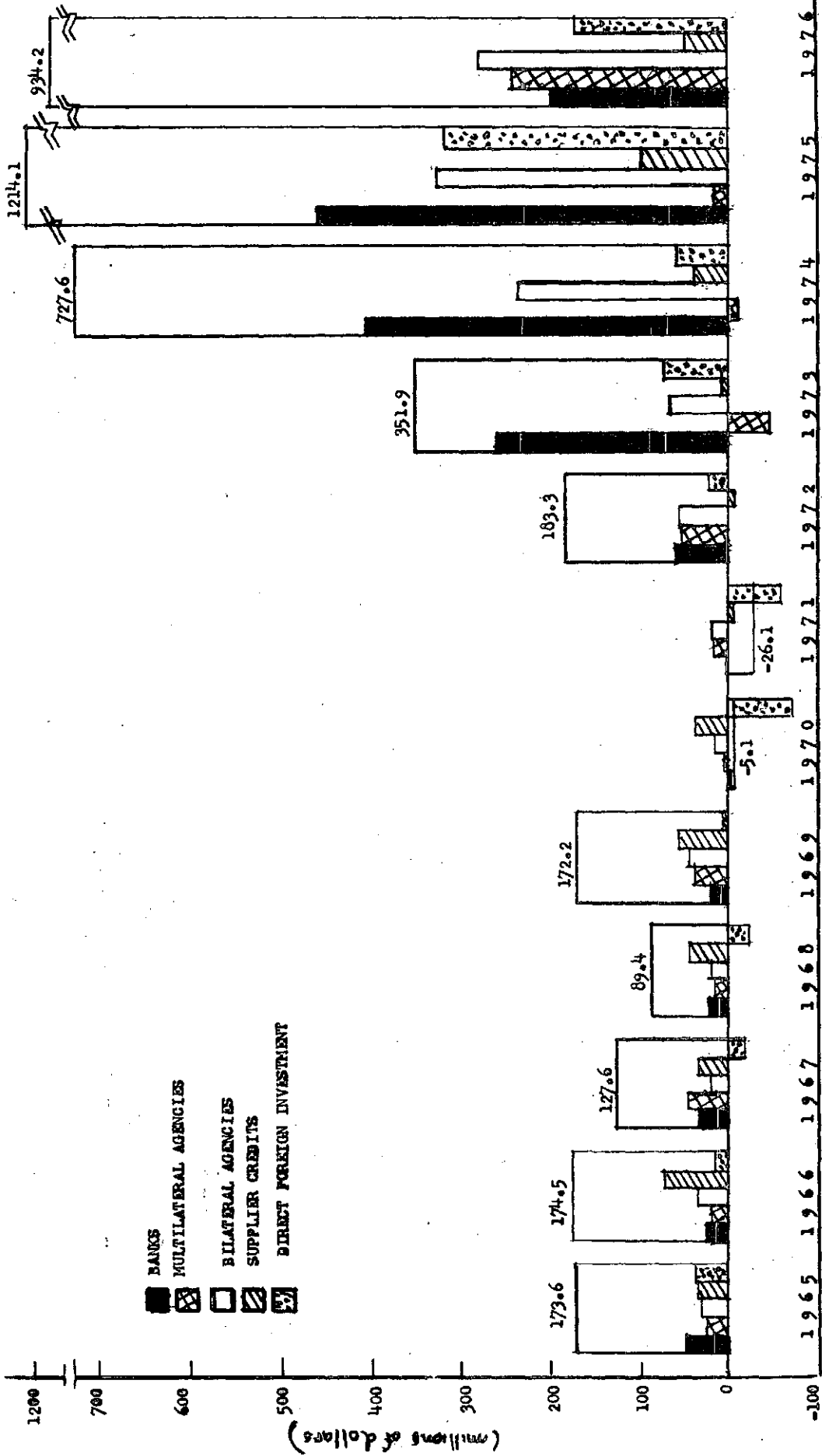
The above clearly shows a general shift to commercial bank finance over the period 1965-1976. In the case of Peru, one can track the shift by reviewing the annual data on net external financial flows that are presented in figure 4.1. While these data are not directly comparable to the external debt figures just shown, they provide an 

Figure 4.1  
PERU : NET EXTERNAL FLOWS BY SOURCE 1965-1976



Source : CEPAL on the basis of official data.

2) All public sector except direct foreign investment. Loans include transactions for material defense.

adequate indication of how and when the shift took place. In order to provide a complete picture of the play of forces among the various types of finance, the figure / also incorporates the annual net flows of foreign direct investment.

Data reveal that during 1965-1968 the principal sources of finance were commercial suppliers' credits. But the fact that net flows from commercial banks were as significant, and in some cases more significant, than official finance means that they were gaining importance with respect to the relatively minor role attributed to them at the outset of the period. As for flows of direct foreign investment, they were of importance only in 1965; net inflows were marginally positive in 1966 and were negative in 1967-1968. When viewed as a whole, total flows averaged 141 million dollars per year / in 1965-1968, although this figure is biased downward by the unusually small amount of finance realized in the last year.

During the period of stabilization, 1969-1971, the most notable feature is negative flows of finance. While total flows were strongly positive in 1969 - perhaps reflecting disbursements on prior commitments - they averaged a negative 16 million dollars in 1970-1971. In these latter two years net financing from all sources was marginal, with direct foreign investment registering significant negative balances due to divestment.

As seen in the figure, there was a general recovery in finance in 1972, which coincided with the reactivation of public sector

activity. It also was the year in which finance clearly began to shift in favor of commercial banks. Indeed, between 1973 and 1975 commercial banks dwarfed all other sources, with some balance among sources being restored only in 1976. In this same period bilateral finance and direct foreign investment were of some significance as well. However, suppliers' credits ceased to be an important source of finance and multilateral flows - negative in 1972-1974 - became significant only in 1976.

Leaving aside for now the qualitative implications of the shift towards commercial bank finance, it is of interest to examine the impact that the reliance on banks had for government finance.

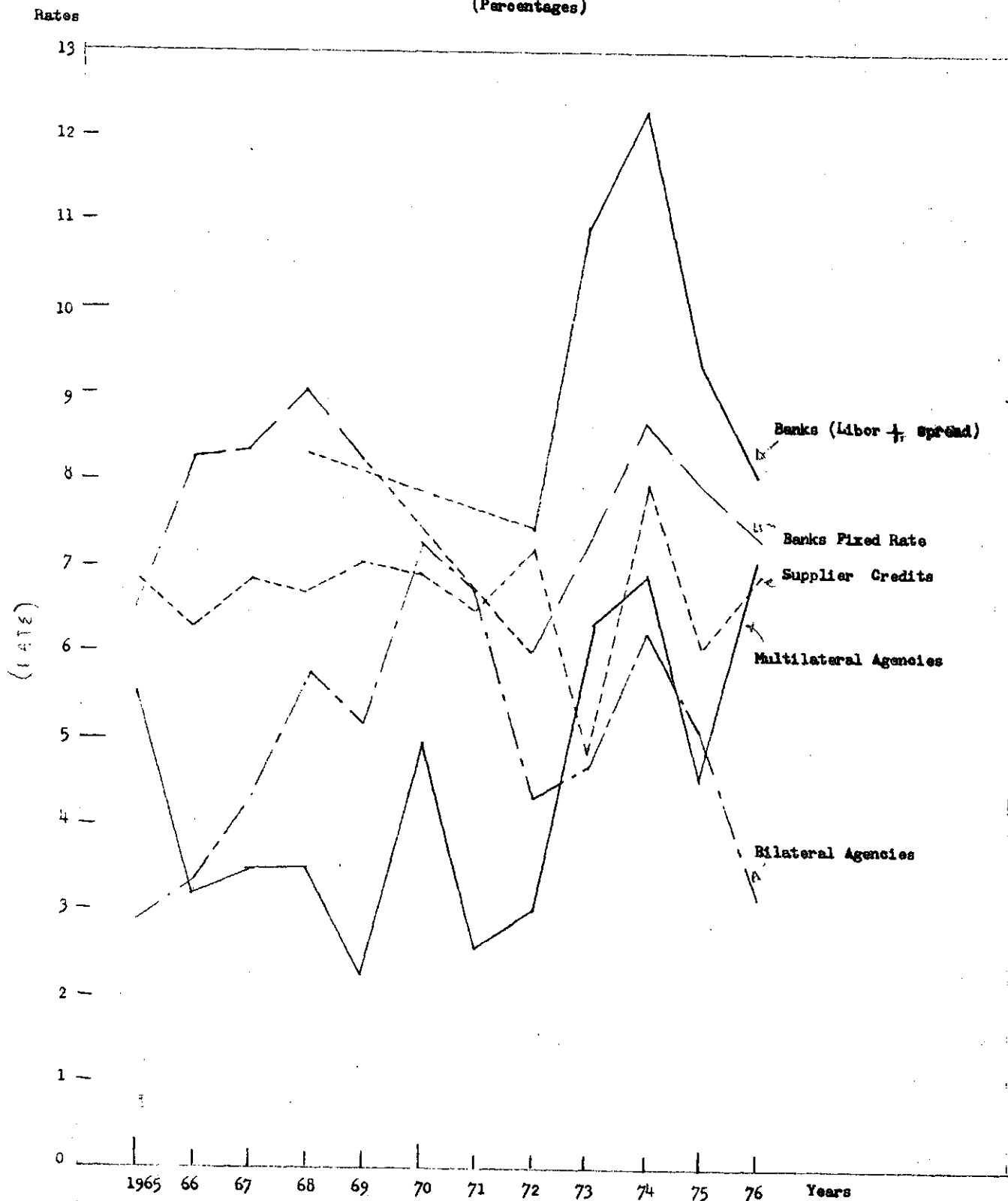
With regard to the cost of credit, the shift to banks pushed the government into the highest echelon of interest rates. This is seen in figure 4.2 which presents the average interest cost of the various types of foreign loans. By moving out of suppliers' credits and into bank loans the government gave up intermediate rates of interest for the highest possible rates. Moreover, the differential rate between banks and suppliers' credits was by no means marginal. Of course, the difference with respect to official finance was of even greater magnitude.

Another result of the shift to commercial bank finance was shorter repayment terms. By viewing figure 4.3 one can see that banks had the shortest available maturities. Again by shifting from suppliers' credits to banks, the government moved away from an intermediate tenor to the short end of the maturity spectrum. The weight of repayment terms was further aggravated by the fact that over the 12 years there was a noticeable shortening of maturities of official agencies as well.



Figure 4.2

PERU : AVERAGE RATES OF INTEREST ON LOANS, 1965 - 1976 <sup>a/</sup>  
(Percentages)







Source : CEPAL, on the basis of official data

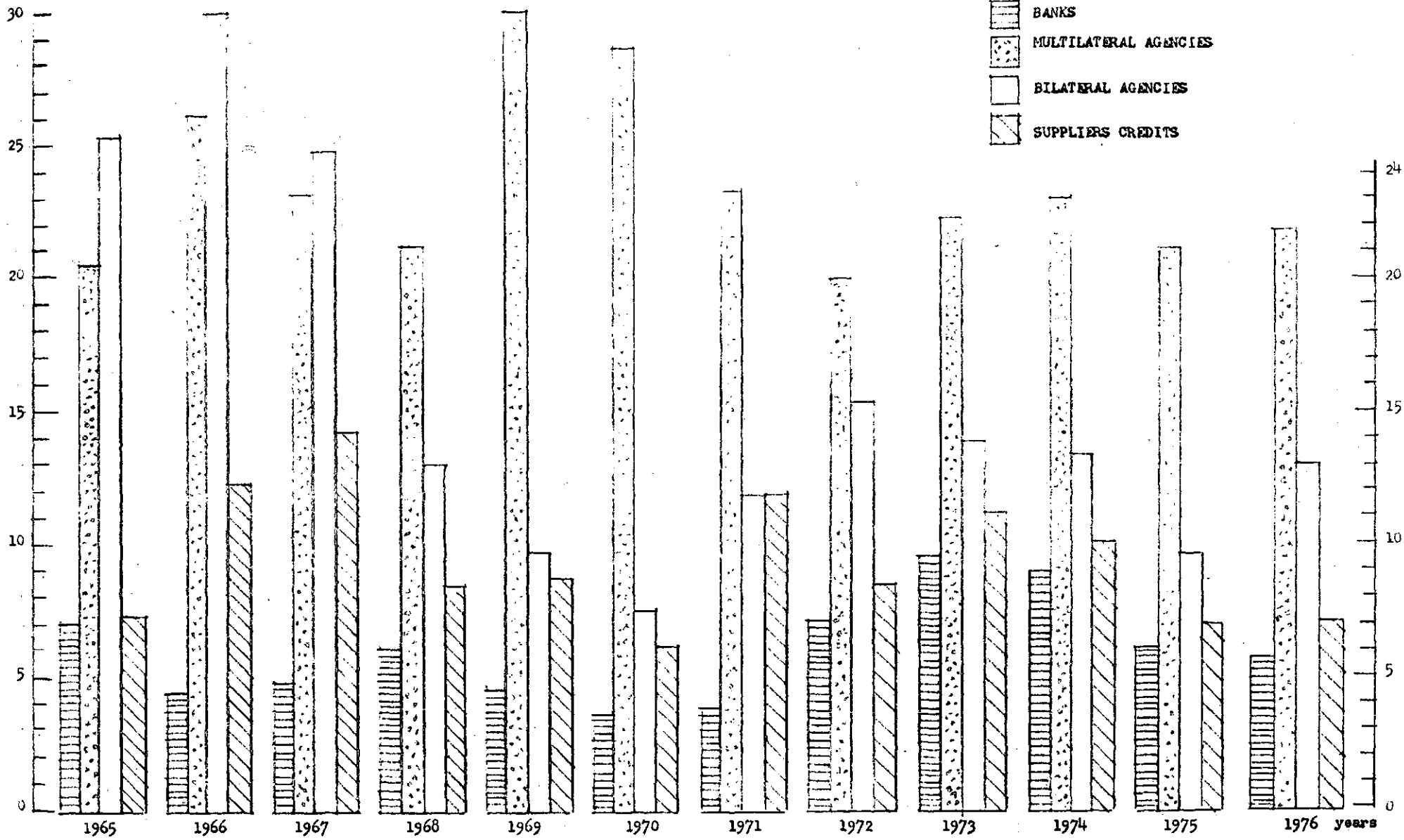
<sup>a/</sup> All loans, including those related to national defense

Figure 4.3

PERU : AVERAGE TOTAL MATURITY ON LOANS BY SOURCE <sup>a/</sup>

LEGEND

-  BANKS
-  MULTILATERAL AGENCIES
-  BILATERAL AGENCIES
-  SUPPLIERS CREDITS



Source : CEPAL, on the basis of official data

<sup>a/</sup> All loans, including those of national defense

Thus one has seen that during 1965-1976 the role of commercial banks in public sector external finance took a dramatic leap, with the shift taking place most notably around 1972. Unlike the experience of many developing countries which increased their reliance on bank finance in the 70's, the shift was not from concessional sources to banks, but rather from suppliers' credits to banks. The higher profile for commercial lending institutions meant that the bulk of government finance was carried out under the hardest credit conditions as opposed to the nominally (see below) intermediate terms that suppliers offer. The weight of credit terms also was aggravated by a noticeable stiffening of conditions on official credit.

Notwithstanding the impact of the shift to banks on the average terms of credit, it is by no means certain that Peru necessarily was worse off as a result. It is true that suppliers' credits commonly had average maturities between 7 and 14 years and fixed interest rates of between 6 and 7 per cent - far softer than bank credit. But these terms severely understate costs since additional margins probably were hidden in the purchase prices of the goods financed and the charges for accompanying services. There also were implicit costs in having finance tied to specifically-sourced goods. In contrast, bank finance was not tied to specific foreign suppliers; indeed, it largely was not tied to foreign purchases at all. This in turn introduced new flexibility into the finance of development. It would seem, then, than all one can really say about the shift to banks is that a relatively poor country continued under the yoke of rather inappropriate commercial sources of finance.

## II. Factor underlying the behavior of supply

After having tracked the shift to commercial banks, the next step is to try to explain why the various sources of supply behaved the way they did.

The response from the supply side is, of course, derived from a number of forces. On the one hand, the government must select a particular source of finance. While selection is undoubtedly based on a desire to secure the most favorable terms possible, more often than not availability is the overriding concern. And availability is determined by many factors such as the credit institutions' perception of risk, its liquidity position, political motivation, marketing strategies, etc.; even personal rapport between government officials and key persons who control or influence decisions in credit institutions can be relevant. The following paragraphs will attempt to analyse in a brief way those factors underlying the behavior of the principal sources of supply.

### A. 1965-1968: Dependence on suppliers' credits

As just seen, this was a period when suppliers' credits were a dominant source of supply. This meant that public sector external finance had to rely on credits with an average term ranging between 7 and 14 years and fixed interest rates of 6-7%. These were relatively hard terms for a country as poor as Peru; moreover, as mentioned above these terms probably understate effective costs. The government took recourse to these funds largely because of a lack of availability of more appropriate types of finance.

In Chapter 3, one saw that the public sector at this time was small and relatively unsophisticated by Latin American standards. The situation was reflected in the fact that officials were not particularly experienced in the preparation of proposals for project loans from international agencies; criteria for proposals were relatively stringent and apparently proved taxing to the limited capacity of the public sector.<sup>2/</sup> In contrast, commercial suppliers, eager to sell their equipment, asked few questions about the merits of projects and proved to be a very elastic source of finance. Thus the government embarked on a program of capital intensive investments - the SOGESA steel mill was a large absorber of foreign funds - that easily attracted credit from commercial suppliers.

Another factor of import behind the recourse to suppliers' credits was that the U.S. Agency for International Development (AID) - then a major source of long term concessionary finance to Latin America - had variously frozen CR delayed credit through most of the 5-year term of the government.<sup>3/</sup> Almost as soon as it came into power, loans to the new government were delayed as part of a policy designed to ensure a "satisfactory" settlement of the dispute over the IPC. Curiously, for nearly 3 years there never was an official reason given for the slowdown in loans.<sup>4/</sup> Not until early 1966 did an official statement appear about the freeze; however, shortly thereafter aid was officially renewed when Peru provided assurances that it did not intend to expropriate the IPC.<sup>5/</sup> Unfortunately, the program did not last long as the next year AID loans were once again frozen, because of a much publicized dispute stemming from the fact that the Peruvian government bought supersonic jets from

France after facing long delays in approval of a request to purchase less sophisticated American aircraft.<sup>6/</sup>

The net effect of hegemonic politics during the period was to blackball Peru from one of the more important sources of long term credit in the 1960's. As seen in table 4.2, A.I.D.'s assistance to Peru was far behind that granted to other countries. Ironically, it was the new Peruvian government which had one of social programs in Latin America that most closely mirrored the principles of the Alliance for Progress.

Commercial bank medium term lending during the period - averaging about 30 million dollars per annum on a net basis - was not terribly large. However, as was seen earlier it was of some significance relative to other sources of finance. Moreover, its importance far exceeded the relative and absolute amounts provided.

In the early 60's commercial bank finance to the government was made up mostly of secured short term credits to the state development banks.<sup>7/</sup> But at the very end of 1964 the government secured a 40 million dollar 3-year loan from a group of banks to help close its fiscal gap.<sup>8/</sup> Peru, at this time having a liberal economic environment, free foreign exchange regime and a large amount of direct foreign investment apparently was considered a good enough risk - notwithstanding its fiscal problems - for the banks to extend what was for the time a relatively sizeable medium term credit.<sup>9/</sup> However, the term was very short and repayment ultimately would prove to be burdensome to the budget.

In 1966, with fiscal problems intensifying, recourse to short term bank credit was considerable. The government also managed to refinance the balance due on the 1964 credit of 40 million dollars on 5-year terms and obtained an additional 12 million dollars to boot.

Table 4.2

PERU: COMMITMENTS OF USAID ASSISTANCE, JULY 1963-JUNE 1968

	Total (millions of dollars)	Per capita (\$)
Brazil	1 067	12.5
Chile	346	40.1
Colombia	353	19.0
Peru	90	7.5
Dominican Republic	244	67.0
Nicaragua	73	43.2
Panama	88	69.3

Source: Reproduced from KUCZYNSKI, p. 125.

Then in 1967, with the fiscal situation now in open crisis, a number of desperate short term bridge loans were arranged with banks. In conjunction with the IMF accord the government also arranged a 40 million dollar 5-year general purpose budgetary loan as well. Then, in the chaotic period between the devaluation in late 1967 and the tax reform of June 1969, it was commercial bank short term bridge finance that helped to fill the fiscal gap. Finally, after the tax reform, commercial banks agreed to restructure (refinance) repayments on earlier budgetary loans over a 5-year period. Along with this finance the banks also agreed to provide some "standby" credits for the use of the government during the IMF stabilization program.

The credits just cited are by no means an account of all the bank transactions realized during the period; such detail will be saved for later chapters. What one has tried to show, however, is that, at the margin, bank loans played a key role in keeping the fiscal accounts afloat, or looked at from another angle, they helped to postpone the need to take measures that would rectify the fiscal imbalance.

#### B. 1969-1971: A financial blockade

As seen in the last chapter, with the arrival of the new government in October 1968 there was a serious restructuring of relations with foreign capital. But importantly, foreign capital did not accept the measures passively and, in line with tradition, affected corporations sought to involve their home governments. Not surprisingly the U.S. government became involved; a series of measures were taken to show displeasure with Peru's program to reorient foreign capital to national



development objectives. One of the principal tools used was a financial boycott.

After the nationalization of the IPC, Perú was threatened with the U.S.'s Hickenlooper Amendment. The implications of the Amendment have been concisely explained by Levinson and De Onis:

To protect the interests of American companies abroad, Senator Bourke B. Hickenlooper, urged on by Harold Geneen, the president of IT & T, introduced an amendment to the Foreign Assistance Act of 1962. This amendment required the president to suspend all economic assistance to any country that expropriated the property of a U.S. company, repudiated a contract with a U.S. company, or made a U.S. company subject to discriminatory taxation or administration. Suspension of all forms of economic assistance included not just foreign aid, but such legislation as that allotting sugar quotas to favored nations. A country had six months in which to take 'effective steps' to provide compensation for expropriated property in 'convertible foreign exchange'. Thereafter the president was allowed no discretion to waive enforcement of the amendment.<sup>10/</sup>

In March 1969 the U.S. sent a delegation to Peru to discuss compensation for U.S. assets. It then was agreed to defer implementation of the amendment pending negotiations and court proceedings concerning compensation for the IPC.

But what the U.S. agreed not to do formally was largely done informally. Perú's sugar quota was revoked, arms supplies were suspended, and most bilateral financial programs (including Export-Import Bank loans) were frozen. Moreover, the U.S. used its leverage in multilateral agencies to freeze credit from these institutions as well.

It is important to point out that the financial blockade was not as absolute as it would have been had the Hickenlooper Amendment been evoked. The Peruvian government, facing informal rather than official legal sanctions, attempted to place pressure on multilateral agencies

to honor their commitments to Peru. Efforts were particularly intense at the Inter-American Development Bank (IDB) - where there was a high degree of homogeneity among member governments - and culminated in a presidential speech at an annual IDB meeting in which multilateral agencies were blasted for being "used as an arm of political pressure" against member countries like Peru.<sup>11/</sup> The initiative was somewhat fruitful at the BID where a reasonable level of loan authorizations was maintained.<sup>12/</sup> Some loans also were approved by the U.S. government and the World Bank, but as seen in table 4.3, it is clear that authorizations by these latter two agencies were unusually scarce during 1968-1971.

The blockade clearly was costly to Peru. As seen in table 4.4 net bilateral loans from the U.S. were negative during the period. Donations were unusually large in 1970, but they represent extraordinary acts of mercy designed to help the government overcome the damage of a massive earthquake that struck Peru early that year.

Table 4.5 shows that disbursements from the World Bank also were minimal for the period; moreover, the lack of authorizations during 1969-1971 undoubtedly contributed to the low level of disbursements in succeeding years as well. The only buoyant source of loan disbursements was the IDB, which as was just pointed out, was a focal point of Peruvian resistance to the boycott.

Table 4.3

PERU: FINANCIAL ASSISTANCE FROM THE UNITED STATES AND WORLD BANK  
OCTOBER 1968-DECEMBER 1971

Source	Date authorized	Amount (millions of dollars)	Purpose
World Bank <u>a/</u>	8-9-1970	30	Road construction
Export-Import Bank <u>b/</u>	8-9-1970	4.3	Hercules aircraft
Other United States <u>c/</u>	29-6-1971	3.0	Community development

Sources: World Bank: Statement of Loans, May 31, 1977.

EXIMBANK: Statement of Loans, June 30, 1976

Other: United States Foreign Credits, (June 30, 1973). and United States Department of Treasury. Statement of Loans, November 1974

a/ Includes IFC.

b/ Direct loans only.

c/ Excludes Commodity Credit Program.

Table 4.4

PERU: BILATERAL FINANCE ACCORDING TO SOURCE, 1965-1976<sup>a/</sup>

(Millions of dollars)

	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976
United States	24	30	12	14	-1	-5	1	46	35	-13	12	37
Europe	9	8	11	8	45	7	-8	-11	-9	-4	43	40
United Kingdom	(-)	(-)	(1)	(1)	(-)	(-)	(-)	(1)	(-)	(3)	(14)	(8)
Germany	(3)	(4)	(8)	(5)	(29)	(-4)	(-9)	(-8)	(-12)	(-6)	(-)	(4)
France	(-)	(-)	(-)	(1)	(4)	(5)	(7)	(-1)	(-3)	(-6)	(-1.3)	(2)
Japan	-	-	-	-	-	-	-	8	34	169	153	62
Centrally planned	-	-	-	-	-	-	-	7	5	52	61	88
Canada	-	-	-	-	3	13	9	2	6	19	28	13
Other	-	-	-	-	-	4	16	4	-6	14	28	39
<u>Subtotal<sup>b/</sup></u>	<u>32</u>	<u>37</u>	<u>23</u>	<u>22</u>	<u>47</u>	<u>19</u>	<u>19</u>	<u>55</u>	<u>65</u>	<u>237</u>	<u>323</u>	<u>279</u>
Donaciones	24	28	32	37	31	82	39	39	42	48	49	58
<u>Total</u>	<u>57</u>	<u>65</u>	<u>55</u>	<u>59</u>	<u>78</u>	<u>101</u>	<u>58</u>	<u>94</u>	<u>107</u>	<u>285</u>	<u>372</u>	<u>337</u>

Source: Table A44, statistical appendix.

a/ Net flows.

b/ May not sum properly because of rounding.

Table 4.5

PERU: MULTILATERAL FINANCE ACCORDING TO SOURCE, 1965 - 1976<sup>a/</sup>

(Millions of dollars)

	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976
IBRD	14	14	15	3	5	2	4	2	-	-2	68	11
IDB	11	8	10	12	10	16	20	21	10	6	9	10
CAF	-	-	-	-	-	-	-	-	-	1	-	-
IMF	-	-	22	4	25	-9	-7	30	-58	-17	-	220
<u>Total</u> <u>b/</u>	<u>25</u>	<u>22</u>	<u>48</u>	<u>19</u>	<u>40</u>	<u>9</u>	<u>17</u>	<u>54</u>	<u>-49</u>	<u>-12</u>	<u>76</u>	<u>241</u>

Source: Table AI.1, Statistical Appendix.

a/ Net flows.

b/ May not sum properly due to rounding.

As for suppliers' credits, there is no specific information about why they behaved the way they did. But perhaps it is no coincidence that net flows from U.S. suppliers were negative in 1969-1971 (see table 4.6). The negative attitude of the U.S. government and difficulty in obtaining official export credit guarantees from its agencies probably discouraged credits from this source. Also, well-publicized investment disputes may have adversely affected the willingness of suppliers to extend external credit. Finally, as was seen in the last chapter, the period was dominated by stabilization efforts, which meant that investment activity was restrained and opportunities for "tied" external finance were commensurately reduced.

It has been shown that during this period commercial banks provided practically no new credit to the government. As seen in the previous chapter, many banks had links with nationalized firms and their restrictive attitude on credit could have been related to Peru's treatment of foreign investors. However, it is difficult to determine whether banks were cooperating with the boycott or simply responding to objective circumstances. It has to be remembered that banks at the time were still very cautious lenders to developing countries. Not only was the public sector's external debt clearly burdensome, but there was great uncertainty about the government's treatment of foreign capital. Moreover, far-reaching reforms were being introduced and the nature of public policy was clearly interventionist, in contrast to the banks' ideological preference for free market economics. Furthermore, for U.S. banks, no loans guarantees could be secured because the doors of the U.S. Eximbank were closed to Peru. Thus, a cautious attitude

Table 4.6

PERU: SUPPLIER CREDITS ACCORDING TO SOURCE, 1965-1976<sup>a/</sup>

(Millions of dollars)

	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976
United States	2	19	7	1	-7	-6	-3	8	-1	-	3	-5
Western Europe	27	38	21	48	65	18	-17	-30	-15	-9	35	31
United Kingdom	(1)	(-2)	(-2)	(3)	(5)	(2)	(1)	(-3)	(-4)	(2)	(1)	(-)
Germany	(-2)	(21)	(2)	(-10)	(-14)	(-9)	(-21)	(-11)	(-16)	(-17)	(-7)	(-5)
France	(21)	(-)	(-1)	(23)	(19)	(-4)	(-9)	(-7)	(-9)	(2)	(29)	(11)
Italy	(2)	(1)	(12)	(15)	(58)	(35)	(20)	(-3)	(16)	(-)	(3)	(9)
Japan	9	16	11	-2	1	-5	-4	-7	8	13	-6	-6
Centrally planned	-	-	-	-	-	-	-	8	22	44	65	7
Canada	2	-	-	-	-1	32	14	-2	-10	-6	-6	-6
Mexico	-	-	-	-	-	-	-	-	-	-	-	14
Other	-	1	1	1	-	1	1	15	2	-4	7	10
<u>Total b/</u>	<u>38</u>	<u>74</u>	<u>39</u>	<u>47</u>	<u>58</u>	<u>39</u>	<u>-8</u>	<u>-8</u>	<u>7</u>	<u>39</u>	<u>98</u>	<u>46</u>

Source: Table A.5 Statistical Appendix.

<sup>a/</sup> Net flows.

<sup>b/</sup> May not sum properly due to rounding.

could have been expected even in the absence of a boycott, making bank involvement in the affair very problematical.

Finally, it should be mentioned that the banks did reluctantly go along with the authorities' request in 1969 for a refinance of 1970-1971 obligations; in fact, their options were limited since official lenders had agreed to refinance their obligations and Peruvian authorities were hinting that creditors who were unwilling to cooperate with them would simply not be repaid. As one will see later in Chapter 8, the refinancing was not very pleasant as commercial banks were careful to attach rather onerous conditions to their credits.



C. 1972-1975: from financial famine to financial feast

In this period the pendulum changed and Peru actually became swamped with external credit. There were some special factors at play and it is worthwhile viewing them in detail.

1. The removal of the financial blockade

By 1972 there were clear signs that the U.S. was reformulating its position on Peru. Around mid-year U.S. foreign aid agencies approved new loans in an amount close to 28 million dollars (mostly for earthquake damage) and there were abundant food credits from the Commodity Credit Corporation.<sup>13/</sup> As further evidence of a thawing of the freeze was that this year the IBRD convoked a consultative group meeting in Paris in which it declared Peru creditworthy, i.e., no longer in need of refinance, and formally supported the government's recently formulated development plan. It is pretty clear why the U.S. was having second thoughts about the value of maintaining a hard line with the government: Peru by now had shown that it had sufficient resolve to resist external pressures; European, Japanese and Soviet business had been actively penetrating the Peruvian economy - formerly an American preserve - and, perhaps most importantly, oil had been discovered in the Amazon, making the country potentially important to the U.S.'s energy strategy.<sup>14/</sup>

While steps were taken to remove the boycott in 1972, its effects lingered for several more years, with the consequent loss in terms of access to concessionary credit. The World Bank actually

did not renew the flow of credit to Peru until August 1973 when it approved an agricultural development loan of 25 million dollars. Meanwhile, the U.S. Export-Import Bank - important both because of its own loans and the guarantees it provides private lenders - did not authorize a new credit until March 1974, and it was for the benefit of the U.S.'s Southern Peru Copper Corporation. The first Eximbank credit to the public sector did not appear until August 1974, shortly after the signing of the Greene Accord, and was for 1.4 million dollars to help cover the purchase of 2 new Learjets.<sup>15/</sup> Thus, the government of Peru/<sup>had</sup>suffered through a financial blockade on concessionary finance of varying degrees of intensity for a period of nearly 6 years.

## 2. Diversification of sources of finance

Given that Peru encountered overt and disagreeable political conditions attached U.S. foreign assistance during 1963-1968, and then again in 1969-1974, along with loss of access to credit from international institutions, it comes as no surprise that officials became interested in diversifying their sources of finance.<sup>16/</sup> This is manifested by the fact that by 1972 the government was receiving finance from/<sup>many</sup>non-traditional areas. According to table 4.4 by now Japan and the Centrally Planned Economies - of no importance in the 60's - were major sources of finance. So was Canada. Pursuit of this strategy intensified in subsequent years, such that the U.S. share of bilateral loans/<sup>to the government</sup>fell from over 77% in 1965-66 to only 8% in 1975-1976.<sup>17/</sup>

The same phenomenon occurred with regard to supplier credits (see again table 4.6). The most notable feature is that this type of credit, which with respect to other sources of finance was of less relative significance in the 70's, became dominated by the Centrally Planned Economies. Indeed, it was the greater role of these countries in both supplier credits and bilateral finance that most symbolized Peru's program of diversification.<sup>18/</sup>

As it turned out, the key actor in the drive for diversification<sup>19</sup> was commercial banks. These institutions also were the principal factor behind the dramatic rise in external finance available to the government after 1971. Next, it shall be seen why the radical change took place.

### 3. Commercial banks: their penetration of the Peruvian market

In 1971 Peru was faced with a severe dilemma. The government had just formulated an ambitious development plan designed to restructure the economy and generate rapid economic growth. Moreover, <sup>the</sup> public sector was to be the principal agent of development, sponsoring large investments in productive sectors. While much of the finance could be secured locally, foreign funds were clearly crucial for successful implementation. But the logical sources of supply of long term development loans - i.e. international and bilateral agencies - were relatively inelastic, both because of the aforementioned financial blockade and the institutional limits on funding from these institutions.<sup>19/</sup> Large scale direct foreign investment

obviously was not compatible with public policy. Thus, officials viewed foreign commercial banks as a potential source of external finance.

Indeed, some effort was made to court the banks' favor. As was seen earlier, throughout the reform period fiscal and monetary policy was conservative and good relations were maintained with the IMF. Also, commercial banks were not treated harshly in the reforms on private capital; major banks were allowed to keep their branches in Lima and those nationalized, such as Chase Manhattan received rather generous settlements.

Coincidental with Peru's desire to secure commercial bank finance was a maturation of a structural change in banking, underway since the <sup>late</sup> 1950's, that eventually would make these institutions more receptive to finance for developing countries. By 1971 banks were actively courting developing country clients, and Peru eventually got caught up in the wave of new lending to these countries. Given the importance of this event to Peru, it is worthwhile to take a relatively long digression and review just how banks became involved with developing countries.

a) A digression: the structural change in world banking

Prior to 1970 commercial banks were rather limited lenders to LDC's, their activity generally being restricted to short term lending for trade and occasional project loans that were protected by guarantees of export credit agencies such as the U.S. Export-Import Bank.<sup>20/</sup> However, this conservative posture hid some radical changes that were taking place elsewhere in world banking.

and would eventually culminate in bankers becoming a major source of finance for developing countries.

The change actually began in the United States in the 1950's when there developed a new breed of banker who was a "salesman at heart" and who would aggressively seek new business.<sup>21/</sup> The attitude was partly attributable to the high liquidity in banks during the 50's. However, more fundamentally, banking officials conditioned by the depression of the 1930's to conservative strategies were beginning to retire and "a whole new group of what was to become the 'go-go guys' of the 1960's were entering top management".<sup>22/</sup> Initially, U.S. banks focussed their expansion on domestic markets, as evidenced by the fact that prior to 1960 only 6 U.S. banks had foreign branches.<sup>23/</sup> However, the wheels already were in motion for a massive internationalization of American banking activities that would later be followed by banks in Europe, Canada and Japan.

The convergence of a number of factors promoted expansion abroad.

One key ingredient was the development of the Eurodollar market.

"The origin of the Eurodollar market can be traced back to the 1920s when U.S. dollars were deposited in Berlin and Vienna and converted into local currencies for lending purposes. These practices did influence the local money markets. After World War II, the U.S. dollar was designated

by the IMF as an intervention currency in the foreign exchange market. This established the common acceptability of the U.S. dollar as a key currency for international trade, investment, exchange arbitrage, and balance of payments settlements. The continuous balance of payments deficits of the United States resulted in a growth of official reserves assets in Western European countries, and their central banks looked for investment opportunities for short-term gains. In the 1950s, Russian banks in Western Europe preferred to place their holdings of U.S. dollars with British and French banks against the risk of possible seizure by the U.S. authorities in case of crisis. Under these circumstances, Eurobanks simply practiced the principles of free economy by establishing competitive spreads between creditor and debtor rates of interest. Some French banks extended U.S. dollars loans to Italian banks during the 1950s as typical operations in small amounts.24/"

And the market was an attractive place to do business; being essentially an offshore depository of foreign currencies, it was devoid of any regulation by national authorities. Thus, reserve requirements and other regulatory measures were absent, lowering the cost of banking operations and creating opportunities for enhanced profit-making.

The market's growth was given impulse by a series of other factors. In 1957, British banks were forbidden to finance trade for non-residents, thus making "offshore" deposits of the eurodollar market a convenient ~~\_\_\_\_\_~~

tool for evading the regulation. In 1958, Western Europe adopted full currency convertibility, which promoted trade in goods and currencies, thereby generating requirements for international finance. The same year the EEC was formed. Then in the 60's, when the U.S. government established a series of capital controls and interest rate regulations to stem its growing balance of payments deficit, U.S. banks found the Eurodollar market an essential source of funding for activities at both home and abroad.<sup>25/</sup>

While the existence of the Eurodollar market facilitated the expansion of international activities of U.S. banks, an important motivation for such overseas operation was the rise of U.S. direct foreign investment in Europe in the early 60's. In order not to lose their corporate clients,<sup>big money-center</sup> U.S. banks had to move abroad and lend abroad.<sup>26/</sup> As big banks increased their international lending operations, other/<sup>smaller</sup> U.S. banks were obliged to follow for competitive reasons. And in the face of expanding U.S. banks, European banks had to consider a more aggressive lending posture as well. To a lesser extent, Canadian and Japanese banks also had to respond defensively to the growing presence of the U.S. banks abroad.

While U.S. banks were at the vanguard of the growth of international banking, they also induced some major innovations that facilitated greater international lending. In the late 50s and early 60s lending out of the Eurodollar market usually was short-term (less than one year), reflecting the current nature of the deposit base. However, banks soon found that they could "purchase"

short term deposits on the market and, then, by continuously rolling them over on interest fixing dates, use these deposits to fund much longer term loans, 3-5 years being typical by the late 1960s.<sup>27/</sup> Of course this created considerable mismatching between deposits and loans, but the risk was considered minimal given what was perceived to be an almost automatic refunding of the loans every 180 days.

Another major innovation was the use of lending consortia or syndicates. Banks found that they could minimize their individual risk if a group of them joined together to form a loan, each taking on a participation.<sup>28/</sup> In this way banks could mobilize large amounts of money for a borrower, while at the same time keeping to modest proportions the exposure of any one institution. Moreover, the syndicate, by reducing the lending requirements of a bank on any given operation, facilitated the entry of smaller banks into the international arena.

By the latter half of the 1960s the expansion of world banking was becoming intense. An environment of rapid growth of world trade and investment generated new opportunities for foreign lending and many more banks set their sights on the development of an international portfolio. Moreover, the desire to lend abroad was stimulated by the fact that the aggressive attitude found in some U.S. banks in the early 50s was by now becoming more acute and generalized; the business psychology of the times in world banking was growth at all costs via the expansion of assets and the leveraging of capital. And



there was no better way to achieve this goal than by "going international" and tapping the deposits available in a fast growing Eurodollar market.<sup>29/</sup> As an indication of the growth taking place, one can look to the expansion of overseas branches of U.S. banks, which were at this time the most aggressive group of institutions. In 1965 there were 13 U.S. banks with 211 branches overseas; by 1970 the number has risen to 79 banks with 536 branches.<sup>30/</sup> This, of course, is a conservative indicator since it excludes from consideration foreign subsidiaries of U.S. banks.

Up to 1970, most medium term bank lending activity took place among the industrialized countries, although as early as the mid-1960s some lending had been going to developing countries, mostly large ones like Brazil and Mexico and often as a result of banks following investments by transnational corporations. But around 1970, lending to developing countries became more marked, and motivated by considerations broader than the need to service TNCs. Soon, thereafter the periphery was to become a major client of international banks.

The major reasons behind the lending to LDCs were excessive liquidity and competition, each of which fed upon the other. After 1970 successive waves of newcomers - notably U.S. regional banks and Japanese institutions - entered the international market in search of easy profits and the freedom of operation of a non-regulated market. This tended to further fuel international liquidity, which already had been growing rapidly.

"The size of Eurodollar pool grew steadily, fed partly by the continued U.S. deficits but also by deposit creation on the part of proliferating financial institutions. Each U.S. bank branch and consortium bank established in London enlarged the Eurodollar pool by depositing their deposits with each other, thereby creating new deposits. Moreover, the increased number of financial institutions created an ever greater will to lend as each institution sought to build a portfolio."<sup>31/</sup>

Perhaps the main factor that initiated the drive in LDC markets was the 1970-1971 recession in the Center; with loan demand depressed in the industrialized countries, some aggressive banks turned to the periphery in search of new clients. Such a strategy proved attractive because many developing countries appeared to be better risks at this time as they had achieved high growth rates and sound balance of payments positions on the strength of the opening up of world trade in the 60's. Another attraction was that loans to governments - usually the principal entrepreneur in developing countries - were seen as being particularly secure because, unlike corporations, governments do not go bankrupt and therefore are always available to service their loans.<sup>32/</sup> Finally, loans to LDC governments were especially profitable because borrowers were disposed to pay risk premiums of 2% or more over base interest rates in order to secure bank credit.

The initial flow of lending to LDC's was concentrated in the more advanced countries like Brazil. However, as competition pushed more banks into the periphery the base of lending expanded.

"... competitive pressures became so hectic that banks - many of them new entrants into the international scene - saw their lending spill over into the smaller, less-developed countries of the region; countries traditionally accustomed to obtaining capital from official sources found the Eurocurrency market to be a more than willing supplier of funds. Indeed, by 1972 countries had discovered it to be a borrower's paradise; not only was there easy access to credit, but competition caused margins to be drastically reduced and maturities to reach unprecedented lengths. By way of example, Brazil, which was a leading borrower within the developing world, found that it could regularly secure credits with a 10-15 year maturity. As for spreads, they declined from 2 1/4% in 1971 to 1 1/2% in mid-1972 and 3/4-1% in 1973. At the same time lending was so voluminous that the country even found it necessary to introduce policies to discourage foreign bank loans."<sup>33/</sup>

When the OPEC petroleum price rise took place in late 1973, the banks became even more eager to lend, although the motivation behind the loans changed somewhat. Flooded with deposits from the OPEC surplus, banks simply had to turnover the funds in the form of new loans. Of course, developing countries, facing the sharply increased cost of petroleum (and other commodities such as food) were willing clients; after all, they had to avoid a radical balance of payments adjustment and more appropriate sources of long term finance were unavailable due to the industrialized countries' failure to organize an official mechanism for the recycling of the OPEC surplus.

Some bankers have tried to paint their role in lending to LDC's during this period as simply a response to the demand of these countries for finance, in other words lending was "demand driven".<sup>34/</sup> This is simply a half truth which it is important to clarify here.

While developing countries no doubt had a strong demand for resources, banks were just as eager and in some cases even more eager to lend; there clearly was a bandwagon effect in lending as banks bitterly attempted to stay ahead of their competitors. Indeed, the general strategy during this expansive period of banking on at least one occasion has been characterized as a "glad-handed, name-your-price approach" to lending.<sup>35/</sup>

But perhaps more importantly, bankers, in their desire to build up portfolios, often were lax in their evaluation of such matters as the use of credit, facility for maturity transformation and medium term ability of a country to generate foreign exchange to service debt.<sup>36/</sup> This problem was particularly acute in the 1972-1974

when the new entrants to international banking mostly were small-and medium-sized institutions which had a willingness to lend that far exceeded their capacity to evaluate credits.<sup>37/</sup>

The euphoric and rather haphazard expansion of banking ended abruptly in 1974 when a series of bankruptcies shook up the world banking industry. The failure having the greatest impact was that of Bankhaus I.D. Herstatt of Germany in June in which losses on foreign exchange operations were reported at more than 160 million dollars.<sup>38/</sup> International bankers then panicked and quickly reviewed their international lending policies. Behavior became "reactive and conservative". As a manifestation of the caution that prevailed it can be seen in table 4.7 that lending to developing countries slowed down dramatically in the second half of 1974. Moreover, margins on loans to developing countries shot up to 1 1/2 - 1 3/4% and available maturities were considerably shortened.

Lending remained depressed in early 1975. By the second half of the year bankers realized that they had to renew the flow of loans to LDC's; on the one hand they still were flush with OPEC deposits, while on the other their preferred clients in the industrialized countries were seeking relatively little credit as a result of the deep recession in the Center. Thus, as seen in table 4.7, bankers boosted their lending to developing countries. However, they were much more selective with regard to whom they granted loans. Furthermore, the terms of lending became particularly onerous. By the second half of 1975 many developing countries had to accept margins of 2% or more. With regard to maturities, less than 20% of all publicized credits to LDCs had a term in excess of 6 years, compared to 76% in 1974. As for loans with a maturity of more than 10 years, they virtually disappeared from the market-place.<sup>39/</sup>

Table 4.7

PUBLICIZED EUROCURRENCY CREDITS TO NON-OIL EXPORTING DEVELOPING COUNTRIES

(Billions of dollars)

1973	1974				1975			
	I	II	III	IV	I	II	III	IV
6.1	2.3	3.0	1.4	1.6	1.1	2.0	2.5	2.9

Source: IBRD, Borrowing in International Capital Markets, first quarter 1975, May 1975; fourth quarter 1975, February 1976.

b) Commercial banks penetrate the Peruvian market

It has been seen that the bank lending began to take on importance in Peru in 1972. It comes as no coincidence that the date of entry closely corresponded to the time when much publicity was being aired about petroleum in the Peruvian Amazon. Moreover, banks undoubtedly were in a position to be informed about these developments because many \_\_\_\_\_ banks had close ties with corporations drilling in the jungle fields. But it should be pointed out that given the frantic nature of lending in the early 70's, Peru probably would have become a \_\_\_\_\_ client of banks with or without petroleum.

After 1972 lending to Peru picked up at a pace commensurate with the rhythm \_\_\_\_\_ of global bank expansion. By 1974 net disbursements by these institutions were 400 million dollars, nearly 7 times the level recorded in 1972 (see again figure 4.1); the banks' share of net flows of loan capital to the government rose over the same period from 34% to 61% of the total.

Furthermore, there is evidence that bankers were highly aggressive in their penetration of the Peruvian market. Unsolicited letters offering lines of credit on highly favorable terms were frequent as were foreign bankers' visits to Lima for the purpose of generating interest in new loans.<sup>40/</sup> At its zenith, offers for finance were intense; as one local financier remarked: "foreign bankers wanted to give us money before we asked for it."<sup>41/</sup>

One has already seen that the public sector's debt control system was not well constructed / <sup>to</sup> resist internal pressures to borrow abroad;

the aggressive attitude of bankers between 1972-1974 further burdened the effectiveness of the control system. It comes as little surprise then that a country with a current dollar per capita income of only 800 dollars in 1974<sup>42/</sup> was able to accumulate by the end that same year 1.1 billion dollars in disbursed and committed medium term bank debt,<sup>43/</sup> equivalent to roughly 75 dollars per habitant. Relatively speaking, Peru also became important to the banks; by 1975 it ranked among the top 7 non-oil developing countries that had borrowed from banks.<sup>44/</sup>

Figure 4.1 shows that despite the retrenchment that took place in world banking in the first half of 1975, net disbursements from these institutions rose slightly that year. Much of this disbursement represents the forward momentum generated by the hectic pace of lending in earlier years. But from there on out banks would take a much more restrictive attitude towards lending to the government.

#### D. 1976: Peru loses its creditworthiness

The newly conservative attitude of bankers in late 1974-1975 continued to dominate international lending in 1976. Terms of loans remained very onerous and banks tended to favor countries that, in their view, were trying to adequately adjust their balance of payments. Peru, of course, at this time clearly had severe external problems and was relatively slow in taking measures to adjust its balances of payments. But the new economic team installed in September of the previous year apparently was able to generate enough confidence to maintain the flow of bank credit, albeit at levels considerably inferior to 1974-1975. Indeed, authorities were able to convince banks to extend



400 million dollars in support of the June stabilization program  
- and this was done without the protection of an IMF standby agreement.  
This credit, however, proved to be the end of the honeymoon between  
Peru and international bankers and from thereon relations between the  
two parties underwent serious deterioration. At the close of the period,  
Peru's disbursed and committed external debt to banks had reached nearly  
2 billion dollars.

### III. Summary

One has just seen that in the early and mid-sixties the public sector of Peru had been basically reliant on suppliers' credits. This situation developed out of the fact that suppliers' credits were the only elastic source of external finance for the government. Commercial suppliers were ready with finance to support sale of their goods. On the other hand the government found the technical requirements of multilateral financial institutions to be burdensome vis-a-vis the limited administrative capacity of public authorities; major sources of bilateral finance (e.g. USAID) had been restricting their credit flows to the government because of uncertainty over local treatment of foreign investors, and private commercial banks simply were not accustomed to regularly extending medium term finance to LDC governments. The nature of resource flows in the mid-60's created a debt structure for Peru in which there was a relatively high profile for commercial suppliers and a low representation of official concessionary finance. The cost and tenor of debt reflected the quasi-commercial terms offered by foreign suppliers.

During 1967-1968, the profile of banks began to rise slightly due to their loans for the country's fiscal and balance of payments deficits. But then with the change in government in late 1968, almost all external finance to the government was cut off as a response to investment disputes arising from nationalization of foreign firms. The financial boycott was quite severe up through 1971. But thereafter

Peru gradually began to regain access to new credit. There were a number of reasons for this. One was the discovery of petroleum in the jungle which made Peru strategically important to the political powers in the center. Another was Peru's able management of economic affairs and its drive to diversity economic relations, thereby increasing interface with countries outside the scope of the boycott. But most importantly, structural changes in World banking had made commercial banks eager lenders to LDC governments and many banks saw Peru as a new market in which to expand business. The penetration began in 1972 and intensified in succeeding years, with the cost of credit declining in a commensurate fashion. By 1975 Peru was a major client of the banks and the government was heavily indebted with these institutions. Things became more difficult in 1976, however. Banks had turned generally less enthusiastic about loans to LDCs and Peru's economy was showing severe signs of strain. Commercial lenders agreed very reluctantly to refinance Peru's debts in 1976, but on very onerous terms. The country was now a "problem" and relations with commercial bankers were to deteriorate further in the post 1976 period.

Footnotes

Chapter 4

1. See IDB, table 2.
2. Kuczynski, p. 95.
3. Export-Import Bank finance as well as that of other agencies was unaffected. A good account of how the freeze evolved is found in Levinson and De Onis, pp. 146-156.
4. Ibid., pp. 151-153.
5. Pinelo, p. 132.
6. Ibid., pp. 132-133. Also see Kuczynski, pp. 156-160 and Levinson and De Onis, pp. 154-155.
7. Kuczynski, p. 58.
8. The loan was originally signed in late 1964 and then amended in early 1965. The credit, for the purposes of this study, has been classified a 1964 loan and therefore is not part of the data base that is used for analysis in later chapters. However, the loan was refinanced in 1966 and this does appear in the data base.
9. Kuczynski, p. 100.
10. Levinson and De Onis, p. 144.
11. The quote is the author's translation and is taken from a speech given by the President of Peru to the assembly at the 12th Annual Meeting of Governors of the IDB in Lima, Peru during May 1971. See IDB (1971), pp. 22-29.
12. See U.S. Treasury, p. 283.
13. U.S. Treasury, pp. 173-174.
14. This latter point is made in Fitzgerald, p. 68.
15. A guarantee of 1.4 million dollars was given for a complementary private credit.
16. This strategy was an explicit part of the 1971-1975 economic plan. See INP, p. 47.
17. The U.S.'s share of trade also declined markedly. Exports to the U.S. fell from 34% of the total in 1965 to 24% in 1976. Imports over the same period fell from 40% to 35% (IMF).

18. For a detailed analysis of the economic and financial relations between Peru and the centrally-planned economies see Estremadoyro.
19. Official aid finance had shown no real growth since 1965. See OECD, p. 153.
20. It should be noted that bank lending to Latin America was considerable in the first quarter of the century. However, after the financial collapse of 1929 banks retreated to a very conservative posture with regard to lending to developing countries. See Davis, p. 20.
21. Hayes, pp. 33-34.
22. Aronson, (1975), p. 16.
23. Robinson, p. 198.
24. Lees and Eng, p. 435.
25. See Aronson (1977) Chapter 4 for an informative review of the controls and their impact on bank behavior.
26. Robinson probably has one of the best examinations of the expansion of U.S. banks abroad. Another comprehensive source of information on the foreign operations of U.S. banks is found in the FINE study of the U.S. House of Representatives (1975 and 1976). Also see Lissakers.
27. Robinson, p. 254. For a good description of the transformation process, see Wellons (1977), p. 26.
28. For a good description of how syndicates are formed see MIOSSI.
29. See Ganoë.
30. See U.S. House of Representatives (1976), p. 79.
31. Weinert (1973), p. 35.
32. For a discussion of this fact, see Iglesias, pp. 96-97. Also see Weinert (1978).
33. Devlin (first half of 1978), pp. 77-78.
34. See Friedman, p. 48 and Watson, p. 27.
35. Wall Street Journal as quoted in Hayes, p. 49.

36. See Cummings.
37. See Wellons (1977), p. 24. Also see Weinert (1973), p. 35.
38. See Aronson (1975), p. 22. There were other problems as well. In October Franklin National Bank of New York went bankrupt after many months of support from the U.S. Federal Reserve. In the same month Banque de Bruxelles, Union Bank of Switzerland and Lloyds of London announced large losses on foreign exchange operations. See Lissakers, p. 24.
39. See table 8 in IBRD, fourth quarter, 1975 (February 1976).
40. This observation is the result of the author's field research in Peru.
41. See Everett Martin.
42. The source of this figure is CEPAL. At 1970 prices per capita income in 1974 was roughly 600 dollars. See Cepal, Economic Survey for Latin America 1977.
43. See BID table 42.
44. Includes short term obligations. See Morgan Guaranty Trust Company, September 1976, p. 11.

Chapter 5

BANK LENDING TO PERU: AN INTERTEMPORAL COMPARISON, 1965-1970 AND 1971-1976

The last chapter provided some limited flavor of the role of commercial banks in the external finance of the public sector; however, the analysis was very general and provided little insight into the nature of the banks' involvement in Peru. It will be the task of this chapter to begin the gradual process of penetration of aggregate data that is the raison d'etre of the whole study. Chapter 5, through the use of an intertemporal comparison, will attempt to indicate how actors, relationships and functions changed radically between 1965-1970 and 1971-1976. The former time frame is reflective of a traditional period, i.e., when bankers' interests basically were focussed on the industrialized countries and medium term lending to LDCs was an exception rather than a rule. Banks involved in Peru prior to 1971 then might be considered to be the country's traditional lenders. The second period, of course, is reflective of the effects of the boom years of world banking when there was a wholesale expansion into markets of developing countries. Here the stage is shared between the traditional banks of the first period and the aggressive newcomers of the 1970's. One will see that the changed environment also brought fundamental changes in relationships and lending activities. The following pages will shed light on which banks have lent to Peru over the two periods; the various modes of credit extension; how interest rates, maturities and penalties on their loans evolved; the relative importance of the various types of loans (e.g. projects, refinance, free disposition, etc.) in total lending as well as the terms carried by each; where loans were booked by the banks; currencies employed; and the degree to which restrictive clauses such as waivers of sovereign immunity and local legal jurisdiction were employed in loan agreements.

#### A. THE ACTORS: PERU'S PRINCIPAL COMMERCIAL LENDERS

Table 5.1 displays the government's principal lending banks for the periods 1965-1970 and 1971-1976. Institutions are broken out into six groups according to the relative importance of the banks, using as a criterion the gross amount of all authorizations for each period.<sup>1/</sup> One can consider the first three groups of banks as Peru's major commercial lenders; the next two groups as of intermediate importance and the last group as relatively minor lenders at the institutional level.

Several things are immediately striking about the data within and between periods.

In the earlier period, the predominant lending institutions were almost exclusively from the United States. This is seen in the fact that of the first 5 of the 6 groups of commercial banks, only one was of a non-U.S. character, that being the Bank of Nova Scotia of Canada.

Another characteristic of the period is that Peru's commercial lenders tended to be large in size. Major lenders (groups 1-3) were clearly superbanks, ranking in size among the top 22 of the world's largest banks. Moreover, all these institutions were relatively well-experienced in international lending and could be called money center banks, i.e., at the hub of world commercial finance. Those banks of intermediate importance as lenders also were relatively large in size, ranking between 39 and 78 in the top 300 of world banking. However, unlike the major lenders, these institutions generally were not at the vanguard of international finance at this time.

A final observation that one can make about this first period is that a handful of institutions were responsible for the bulk of the lending. As seen in table 5.2 the 6 U.S. superbanks in the top 3 groups accounted for over 70% of the total value of commercial bank loans authorized in the period. Thus, the public sector displayed a high degree of dependence on a few key U.S. banks.



Table 5.1

PERU: MAJOR COMMERCIAL BANK LENDERS GROUPED ACCORDING TO THE AMOUNT AUTHORIZED, 1965-1970 AND 1971-1976 <sup>a/</sup>

1965-1970			1971-1976		
Lendings banks and amounts authorized in millions of dollars <sup>b/</sup>	Country headquarters of bank	International ranking of bank <sup>c/</sup>	Lendings banks and amounts authorized in millions of dollars <sup>b/</sup>	Country headquarters of bank	International ranking of bank <sup>c/</sup>
<u>Major lenders</u>					
1. <u>&gt;45 and &lt;55</u> Bankers' Trust Citicorp Manufacturers Hanover	United States United States United States	11 2 5	1. <u>&gt;123 and &lt;150</u> Citicorp	United States	2
2. <u>&gt;35 and &lt;45</u> Chase Manhattan Continental Illinois	United States United States	3 22	2. <u>&gt;95 and &lt;123</u> Manufacturers Hanover <sup>d/</sup> Wells Fargo	United States United States	16 69
3. <u>&gt;25 and &lt;35</u> Bank of America	United States	1	3. <u>&gt;68 and &lt;95</u> Bank of America Chase Manhattan	United States United States	1 4
<u>Intermediate lenders</u>					
4. <u>&gt;15 and &lt;25</u> Bank of Nova Scotia	Canada	47	4. <u>&gt;41 and &lt;68</u> Bank of Nova Scotia Bankers Trust Continental Illinois Morgan Guaranty Crocker National Bank Dresdner Bank Banco de Brasil <sup>e/</sup> Royal Bank of Canada	Canada United States United States United States United States Germany Brazil Canada	53 32 30 19 79 14 12 22
5. <u>&gt;6 and &lt;15</u> Charter New York Corporation Crocker National Bank First National Bank Boston Franklin National Bank National Detroit Corp.	United States United States United States United States United States	39 48 59 78 57	5. <u>&gt;16 and &lt;41</u> Banca Commerciale Italiana Bank of Tokyo Lloyds Bank Franklin National Bank Union Bank of Switzerland National and Commercial Banking <sup>f/</sup> Banca Tristate Corp. Banca Nazionale del Lavoro Long Term Credit Bank of Japan Credit Lyonnais <sup>f/</sup> Banque Francaise du Comm. Exterieur <sup>f/</sup> Canadian Imperial Bank of Commerce Fugji Bank Amro Bank <sup>f/</sup> First Pennsylvania Corp. Deutsche Bank Bank of Montreal Chemical Bank First Chicago Corp. Security Pacific Corp. Commerzbank A.G. American Express Int. Toronto Dominion Bank	Italy Japan United Kingdom United States Switzerland United Kingdom United States Italy Japan France France Canada Japan Holland United States Germany Canada United States United States United States Germany United States Canada	24 28 31 ... 41 102 199 20 44 7 174 29 13 48 106 6 45 23 35 54 26 223 66
<u>Minor lenders</u>					
6. <u>&lt;6</u> See table A5.1 in the statistical appendix for the names of the 15 banks in this group			6. <u>&lt;6</u> See table A5.1 in the statistical appendix for the names of the 131 banks in this group		

Sources: CEPAL on the basis of official data.

<sup>a/</sup> For credits with and without an export credit guarantee.

<sup>b/</sup> The range of authorizations in each group are different for the two periods due to the much greater value of loans in 1971-1976. However, the scaling of the values for each group have been done in such a way that 1971-1976 is proportional to 1965-1970.

<sup>c/</sup> Ranked on a scale from 1-300 in world banking. Size is based on assets; 1965-1970 uses asset size for 1969 as published in *The Banker*, June 1970, p. 596; 1971-1976 uses asset size for 1975 as published in *The Banker*, June 1976, p. 645.

<sup>d/</sup> If credits with export credit guarantees were excluded, would fall into group 3.

<sup>e/</sup> If credits with export credit guarantees are excluded, would fall into group 5.

<sup>f/</sup> If credits with export credit guarantees are excluded, would fall into group 6.

Table 5.2

PERU: DISTRIBUTION OF TOTAL AUTHORIZATIONS AMONG MAJOR, INTERMEDIATE  
AND MINOR LENDERS, 1965-1970 AND 1971-1976<sup>a/</sup>

(Percent)

	Major lenders	Intermediate lenders	Minor lenders	Total
1965-1970	71.7	17.4	10.9	100
1971-1976	23.0	46.8	30.2	100

Source: CEPAL, on the basis of official data.

<sup>a/</sup> Lending groups correspond to those of table 5.1.

This might be a manifestation of an unsophisticated borrower content with a cozy relationship with a coterie of convenient and familiar institutions. Indeed, Kuczynski has hinted that in the 1960's the public sector was unfamiliar with non-U.S. banks and visa versa. 2/

Turning to the second period, 1971-1976, one can see that there was a rather dramatic change in the sources of private bank credit.

Table 5.1 shows that in terms of major lenders, groups 1-3 continue to be dominated by very large U.S. banks. However, Bankers Trust and Continental-Illinois, major lenders in 1965-1970, slipped to an intermediate level of importance in 1971-1976. There also is a newcomer to the group of major lenders—Wells Fargo. The role of this bank in Peru's finance is very important and will be discussed in greater detail in later chapters.

While the group of major lenders in 1971-1976 is still—with the exception of Wells Fargo—from the same club of U.S. money center banks that stood out as important lenders in the earlier period, the intermediate groups of lenders (4 and 5) are characterized by many new actors and a much greater geographical dispersion. The only banks from the intermediate group of 1965-1970 that maintained their relative importance in the second period are Crocker National Bank, the Bank of Nova Scotia, and Franklin National (which no longer exists due to bankruptcy in 1974). However, it is significant that they are joined by many other banks from the U.S., Canada, Japan, Europe and even one bank from South America. The one characteristic that is common to the two periods is that the banks in the intermediate group continue to be rather large in size; with the exception of the National and Commercial Banking Group, Bancal Tristate Corporation, Banque Francais du Commerce Exterieur, American Express and First Pennsylvania Corporation, all the banks are within the top 79 of world banking.

With regard to minor lenders (group 6) their number increased dramatically, from only 15 banks in 1965-1970 to 131 banks in 1971-1976. There is probably

no better indicator than this to show the massive transformation of banking in the 1970's.

Perhaps the most dramatic change between the two periods is that unlike 1965-1970, when the major lenders also were responsible for the bulk of total lending (72%), in 1971-1976 these same lenders accounted for only 23% of the total credits authorized (see table 5.2). The massive influx of new actors in the 1970's, whose lending was of an intermediate or minor importance at the institutional level, in the aggregate accounted for more than three-fourths of the value of all loans in the period. Intermediate lenders accounted for 47% of total authorizations, compared to only 17% in 1965-1970. Meanwhile, the 131 banks categorized as minor lenders—some of whose authorizations did not exceed \$1 million for the period—as a group accounted for nearly a third of total lending, compared to only 11% in the earlier period. Thus, in the changed environment of the 70's, important lending came from many new sources.

The much greater importance of intermediate and minor lenders as agents of finance might suggest greater independence for Peru as a borrower. This is undoubtedly true to some degree. However, as will be seen from the next chapter on syndication, one can overstate the degree of independence by merely focussing on the number of individual actors in Peru's external commercial finance.

#### 1. Grouping banks according to country of origin

Shedding more light on the subject is table 5.3, which provides another view of the sources of commercial lending. Here data and loans are grouped according to the country of origin of the lending bank; in addition, for each country group one finds data on the number of lending institutions, their average size, and the number of credits extended for the period.

These data confirm the overwhelming presence of American banks in Peru's commercial finance in the mid and late 60's. Fully 86% of the value of all loans came from banks whose home office was located in the U.S. The lending

Table 5.3

PERU: COMMERCIAL BANK AUTHORIZATIONS ACCORDING TO COUNTRY OF ORIGIN, 1965-1970 AND 1971-1976 a/

Country of banks	Percentage of total loans authorized	Number of institutions <u>b/</u>	Average size <u>c/</u>	Number of credit transactions
<u>1965-1970</u>				
United States	86.1	14	5	49
Japan	0.1	1	26	1
Canada	7.8	3	42	5
United Kingdom	1.5	2	74	5
Germany	1.1	1	14	1
France	-	-	-	-
Italy	1.0	1	25	3
Switzerland	-	-	-	-
Other	-	-	-	-
Consortium	1.0	2	301 <sup>c/</sup>	2
Unknown <u>d/</u>	1.2	3	...	5
<u>Total</u>	<u>100.0</u>	<u>27</u>	<u>5</u>	<u>71</u>
<u>1971-1976</u>				
United States	45.3	42	17	196
Japan	11.6	26	41	160
Canada	10.2	6	46	61
United Kingdom	6.5	11	54	41
Germany	6.4	11	18	27
France	4.3	6	43	39
Italy	2.1	8	30	24
Switzerland	2.5	7	54	15
Other	7.5	24	53	58
Consortium	3.5	23	301 <sup>c/</sup>	48
Unknown <u>d/</u>	0.2	1	...	3
<u>Total</u>	<u>100.0</u>	<u>167</u>	<u>27</u>	<u>672</u>

Source: CEPAL on the basis of official data.

a/ All credits, i.e., with and without guarantees of an export credit agency.

b/ Subsidiaries have been consolidated into parent.

c/ Ranked according to asset size on the basis of The Banker's top 300 in world banking. The period 1965-1970 uses asset data for 1969 and 1971-1976 uses asset data for 1975. The country average was calculated by weighting the asset size of each bank in dollars by the amount authorized in each period. The resulting average asset size was then assigned a rank according to where it placed in the top 300 of The Banker's. A rank of 301 is used to indicate an average asset size too small to be ranked in the top 300. Banks whose origins are unknown, of course, received no ranking and do not figure in the overall averages. Since the number of unknown banks is small, and their weight insignificant, the absence of these banks in the ranking exercise had little effect on results.

d/ Banks whose national origin could not be identified.

came from 14 U.S. institutions, equivalent to slightly more than half of the total number of banks lending to Peru in this period. Moreover, given the concentration of lending in the hands of a few very large banks, the weighted average size (ranked by assets) of U.S. institutions relative to the top 300 in world banking was a very large five.

The only other country with a significant presence was Canada, whose commercial banks accounted for 8% of the loans authorized. This lending was carried out by three institutions whose weighted average asset rank was 42.

All together there were 27 lending institutions for the first period, and due to the dominance of big U.S. institutions, the weighted average size corresponded to the same size as that of the U.S. banks.

In the 1970's one sees much greater dispersion in all senses. The total number of lending institutions jumps to 167, six times the number of participating institutions in the 60's. Reflecting the greater number of banks of all sizes, the average size of lending institutions falls from 5 to 27. A rank of 27, however, indicates the continued importance of large institutions.

Likewise, the weight of U.S. banks in total authorizations declines by nearly half, while Japan, the United Kingdom, Germany, France and "other" areas take on much higher profiles. Nevertheless, the U.S. participation remains 4 times the size of the next most important country group (Japan). Thus, the U.S. continued to dominate with the difference that hegemony was considerably less intense and shared among 42 instead of just 14 institutions. 3/

It is interesting to note that the nature of the role of U.S. banks is at least partially consistent with the general notion that in the sixties commercial banks basically followed national trade and investment flows. The overwhelming dominance of U.S. institutions in 1965-1970 conforms with the high profile of American firms as investors in Peru—as was seen in Chapter 3, 80% of all foreign direct investment was sourced from the U.S. This country also was a metropole for trade, being a source for 40% of Peru's exports and 37% of its imports. The

maximum trade captured by any other country was slightly more than 10% (see table 5.4). If general patterns were followed, it is likely that U.S. banks were predominant in servicing the trade and investments of American firms with Peru. Thus, the Peruvian market was highly familiar terrain to some U.S. banks. Lending to the government could then be seen as being consonant with protecting the business of their corporate clients and therefore the business of the banks themselves.

Another factor behind the dominance of U.S. banks in this early period undoubtedly is the fact that in the 1960's these institutions were easily the most experienced overseas lenders. They also tended to have a very large resource base; of the top 11 banks (ranked by assets) in world banking in 1969, 8 had their headquarters in the U.S. 4/

The reduction in the role of U.S. lending institutions in 1971-1975 is consistent with their lower profile in investment and trade in this period. Although it would be difficult to empirically position the U.S. as investor in Peru, it is generally felt that divestment in the reform period, coupled with increased activity of European and Japanese firms provided for greater geographical dispersion of foreign investors. Table 5.4 also shows a significant decline in the U.S.'s trade share. However, two factors suggest that forces other than trade and investment were at play in the behavior of bank flows: (i) the decline of the U.S.'s share of lending is much more severe than its reduced role in trade and probably more severe than any decline that might have occurred in its share of foreign investment; and (ii) the relative change in importance of Japanese and European countries as commercial lenders generally is not proportional to the behavior of their shares in trade. (No data are available on investment flows.) These trends would be consistent with analysis presented in Chapter 4 that established conditions in which banks in the early 70's expanded lending to developing countries, and Peru, for its own sake, i.e.,

Table 5.4  
PERU: DIRECTION OF TRADE  
(Percentage)

Country	1965-1968		1972-1975	
	Exports	Imports	Exports	Imports
United States	40	37	32	32
Japan	12	7	14	10
Germany	11	12	8	11
France	2	2	2	2
United Kingdom	3	5	3	4
Canada	-	3	-	4
Other	32	34	41	37
<u>Total</u>	<u>100</u>	<u>100</u>	<u>100</u>	<u>100</u>

Source: CEPAL on the basis of official data.



the principal consideration was development of an international portfolio and not service or protection of business with home country non-financial corporations.

## 2. Grouping banks according to their size

Mention has been made several times about the size of the banks lending to Peru. In order to clarify this point it is useful to view separately how gross authorizations were distributed among banks when they are grouped according to their size. Table 5.5 provides such information by breaking out total authorizations according to eight groups of banks, where each group represents a range of total assets denominated in U.S. dollars.

The table gives impressive evidence of Peru's dependence on very large commercial banks. In 1965-1970, 78% of the total value of authorizations were derived from banks in the two largest ranges of assets, which were equivalent to numbers 1-38 in the international rankings. In the second period, 1971-1976, 59% of the gross value of authorizations came from the top two groups, this time equivalent to numbers 1-46 in the international rankings. <sup>5/</sup> Thus large institutions clearly dominated commercial lending to the government.

One does see, however, some significant differences between the periods. In 1971-1976 there are both absolutely and relatively more institutions in the first two ranges of assets; for 1965-1970 there are 13 banks in groups 1 and 2, representing nearly 50% of all lenders, while in the second period the two top groups incorporate 42 banks that represent only 25% of all institutions. Likewise, in the second period the intermediate—and small—sized banks are of relatively more importance, both in terms of their number and the value of their authorizations.

In the 70's, then, there clearly was greater dispersion of lending, both within the group of large banks and among the groups of all banks ranked according to assets. But this does not diminish the fact that among the 167 lenders to Peru in 1971-1976, 42 very large institutions had great influence over the government's external resource flows.

Table 5.5

PERU: COMMERCIAL BANK AUTHORIZATIONS ACCORDING TO THE ASSET SIZE OF BANKS, 1965-1970 AND 1971-1976

Asset range <u>a/</u> (millions of dollars)	Equivalent world rank (1-300) <u>b/</u>	Number of banks in study	Percent of credits <u>c/</u>
<u>1965-1970</u>			
1. 25 573 - 12 787	(1- 5)	3	33.2
2. 12 786 - 6 394	(6- 38)	10	44.6
3. 6 393 - 3 197	(39- 76)	6	16.2
4. 3 196 - 1 599	(77-137)	2	2.9
5. 1 598 - 800	(138-254)	1	0.9
6. 799 - 706	(265-300)	-	-
7. <706	(> 300)	1	0.8
8. Unknown size		4	1.5
<u>All banks</u>		<u>27</u>	<u>100.0</u>
<u>1971-1976</u>			
1. 65 789 - 32 895	(1- 10)	8	17.6
2. 32 894 - 16 448	(11- 46)	34	40.9
3. 16 447 - 8 244	(47- 91)	25	18.5
4. 8 223 - 4 112	(92-147)	24	7.7
5. 4 111 - 2 056	(148-263)	21	6.9
6. 2 055 - 1 634	(264-300)	4	0.7
7. <1 634	(> 300)	26	5.1
8. Unknown size		25	2.6
<u>All banks</u>		<u>167</u>	<u>100.0</u>

Source: CEPAL on the basis of official data.

a/ While the asset range for the two periods involve different dollar values, the range for 1971-1976 is scaled in a manner which is proportional to 1965-1970. The asset range for 1965-1970 is from balance sheet data for 1969 and the range for 1971-1976 reflects data for 1975.

b/ The world ranks are on a scale of 1-300 and correspond to the asset range for each period. Based on The Banker ranking of the top 300 in world banking for the years 1969 and 1975, respectively.

c/ All credits, i.e., with and without guarantees of export credit agencies.

## B. ORGANIZATION OF CREDIT

During the first period, 1965-1970, banks extended credit on an individual basis, providing the impression that finance was a rather personalized affair, i. e., the public sector had direct contact with its bankers.

While banks lent individually, it was not uncommon, however, for them to band together in the extension of a credit. Such multibank loans accounted for roughly 68% of the value of authorizations in 1965-1970.

Multibank loans were characterized by a common umbrella loan agreement. However, no bank was explicitly identified as the organizer of the credit, 6/ nor was any bank designated to administer or enforce the loan over its duration. Likewise, no explicit fees were charged for organization or administration. Thus, each bank disbursed on its own and repayments were channeled directly to each institution. Presumably the attraction of these multi-institutional agreements were three fold: (i) a larger amount of resources could be mobilized, providing less risk for each individual bank; (ii) by joining into a group the banks became all that more imposing to the borrower, thereby enhancing leverage during both the negotiation and enforcement periods of the credit and (iii) group lending provided psychological security, i. e. a bank could enjoy the comfort of knowing that its peers were accompanying it in taking on a certain risk.

The multibank loans to Peru had no international character in the sense that all the banks were from the same country. Moreover, the number of institutions joining together in a loan did not exceed 11 on any one agreement.

The multibank credit of the 60's was a precursor of the syndicated credit that became commonplace in the 70's and was responsible for generating nearly 80 percent of the total authorizations in 1971-1976. In a syndicated credit a

lead bank(s) initiates negotiations with a borrower and solicits participations from other institutions. Thus, in the age of syndication a bank's importance to a borrower can go beyond the mere level of its loan authorizations.

Once a loan is arranged, one of the lead banks is designated as agent for the other participating banks and has responsibility for administration of the credit, e.g., making disbursement and receiving repayment. The agent also is responsible for enforcement of the credit agreement should the borrower fail to comply with the terms of the contract. <sup>2/</sup> Both the lead banks and the agent receive special fees for their services. And it also has become a practice to give fees to other banks as inducement for them to participate in the syndicate. Syndicates generally have some international flavor, as banks of various nationalities often cooperate in the arrangement of a loan. The attraction of a syndicate to a bank is similar to the attraction of the aforementioned multibank agreements with one additional incentive: the existence of fees which increase the yield on any given loan. Chapter 6 will analyse syndicates in some detail in order to reveal their nature and to see what advantages such arrangements have for the borrower.

### C. TERMS OF CREDIT

With regard to interest charges and maturities of commercial bank loans without external guarantors, they are presented in tables 5.6 and 5.7 for the two basic periods being examined.

#### 1. Interest rates

##### 1965-1970

As can be seen, the most prevalent way of costing loans in 1965-1970 was by use of a floating prime rate, i. e., a spread or margin added to an interest rate for prime borrowers that was subject to periodic adjustment. Fully 81% of the total value of authorizations was costed via the use of this

Table 5.6

## PERU: INTEREST RATES ON COMMERCIAL BANK LOANS, 1965-1976a/

	1965	1966	1967	1968	1969	1970	1965- 1970 average	1971	1972	1973	1974	1975	1976	1971- 1976 average
<b>1. Percentage of loans w/prime rate spread b/</b>	-	73.6	78.2	82.3	-	100.0	80.8	-	4.2	2.1	4.6	0.5	6.0	2.5
Average spread (%)	-	1.50	1.75	1.75	-	1.75	1.72	-	1.91	1.04	1.11	1.75	1.58	1.42
<b>2. Percentage of loans w/libor spread</b>	-	-	-	8.7	-	-	3.4	100.0	84.1	94.8	92.6	99.5	94.0	94.1
Average spread (%)	-	-	-	1.74	-	-	1.74	2.25	2.08	1.67	1.14	1.79	2.17	1.75
<b>3. Percentage of loans w/fixed interest rate</b>	100.0	26.4	21.8	9.0	100.0	-	15.8	-	-	3.1	2.8	-	-	1.3
Average rate (%)	6.30	8.20	8.10	9.00	8.30	-	7.90	-	-	8.25	8.82	-	-	8.49
<b>4. Percentage of loans w/other type of rate c/</b>	-	-	-	-	-	-	-	-	11.7	-	-	-	-	1.10
Total loans	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
<b>Memorandum item</b>														
U.S. prime rate (average)	...	5.67	5.63	6.33	8.00	7.81	6.69	5.65	5.22	8.15	10.71	7.73	6.73	7.37
Eurodollar rate (average) <sup>d/</sup>	5.01	6.40	5.71	6.58	9.79	8.47	6.99	6.79	5.42	9.32	11.20	7.62	6.13	7.75

Source: CEPAL on the basis of official data. Memorandum items are derived from Morgan Guaranty Trust Co, World Financial Statistics, March 20, 1972 and World Financial Markets, March 1976.

a/ For credits without export credit guarantees. Rates are weighted by amounts authorized.

b/ It was not possible in every case to identify the type of prime rate used. Therefore the rate used here is a composite and caution is merited. However, data and evidence suggest that the prime rate employed was basically the United States prime rate.

c/ Percentage of total loans that were not costed on the basis prime or libor spreads, or fixed rate.

d/ 6 month rate.

Table 5.7

PERU: MATURITIES ON COMMERCIAL BANK CREDITS, 1965-1976<sup>a/</sup>

(Years)

	1965	1966	1967	1968	1969	1970	1965- 1970 average	1971	1972	1973	1974	1975	1976	1971- 1976 average
1. Average grace period	1.53	0.52	1.18	1.47	0.87	0.50	1.03	1.50	2.54	3.75	4.79	2.69	2.00	3.20
2. Average amortization period	4.79	3.84	3.51	3.90	1.09	4.50	4.01	3.50	3.67	4.87	4.64	2.99	2.83	3.82
3. Average total maturity <sup>b/</sup>	6.32	4.38	4.70	5.38	3.09	5.00	5.05	5.00	6.22	8.71	9.51	5.68	4.84	7.06

Source: CEPAL, on the basis of official data.

<sup>a/</sup> Averages are weighted by authorizations. Only for credits without guarantees of export credit agencies.

<sup>b/</sup> The sum of grace and amortization periods may be less than the total maturity because of the existence of bullet loans, i.e., loans with one payment.

type of rate, which for practical purposes was the prime rate prevailing in the U. S. 8/

The average prime rate spread in 1966 was 1.5% and thereafter it rose to 1.75%. The increase in the spread was fully consistent with the open manifestation of fiscal and balance of payments problems after 1966. 9/

An interesting feature of prime rate loans at this time was that many carried a floor, and sometimes a ceiling, on the absolute interest rate that could be charged. For instance, in 1967 a large loan that carried a spread of 1.75% had a minimum absolute interest rate of 7%. In 1968 many floating rate loans carried a 1.75% spread accompanied by not only a floor of 6 3/4%, but also ceiling of 8 3/4%, a curious concession given the deteriorating economic situation of the government. By 1970, the prime rate loans had returned to the practice of a simple floor, this time at 7%.

While a floor interest rate could theoretically have worked against the interests of the borrower, by eliminating any advantage from a sudden drop in the floating prime rate, a band, or mini-max interest rate could have been attractive in as much as it put a predictable cost on credit over the life of the loan. Thus, both borrower and lender were protected against any wild and adverse swings in the floating rate. Unfortunately, the virulent nature of world inflation in the seventies put an end to these types of arrangements in loan agreements. 10/

The table shows that the second most common way of costing loans in 1965-1970 was the use of a fixed interest rate. A fixed rate loan can be attractive to a borrower seeking a predictable cost over the life of a loan; it also conveniently passes the risk of unexpected inflation onto the lending institution. However, bankers naturally prefer floating rates, which explains why in absolute terms the percentage of credit with a fixed rate was relatively small (16%). Given that world prices were rising at a rate of 4 1/2-5% in the late 60's, the cost of this type of credit in real terms was roughly 3 1/2-3% at the time of contraction.

It is significant to note that in this early period the London Interbank Offer Rate (LIBOR) was of little importance as a costing mechanism; indeed, only one

relatively small credit had its cost determined by the LIBOR. This no doubt reflects the dominance of U.S. banks in lending to Peru. For these banks it was more profitable to lend out of New York than London. 11/ And Peru, by virtue of its being a relatively small borrower, could be attended from domestic offices in spite of U.S. government ceilings on the amount of foreign credit that could be extended by the headquarters of its banks. 12/ From the standpoint of the borrower this also was a favorable arrangement; loans out of the U.S., assuming identical spreads, were more economical given that the U.S. prime was consistently lower than the eurodollar rate (see figure 5.1).

#### 1971-1976

Turning to the second period, 1971-1976, there is a radical shift in the costing of credit. As can be seen in the table almost all the loans were priced on the libor. This reflects the fact that by the early 1970's U.S., and most other banks, had been funding their loans to Peru out of the eurocurrency market where the libor was the prevalent pricing mechanism. Loans funded out of domestic markets were much less prevalent, as seen in the negligible representation of the prime rate spread and fixed rate loans. The latter diminished in importance also because of the virulent rate of inflation in the 1970's.

Another notable feature is that at the outset of the second period, 1971 and 1972, the spread over libor was very steep, being 2.25% and 2.08% on average, respectively. The spread was markedly higher than the margin charged on floating rate loans in 1965-1970. However, thereafter the spread on loans declined dramatically, reaching a low of 1.14% in 1974. This was followed by a full circle on borrowing conditions, with a sharp rise in spreads in 1975 and ending up with an onerous 2.17% average margin in 1976.

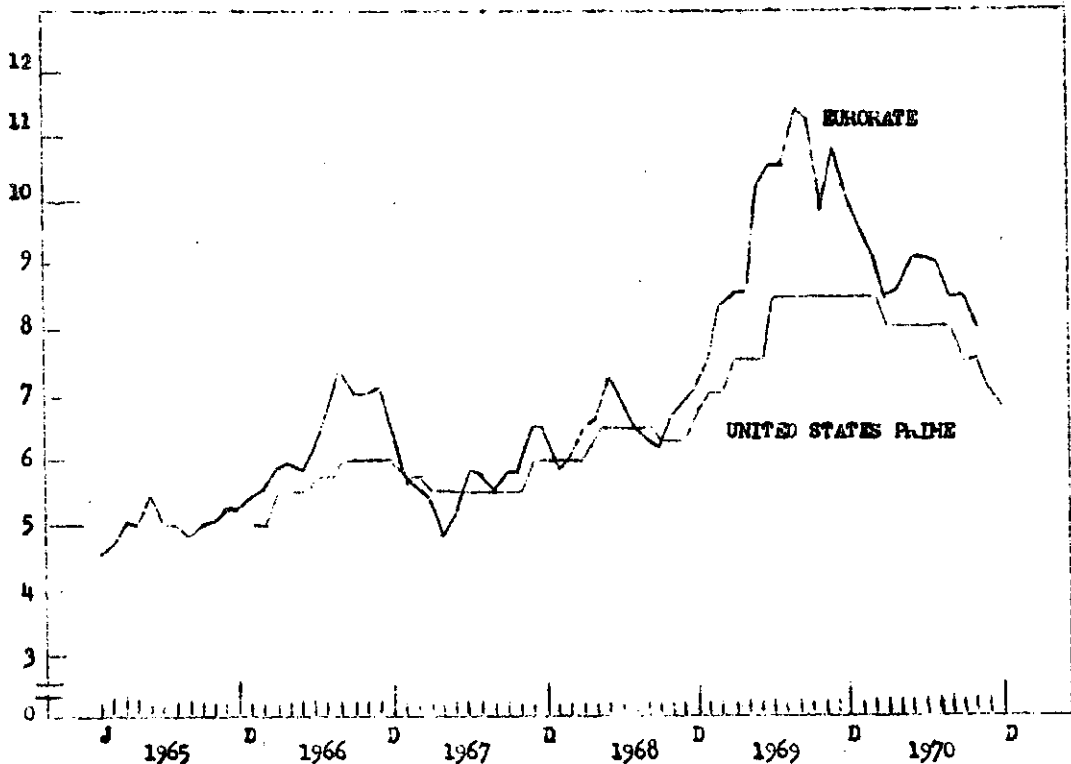
It would be interesting to compare Peru's spreads with those of other countries in order to gain some idea whether trends in Peru were due to general market conditions or to special factors unique to that country. While it would be hazardous to draw firm conclusions from such an exercise, 13/ one can establish



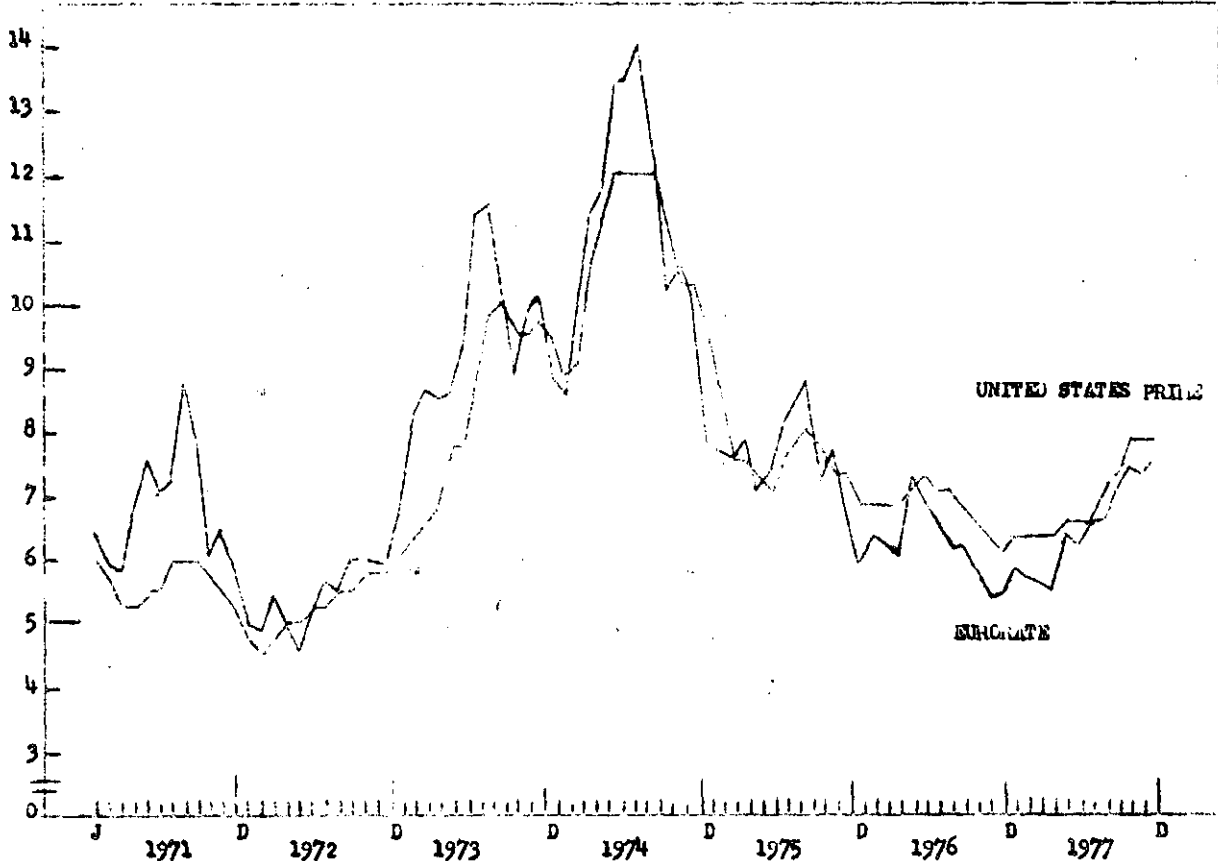
Figure 5.1

EVOLUTION OF THE EURODOLLAR AND U.S. PRIME INTEREST RATES, 1965-70 and 1971-77

Percent



Percent



g/ Eurodollar rate is the 6-months prime banks' bid rates in London

Source : Morgan Guaranty Trust Co., World Financial Statistics March, 1972 and World Financial Markets, March 1978

trends that are, at a minimum, indicative of the relative cost of borrowing and the factors behind any changes over time.

Figure 5.2 presents the study's data on spreads for Peru and the average weighted spreads for Brazil and Mexico—two countries perceived by the banks in the early 70's to be very creditworthy—based on their publicized eurocurrency credits.

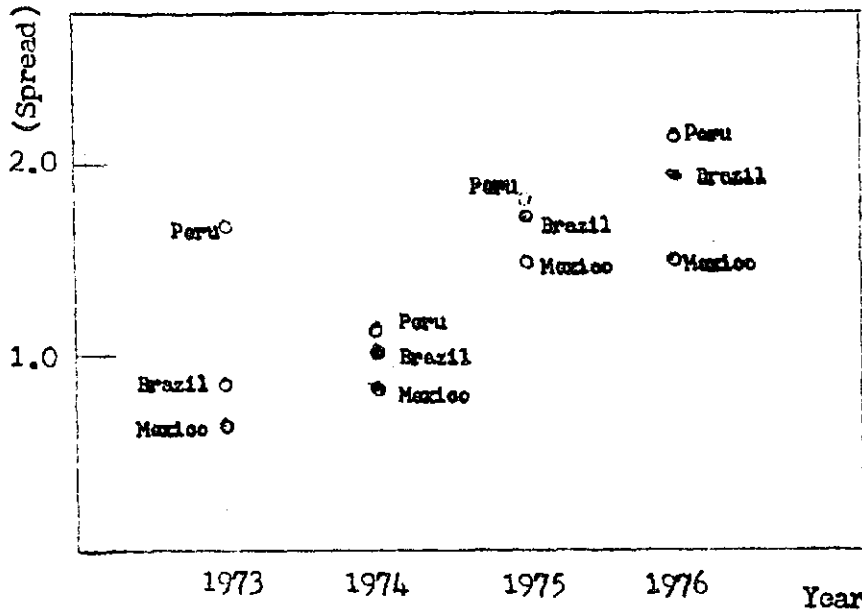
No comparable data are available for 1972, but it is known that Brazil was paying about 1.50% on its commercial money at mid-year, 14/ compared to a rate of 2.25% for Peru. This is fully consistent with a priori notions of how bankers might assess the creditworthiness of the two countries: while Peru's revolutionary government was an uncertain entity in the eyes of the bankers, Brazil had clearly established itself as an obviously dynamic economy enjoying what was then termed an economic miracle.

In 1973, with growing bank liquidity and greater pressure on these institutions to expand their lending, there was a general decline in margins for developing countries; however, as seen in the figures, the differential charge between Peru and "seasoned" developing country borrowers like Brazil and Mexico remained very large, suggesting that risk perception on Peru was basically unchanged.

Interestingly, the figure suggests that in 1974 the banks radically changed their perception of risk in Peru. Spreads for Brazil and Mexico rose with respect to the previous year, reflecting the effects of a general tightening of market conditions due to uncertainties surrounding the oil crisis, inflation and, of course, the failures of Bankhaus Herstatt and Franklin National Bank. Peru, however, went against general market trends as its average spread declined markedly. Thus, although the government continued to pay a margin superior to either of the other two countries, the differential was very much reduced. One can speculate on the reasons for the apparent change in the assessment of risk. First, Peru

Figure 5-2

AVERAGE SPREADS OVER LIBOR OF COMMERCIAL BANK LOANS FOR PERU, BRAZIL AND MEXICO, 1973-1976



a/ Weighted by amounts authorized. Public sector loans only

Source: CEPAL and World Bank, Borrowing in international Capital Markets, various issues.

was by now more familiar to the banks and had straightened out its disputes with foreign firms, as manifested in the Greene Accord of 1974. Second, by 1974 Peru was giving very favorable estimates of its petroleum reserves and arranging for construction of a pipeline to bring the crude to the coast for export. Third, previous borrowing contributed to a rather large accumulation of reserves (see table 3.3) that provided security, i.e., the liquidity needed to service the external debt. All these factors probably contributed to a more favorable assessment of risk. Whether the real underlying circumstances of the Peruvian economy altered to a degree commensurate with the changed perception of risk would be an interesting topic of study.

In 1975 one finds a general rise in margins, which is consistent with a further tightening of market conditions that year. However, it is seen that while the differential between Peru and Mexico remains roughly the same, there is a near elimination of the gap in spreads between Peru and Brazil. Thus, there was a relative erosion of Brasil's position vis-a-vis the other two countries. This also is consistent with outward circumstances. Brazil's enormous external debt and "slowness" in adjusting the balance of payments were by now clearly of concern to its bankers. 15/ While in Peru the balance of payments was not all that healthy either, there was still the security (though waning) of prospects for oil in the Amazon. Meanwhile, Mexico continued to enjoy one of the lowest spreads among developing country borrowers, in part because of its special relationship with the United States, where most of its major commercial creditors were domiciled. 16/

In 1976, borrowing conditions on international markets continued to be roughly as onerous as in 1975. Reflecting this, Mexico shows no real change in its average spread; apparently, the aforementioned special relationship with the U.S. overrode the uncertainty surrounding the 1976 devaluation and change in government, or alternatively, the effects of these events had not yet had a chance to work their way into the average spreads available to the country. However, Peru and Brazil underwent further deterioration, with Peru clearing

suffering the greatest erosion with regard to the bankers perception of risk. Again this appears to be consistent with objective circumstances. By now Brazil had shown signs of formulating a credible program to tackle its balance of payments problems. Peru, on the other hand, suffered from an unforeseen change in government in mid-1975, its balance of payment was worsening and there was a degree of political uncertainty. But perhaps most importantly, the euphoria surrounding petroleum in the jungle had completely evaporated, with all but one of the foreign companies drilling for oil having terminated its operations and abandoned the country.

## 2. Maturities

In the first period, 1965-1970, maturities on commercial bank credits averaged only 5 years, incorporating a short grace period of 1 year and 4 years of amortization (see table 5.7). This would appear to have been in line with general market trends as term loans of 3 to 5 years are considered to have been the norm for the market in the latter half of the 1960's.

It is worthwhile to point out that the longest maturities were achieved in 1965, at somewhat more than 6 years. This may have been less than a coincidence since the government's creditworthiness probably was at a peak at this time. It is difficult to tell whether the arrival of the new military regime in late 1968 affected the banks' willingness to extend the maturities; only in 1969, a year in which little borrowing was undertaken, was the tenor of credit unduly short. However, the unusually short grace periods applied to loans in 1969-1970 are indicative of the bankers' reserve with respect to the new regime.

The second period, 1971-1976, witnessed a 40% lengthening in the average maturity to 7 years. The average, however, hides much longer maturities of 8.7 and 9.5 years for 1973 and 1974, respectively. But what the data confirm

is that banks have been merely providers of medium term finance and, notwithstanding occasional periods of extended maturities, they were far from fulfilling the requirements of long term finance.

Again, it might be instructive to compare Peru's maturities with the two superborrowers, Brazil and Mexico. The caveats that applied to the data on interest margins are equally applicable to maturity information.

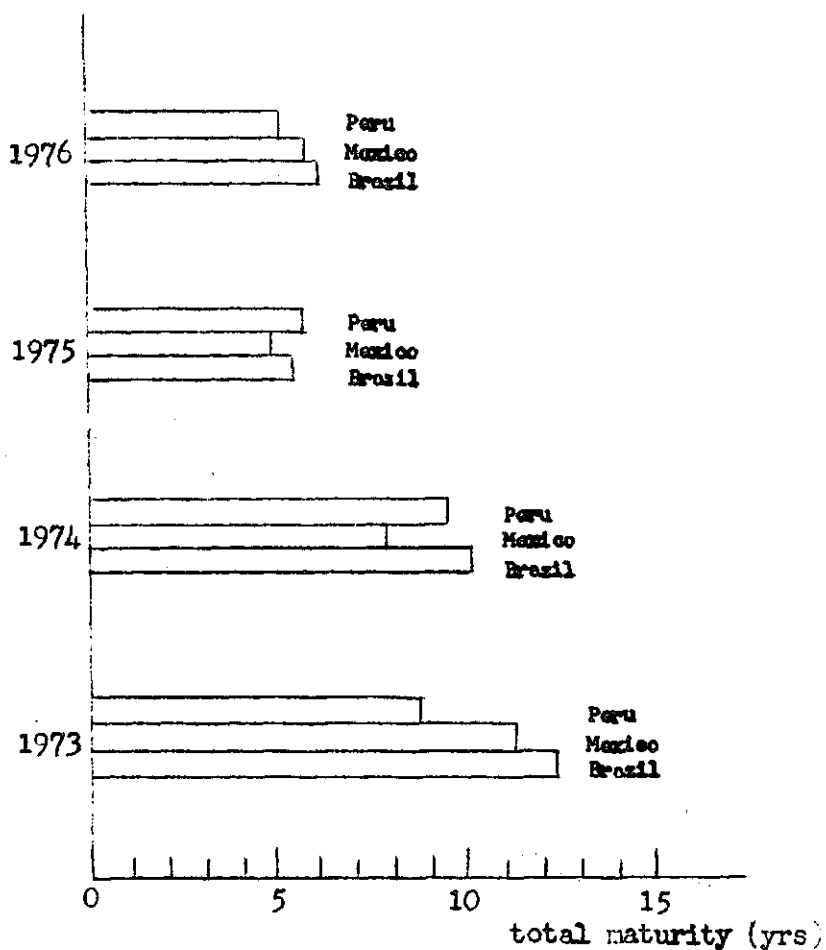
While comprehensive comparative data for 1972 are unavailable, it is known that Brazil was regularly securing loans with at least a 10 year maturity in 1972. 17/ Peru, on the other hand, secured an average of 6 years. The difference was not attributable to differentials in margins—i. e. higher margins for longer maturities—since in this year Peru also had a considerably higher cost of credit. Thus, the short maturity would be another confirmation that Peru was viewed as a rather high risk in 1972. But the large differential also may have been partly reflective of Peru's inexperience in negotiating maturities with international banks; as will be seen momentarily, in later years the respective trends in creditworthiness among the three countries were accompanied by much less marked differences in maturities.

Figure 5.3 shows that although Peru's maturities lengthened in 1973, they still were considerably less than those available to prime developing country borrowers such as Brazil and Mexico. 18/

One has already seen evidence in interest margins that in 1974 Peru was viewed as a better risk. This also holds true with regard to the behavior of maturities as the tenor of Peru's credit was about the same as Brazil's and even longer than Mexico's. Then in 1975 when the market was very tight all borrowers experienced a notable contraction of terms; however, perhaps in part due to its higher interest margin, the average maturity was actually slightly longer than what was available to either Brazil or Mexico. In 1976 Peru again was on short side of maturities, along with the considerably higher interest margin, suggesting serious deterioration of creditworthiness from the viewpoint of its private creditors.

Figure 5-3

AVERAGE MATURITIES ON COMMERCIAL BANK LOANS FOR PERU  
BRAZIL AND MEXICO, 1973-1976 a/



a/ Weighted by amounts authorized. Public sector only.

Source: CEPAL and World Bank, Borrowing in International Capital Markets, various issues.

#### D. FEES AND PENALTIES

Most loans carry clauses that establish fees and penalties. The fees are charged for services, while penalties are for breach of contractual terms. The following paragraphs will show the evolution of these charges for Peru. Analysis does suffer, however, from the general dearth of information on LDC loans; no comparisons could be made with other countries because little or no data of this kind reaches public scrutiny.

##### 1. Fees

There are several types of fees. One common charge is a commitment fee that is paid to a bank to reserve funds until they are fully drawn down. The most common commitment fee is a periodic charge on undisbursed balances. The fee also can be a flat charge on the face value of the loan, but this practice was of little importance for the credits to Peru.

Other fees are charged for the organization and administration of a loan. These can be variously termed management fees, agent's fee, participation fee, etc. They are usually at the front end of a loan, i.e., a flat percentage of the face value of the credit, and if more than one bank is involved, they are distributed in various ways according to some predetermined pattern agreed to by the banks.

Most loans also carry provision for reimbursement of a bank's miscellaneous costs—often termed "out-of-pocket" expenses—for legal dispositions, preparation of the credit agreement, publicity, etc.

Table 5.8 presents data on the average cost of fees in both periods.

What is striking about the period 1965-1970 is that fees as explicit cost items were the exception rather than the rule. Flat fees were most uncommon and less than 15% of the total authorizations carried commitment fees.



Table 5.8

PERU: FEES CHARGED ON COMMERCIAL BANK CREDITS, 1965-1976a/

	1965	1966	1967	1968	1969	1970	1965- 1970 average	1971	1972	1973	1974	1975	1976	1971- 1976 average
<b>1. Percentage of loans w/a flat fee b/</b>	-	-	-	2.0	-	-	1.0	-	49.0	86.0	85.0	99.0	96.0	87.0
Average, specific rate c/	-	-	-	1.00	-	-	1.0	-	0.47	0.45	0.31	0.93	1.32	0.77
Average, overall rate d/	-	-	-	0.2	-	-	-	-	0.23	0.39	0.26	0.92	1.27	0.67
<b>2. Percentage of loans w/a commitment fee e/</b>	-	-	2.0	34.0	-	-	14.0	-	57.0	73.0	43.0	100.0	88.0	74.0
Average, specific rate c/	-	-	1.00	0.25	-	-	0.26	-	0.50	0.46	0.47	0.52	0.72	0.56
<b>Memorandum item</b>														
Percentage of all credits that were unspecified with regard to fees f/														
Flat fees	-	17.0	19.0	7.0	43.0	-	8.0	-	-	1.0	1.0	1.0	-	1.0
Commitment fees	-	17.0	19.0	7.0	43.0	-	8.0	-	-	1.0	1.0	1.0	-	1.0

Source: OEPAL on the basis of official data.

a/ For credits without guarantee of an export credit agency. Averages are weighted by amount authorized.

b/ A one time fee charged on the face value of the loan.

c/ Average for credits that carried this penalty.

d/ The result of applying the specific rate to all credits. Can be viewed as the effective rate for all money in the period.

e/ A fee charged on the undisbursed balance of a loan.

f/ The percentage of credit in the total study that was unspecified with regard to fees. In calculating averages and percents, these credits were excluded from consideration.

In 1971-1976, however, there was a general proliferation of fees. Two principal reasons appear to be behind this trend.

First, banks discovered flat fees to be a discreet way in which to raise the yield on their loans. Moreover, in a bargaining environment a borrower might be more receptive to an increase in fees than an increase in its interest margins; the former are not well publicized and therefore acceptance of higher fees could enable a borrower to hide embarrassingly high interest margins which would reflect badly on its creditworthiness. Also, the longer the maturities the more amenable fees become to a borrower.

A second reason behind the employment of fees was the growing use of syndication for arrangement of loans. In these loans, institutions that organize such a credit (the managers) and the bank that administers or enforces the loan agreement (the agent) expect to be reimbursed for their services. Indeed, some banks, particularly consortium or merchant banks, rely mostly on fees for their earnings, i. e., they organize and/or administer credits, capturing the management and/or agent fee, while placing only a nominal (or even no) amount of interest bearing money in the loan itself. Also in syndication, lead banks have introduced the practice of granting fees to banks willing to participate in a credit.

With regard to the fees themselves, commitment fees were carried on nearly three-quarters of the loans and averaged 0.56 of one percent on outstanding balances. Flat fees of all kinds were charged on 87% of all credits in 1971-1976 and averaged 0.77 of one per cent of the face value of the loans.

It appears that these fees too were at least partly a function of Peru's attractiveness as a borrower. In 1972-1973, a period when fees were gaining wide acceptance among bankers, the flat service charge averaged around 0.46%. However, in 1974 there was a noticeable drop in the average cost, which may be in line with what was earlier shown to be a possible change in the bankers' perception of risk in Peru. But a shift to a creditors' market in 1975, coupled

with clear problems in Peru, caused the average fee to triple to nearly 1.0%. Then, in 1976 when Peru was on the verge of losing its creditworthiness, the fees attached to the already high margins was a rather stiff 1.3% on average.

The fees associated with the reimbursement of "out-of-pocket" expenses, legal fees, etc., were generally a very minor cost item, but at least on the surface appear to have involved a rather odd arrangement. In the vast majority of cases banks gave themselves a "carte blanche", i.e., the loan agreements simply state that the borrower must reimburse for all such expenses. On some occasions vague parameters were set by the use of the term "reasonable" costs. And in the least frequent of cases some dollar ceiling was placed on the amount that could be charged for miscellaneous expenses.

## 2. Penalties

Turning to penalties, two types have been quantified: late payment penalties and premiums charged on any pre-payment of a loan.

In the first period, the most common type of penalty was a premium on the basic interest rate for payments arriving after the due date of an interest or amortization period (see table 5.9). And the penalty for any late payment was stiff, bringing on average for the period a 70% increase in the cost of interest over and above the basic rate. In the second period, this type of penalty was more pervasive, covering 71% of all credit. However, the average increase in the interest rate was lower, 58%. It was not possible to determine to what extent the borrower actually encountered these penalties. Nor was it possible to systematically assess to what extent creditors enforced such penalties. One assumes, however, that banks were flexible in their application. In any case, the penalty fees can be viewed as an "escape valve" because they can be used in lieu of calling a default, which is a contractually legal, but drastic way for dealing with lagging payments.

Table 5.9

PERU: PENALTIES ON COMMERCIAL BANK LOANS, 1965-1976<sup>a/</sup>

	1965	1966	1967	1968	1969	1970	1965- 1970 average	1971	1972	1973	1974	1975	1976	1971- 1976 average
<b>1. Percentage of all loans with late payment penalty b/</b>	-	88.0	-	-	-	100.0	41.0	-	39.0	32.0	25.0	87.0	96.0	71.0
<b>Average premium c/</b>	-	67.60	-	46.10	-	71.40	70.00	-	60.30	57.30	75.10	59.30	42.80	58.10
<b>2. Percentage of all loans with prepayment penalty d/</b>	-	88.0	96.0	8.0	-	-	28.0	-	5.0	65.0	43.0	94.0	76.0	62.0
<b>Average specific rate e/</b>	-	0.23	0.50	0.50	-	-	0.39	-	0.50	1.41	0.71	0.91	1.49	1.18
<b>Average overall rate f/</b>	-	0.22	0.48	0.04	-	-	0.11	-	0.03	0.91	0.31	0.85	1.14	0.74
<b>Memorandum item</b>														
Percentage of credits that were unspecified with regard to fees and penalties g/														
Late payment	17	19	12	43	-	-	10	-	-	2	3	1	7	3
Prepayment	17	19	9	43	-	-	9	-	-	1	1	1	-	1

Sources: CEPAL on the basis of official data.

a/ Only credits without guarantees of export credit agencies. Averages are weighted by the amount of the loan.

b/ Penalty paid on tardy loan repayments.

c/ Percentage increase in original interest rate on amount that is paid past due date.

d/ Flat fee paid on any portion of a loan that is cancelled in advance of schedule. When the fee was scaled over the life of the loan, an average was taken, weighted by the number of years each rate prevailed.

e/ The average rate for credits that had this penalty.

f/ The result of applying the specific rate to all credits can be viewed as the effective rate on all money for the period.

g/ The percentage of credits in the whole study that provided no information with regard to penalties. These credits were excluded from the calculation of percentages and averages.

As for prepayment penalties, they are placed on loans to discourage a borrower from prepaying an expensive credit with a new cheaper loan that may become available to a borrower due to a favorable turn in market conditions. <sup>19/</sup> Banks as a rule dislike prepayment because they can lose a profitable loan and, if not participating in the new credit, they also receive an unanticipated (and perhaps unwanted) inflow of liquidity that would have to be placed again in the market.

The fees themselves can be one basic flat fee on any amount prepaid. But a more common practice, especially in the 1970's, was to scale the flat fee according to when prepayment would be effected. For example a large 10 year loan contracted in 1973 had a 3% penalty for prepayment during the first year of the loan, 2% during the second, and 1% during the third, with no penalty thereafter; a 5 year loan in 1976 had prepayment penalties of 2 1/2% during the first year with a reduction of 1/2% for each year up to the fifth and last year, when prepayment could be effected at a cost of 1/2%. <sup>20/</sup>

As can be seen in table 5.9, about 28% of the credits in 1965-1970 had arrangements for prepayment penalties. Those credits that carried such penalties had an average cost (for 1965-1970) of 0.39 of one percent for the full maturity. In 1971-1976 prepayment penalties were much more common, being borne by over 60% of the credits. Moreover, the penalty averaged 1.18%.

As one might expect, prepayment penalties were most commonly applied when the borrower's terms were most onerous, either due to a lender's <sup>(i)</sup> market, a relatively low level of creditworthiness, or both. This is confirmed by the fact that coverage is the most extensive and the penalties themselves most severe in 1973 and 1975-1976. In contrast, 1974, a year in which bankers appear to have taken a favorable view towards Peru, shows relatively lower coverage and lower prepayment penalties.

There is no doubt that from the standpoint of an individual lending institution discouragement of prepayment makes good commercial sense. However, one cannot help but think that in a broader perspective such penalties on developing country borrowers may be counter-productive for all concerned.

Prepayment strategies of developing countries are a convenient way for borrowers to assuage the frequent surges in interest margins and contractions of maturities that occur because of changing market conditions and/or deterioration of credit-worthiness. A borrower which can trade in old expensive loans for new cheaper loans is effectively enhancing its debt service capacity. Thus through prepayment (and refinance) strategies a borrower can become a better overall risk and assure a greater volume of new debt, generating more resources for development and more business for the banks.

#### E. CREDITS WITH EXPORT CREDIT GUARANTEES

The preceding analysis of the terms and conditions of credit were for loans that did not have any explicit guarantee of an export credit agency such as the U.S. Export Import Bank. It might be instructive to briefly display the terms on these "guaranteed" loans as a way of comparison with unguaranteed bank credits. Table 5.10 provides just such information for the period 1971-1976.

Not surprisingly, the terms are considerably more favorable, as banks were able to pass the risk onto the export credit agency and therefore could provide less than "commercial" terms. In almost all cases the interest rate was fixed, and not terribly high at an average of a little more than 7% for the period 1971-1976 (in the same period world consumer prices rose by more than 10%). Moreover, the average maturity was 8 years, one full year more than the average for unguaranteed loans. Also, the frequency and amount of front-end fees were considerably less than what was charged for unprotected loans.

One must be cautious, however, about generalizing with regard to the nominal differential between guaranteed and unguaranteed credit. First, costs are understated because the export credit agency generally charges the borrower a fee for its guarantee. Second, the loan is tied to the purchases of goods in the

Table 5.10

PERU: BASIC DATA ON COMMERCIAL BANK CREDITS WITH GUARANTEES  
OF AN EXPORT CREDIT AGENCY, 1971-1976 <sup>a/</sup>

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	1971-1976
<hr/>	
1. <u>Interest</u>	
a) Percent of loans with fixed rate	(96.3)
Average rate (%)	(7.9)
b) Percent of loans with libor spread	(-)
Average spread (%)	-
c) Percent of loans with prime spread	(2.8)
Average spread (%)	1.0
2. Average total maturity (years)	8.1
3. Percentage of loans with flat fees	(52.5)
Average fee (%)	0.75

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Source: CEPAL on the basis of official data.

<sup>a/</sup> Only on credits where it was possible to determine the existence or not of fees.

country of the export credit agency, which itself may have implicit costs for the borrower. Third, what appears to be a commercial credit on the surface, really becomes a bilateral government to government loan, which generates potential for the home government of the commercial bank to interfere in the domestic affairs of the borrower.

#### F. TYPES OF LOANS EXTENDED BY COMMERCIAL BANKS

It is interesting to view commercial bank loans when they are broken down into their basic type. This also conveniently provides a forum that will enable a more detailed analysis of the lending activities of commercial banks. But before pursuing analysis it is important to point out that the categories of loans are based on a formal typology which reflects to some degree the legal purpose of a credit, i. e., a refinance credit is understood to be for payment of a prior debt obligation, whether it be to the lending bank or another credit institution; a free disposition credit formally is for any purpose whatsoever; a project credit is linked to finance of a specific investment, etc. However, money is fungible and on a functional basis the differences among credits sometimes can be more formal than real. For instance, refinance credits postpone the outflow of resources via debt payments, thereby freeing a country's foreign exchange for general purpose use, much like a free disposition credit. Likewise, a free disposition credit can be used to repay debt and a project loan for local costs provides free foreign exchange for any purpose. One could go on. But even though there can be little functional difference among the various types of loans, there formal differences sometimes can be important with regard to the establishment of terms and conditions of a credit. Also, as will be seen Chapter 7, it appears that some banks have preferences for participating in certain types of loans.



Table 5.11 breaks out bank credits (without an external guarantor) into 7 basic categories and shows the relative importance of each for the two basic periods under study.

In the period 1965-1970, bank lending activity was extremely concentrated in refinance operations. This type of credit accounted for nearly 80% of all credit extended. Loans of free disposition were a distant second with 15% of the total lending. And lending for projects and capital goods imports was a minor activity indeed.

In the second period, 1971-1976, one sees much greater dispersion, which is indicative of the transformation of world banking and the general willingness of these institutions to lend to LDCs. Refinance operations still predominated lending activities, but their share of total lending fell to less than 50%. Meanwhile, loans of free disposition rose to nearly one-third of all loans. And projects, which received little bank support in 1965-1970, accounted for nearly one-sixth of all commercial credit in the 1970's. One also sees that a significant part of bank credit was formally authorized to compensate for nationalized assets. Thus it is clear that in the first half of the decade of the 1970's commercial banks rather radically diversified the nature of their lending activities with Peru.

#### 1. Free disposition loans

Loans of this type are generally considered to be attractive to the borrower. Since no specific use is attached to the funds, such credits give the borrower considerable flexibility in the allocation of external and domestic resources. Moreover, by not being attached to purchases of goods and services, loans of this type facilitate repayment of debt (domestic and foreign) and foreign exchange accumulation, 21/ the latter being an essential ingredient in keeping commercial bankers confident of a country's creditworthiness. Such loans also demand discipline on the part of the borrower; since there is no



Table 5.11

PERU: BREAKDOWN OF COMMERCIAL BANK CREDITS INTO TYPE, 1965-1970 AND 1971-1976<sup>a/</sup>

(Percent)

Type of loan	1965-1970	1971-1976
Import of K goods	-	2.0
Import of other goods	-	0.1
Refinance	79.9	48.6
Free disposition	15.3	27.8
Projects	4.8	14.7
Nationalizations	-	6.1
Other	-	0.7
<u>Total</u>	<u>100.0</u>	<u>100.0</u>

Source: CEPAL, on the basis of official data.

<sup>a/</sup> Only for credits without guarantees of export credit agencies.

ex ante specification for the resources, the borrower must ensure that they eventually are channeled into areas where their returns exceed the cost of credit.

From the viewpoint of the lender, these loans may be less attractive. With no ex ante purpose attached to the loan, the bank has no insurance that the resources will be used wisely, placing the prospect of repayment squarely on the value of a sovereign guarantee. Also, a bank faces the risk that funds will be used to prepay more expensive loans granted earlier by the institution, something that, as was seen earlier, generally is not viewed favorably.

In the period 1965-1971, only 15% of authorizations were freely disposable loans (see again table 5.11). Almost 95% of the value of these loans carried floating interest rates, which was much higher than the global average for all loans and consistent with the attractive nature of the credit for the borrower. The average interest cost was roughly on par with the global average for all loans in the period and the maturity was slightly shorter than the overall average tenor (see table 5.12). No flat fees were charged, but consistent with the attractive nature of this type of credit, banks had sufficient leverage to place prepayment penalties on all such money with the average penalty being 0.44 of one percent.

A majority of the untied funds for the period was extended in two multibank loans in which the core lenders were Bankers Trust, Manufacturers Hanover, Citibank and Continental Illinois. 22/ One loan, extended in 1966, involved some new money that was melted into a 40 million dollar credit geared basically to refinance earlier debt to the banks. In July 1967 another 40 million loan was extended, this time entirely for the general use of the government. The funds —which were costed at 1.75 over a prime rate and carried a maturity of 5 years— were employed to prop up the ailing fiscal budget and balance payments.

Table 5.12

PERU: TERMS ON CREDITS GROUPED ACCORDING TO TYPE, 1965-1970 AND 1971-1976<sup>a/b/</sup>

Category of loans	Interest rate			Total maturity (in years)	Flat fees and prepayment penalties	
	Percentage of credit in each category with:				Percentage of credit in each category with:	
	(i) fixed rate	(ii) Libor spread	(iii) prime spread		flat fee <sup>c/</sup>	prepayment penalty <sup>c/</sup>
	Actual rates				Actual rate	Actual rate
<u>1965 - 1970</u>						
1. Import of K goods	-	-	-	-	-	-
2. Import of other goods	-	-	-	-	-	-
3. Refinance	13.0 7.96	4.2 1.74	82.9 1.72	5.07	1.0 1.00	14.9 0.32
4. Free disposition	5.5 8.75	-	94.5 1.69	4.78	100.0 -	100.0 0.44
5. Projects	100.0 7.45	-	-	5.64	100.0 -	100.0 -
6. Nationalization	-	-	-	-	-	-
7. Other	-	-	-	-	-	-
<u>1971 - 1976</u>						
1. Import of K goods	9.0 10.43	53.1 1.61	37.9 1.15	6.34	35.3 0.65	21.9 1.28
2. Import of other goods	100.0 9.00	-	-	2.00	-	-
3. Refinance	-	96.1 1.81	1.64/ 1.55	6.98	83.0 1.00	69.6 1.23
4. Free disposition	3.9 8.12	95.2 1.79	1.0 0.75	7.15	93.3 0.61	70.1 1.39
5. Projects	-	93.1 1.71	6.9 1.78	6.87	92.0 0.67	61.6 0.52
6. Nationalizations	-	100.0 1.31	-	8.38	100.0 0.22	100.0 -
7. Other	-	12.2 0.59	87.8 1.25	4.63	100.0 -	100.0 -

Source: CEPAL, on the basis of official data.

a/ Credits without guarantees of export credit agencies.

b/ Average weighted by amounts authorized.

c/ See footnotes to tables 5.8 and 5.9.

d/ 2.3% of the refinance credits had a rate other than those cited in the table.

In 1967 the granting of considerable freely disposable funds to the government may be viewed with surprise given the economic and political problems of the country, which by now were clearly manifest. But the banks apparently were encouraged to participate in a financial package, which included a standby credit from the IMF, because of what Kuczynski termed a "need to do business with a country that had until recently, and might again have, large foreign exchange reserves to deposit abroad". 23/ But if the banks had any doubts about lending to Peru when they agreed to the loan in mid-July 1967, by the time of the signing later that month, the chaotic events in the country clearly had the banks second-guessing the wisdom of their decision. If it had not been for the fact that the banks had fully committed themselves to the credit, the offer probably would have been withdrawn. 24/

Turning to the period 1971-1976, free disposition loans rose to represent something near to one-third of all authorizations. In this case, the average interest for the period of 1.79% over libor was approximately equal to the average spread for all loans (1.79%) and the average maturity rate of 7.15 years was not significantly different than the global average (7.06 yrs.). The percentage of these loans which carried flat fees was somewhat higher than the average for all loans, but the average cost of the fees itself, at 0.61 of one percent, compared favorably to the average for all credit (0.77 of one percent). And, consistent with the rather attractive nature of these loans for borrowers, bankers had relatively greater success in negotiating prepayment penalties, with 70% of all such credit carrying a premium. Moreover, the average penalty of 1.4% was significantly higher than the general average for all credit of 1.18%.

One must be careful to point out that the average terms above are not independent of years in which this type of credit was extended. Roughly 63% these loans were contracted in 1973 and another 29% was arranged in 1975.

The accumulation of freely usable funds in 1973 reflects the interaction of two phenomena.

First, it reflects a borrower which was interested in fortifying the foothold it had established in the international commercial bank markets in 1972. The public sector's investment program was still largely in the planning stage and therefore the capacity to absorb debt into real activities was still limited. Thus, the only practical way to contract funds was through untied loans. Receipts could then be used to build up reserves—something that bankers like to see—and occasionally prepay more expensive older loans with undesirable conditionality. Second, on the supply side it reflects the desire of aggressive non-traditional lenders to capture a piece of the Peruvian market—which was becoming more attractive because of oil and a general consolidation of the military regime's economic and political program—coupled with the efforts of traditional lenders to defend their market position.

This second factor can be illustrated. In early 1973, Wells Fargo, a newcomer to the Peruvian scene, headed a 100 million dollars syndicated general purpose loan to the government. This credit obviously was designed to strengthen the market position that the bank first began to develop in 1972. The loan also was economically attractive to the bank as the Peruvian government was willing to pay 2% over libor for the money at a time when many other developing countries were approaching spreads of 1% or less on their credit. Soon after the Wells Fargo credit, another large free disposition credit at 1.75% over libor was arranged by another group of relative newcomers—Bank of Tokyo, Lloyds and Bolsa International Bank Ltd. and Mitsubishi Bank Ltd. Traditional lenders reacted by arranging their own syndicates providing general purpose funds, e.g., Crocker National arranged a 40 million dollars credit, and Manufacturers Hanover and Citicorp accommodated the government with a \$130 million syndicated general purpose loan. Overall market conditions, coupled with the flurry of competition centered around the Peruvian market, caused margins on these loans to fall drastically.

By the end of 1973 freely disposable loans were being contracted at 1.25% over libor and some loans even carried fixed interest rates for up to 7 years.

After 1973 this type of credit became less prevalent. One reason is that subsequent to this year the government could more readily absorb credit into the many new projects that it began to implement. Another factor is that after mid-1974 banks became more cautious lenders, perhaps making them less inclined to extend general finance. This is especially true with regard to Peru, which by late 1975 displayed an economic situation that clearly was worrisome to the banks.

## 2. Nationalization credits

One has seen that 6.1% of the loans extended by commercial banks in the period 1971-1976 were formally designated for the compensation of foreign firms nationalized in the government's reform program (see table 5.11). This is certainly interesting because it means that in the medium term the government effectively exchanged interface with transnational corporations for interface with transnational banks.

Looked at another way, the banks bailed out their corporate clients and perhaps even bailed out Peru in the sense that funding facilitated terminal settlements with affected corporations, thereby concluding or avoiding conflicts with home country governments. Moreover, the average terms for settlement were relatively favorable. The average interest rate of 1.31 over libor (see table 5.12) compares nicely with the global average of 1.75 over libor and the 8.3 average maturity is significantly longer than the 7 years for all commercial credit.

The most conspicuous loan of this type was a 76 million dollar credit headed by Morgan Guaranty Trust Company and nine other large U.S. banks in 1974. 25/ The amount corresponded to the direct payment that Peru was to make to the U.S. Treasury for compensation of nationalized U.S. firms, as agreed to under the



Greene Accord of that same year. 26/ Terms were very attractive, 1% over libor, 10 year maturity, a flat fee of only 0.11 of one percent and no prepayment penalty. Another important credit of this type was granted in 1976 by a group of six Swiss Banks headed by the Swiss Bank Corporation. 27/ It was for 40 million dollars, 30 million of which was to compensate various Swiss entities that held shares or debt of nationalized firms in the power, communications and manufacturing sectors of Peru. (The remaining 10 million dollars was of free disposition). 28/ The loan carried terms that were more onerous than the previously mentioned credit, with a spread of 1 3/4% over libor and a maturity of 5 years; but taking into account the generally tight borrowing conditions in the market, as well as Peru's eroded creditworthiness, the terms of the loan can be viewed as having been relatively favorable to the government.

Other loans were extended in 1973 that facilitated nationalization of the fishing industry. One was a 14 million dollar credit by a group of American banks headed by Manufacturers Hanover. The cost was a spread of 2% over libor with a maturity of 7 years, both being favorable relative to the general conditions prevailing at the time for credit to Peru. Moreover, there were other credits, totalling more than 45 million dollars, which were formally classified as free disposition or refinance credits, but which really were used to effect the nationalization of the fishing industry. 29/

### 3. Refinance credits

In both periods credits related to refinance of debt were the most common form of loan transaction. A commercial bank can refinance debt owed to itself, another bank, a commercial supplier or an official agency. Refinance may be for debt payments falling due in one year, or less commonly, for the whole balance of the loan, thereby effectively restructuring the original maturity.

Commercial banks generally do not like to refinance their own loans because of the notion that contractual repayment schedules are sacrosanct; 30/ nevertheless, in practice banks often do refinance. In a competitive environment such as in the early seventies, if a bank does not agree to refinance its loans, another bank may be willing to do so, eroding the former institution's market position. On the other hand, if the borrower is in financial difficulty, refinance is often an alternative to default, something that the banks would want to avoid if possible because of the adverse impact that this has on their annual financial statements. Refinance also can be viewed as an alternative to rescheduling, something that the banks resist at all cost. 31/

A bank most often will be willing to refinance another lender's debt when it is seeking to generate new business in a competitive environment. However, occasionally a bank, as a favor to a major corporate client, may refinance a suppliers' credit which the client had extended to the borrower and for which it may be unwilling or unable to refinance itself.

Turning to the period 1965, refinance credits were basically costed with a margin over the prime rate. (See table 5.12.) Both the average margin and maturity for these credits closely correspond to the global averages for all credits.

The majority of all refinance credits were contracted in 1968 and 1970 under conditions of economic stress. The concentration in these two years represents the results of the formal negotiations between the Peruvian government and foreign creditors for the rescheduling or refinance of debt. Both due to multilateral and bilateral agreements, bank refinance totalled 140 million in 1968 and 94 million dollars in 1970. American banks accounted for 88% of the total, while Canadian, European and Japanese banks shared the rest. It is significant to note that notwithstanding a difficult economic environment, banks insisted on rather onerous lending terms. Authorities were never able to

negotiate loans with more than 6 year maturities and the bulk of credit carried only 5 years. Moreover, grace periods were extremely short, 1.5 years in 1968 and only 0.5 years in 1970. This left prospects of a heavy debt service burden almost immediately after the relief was provided.

For this earlier period it is relatively easy to determine the nature of finance because such loans were not terribly large and were of a specific nature, thereby providing for a transparency that allows one to trace obligations being covered by new loans. Such was not the case in the 1970's when credits tended to be very large and tied to general requirements for refinance.

In 1965-1970, 92% of all refinance credits provided information sufficient to determine what was actually refinanced. Of these "specified" credits, 90% of the total value was destined simply to refinance prior obligations to the lending commercial bank. Table 5.13 shows a sequence of loans of one bank in the study. As can be seen, the new credits (nos. 1 and 3) in the period were never really repaid as they were continuously refinanced by the bank. This series is typical of many transactions undertaken by banks in the 1960s, and underscores W. Arthur Lewis' observation that in the end the bankers' are most concerned that interest payments are met and will, even if displaying reluctance, tend to refinance their obligations. 32/

The remaining 10% of the specified refinance credits went to refinance suppliers' credits, and debts owed to bilateral agencies and multilateral institutions such as the World Bank and IDB.

As noted in chapter 4, in the early 60's the Peruvian government had taken heavy recourse to suppliers' credits. As payments began to accumulate in 1965-1968, the banks financed a significant amount of these obligations with new loans, beginning the process of the shift of dependency from suppliers to banks.

Since there is no empirical evidence to explain the bankers' motivation for underwriting suppliers' credit assets, one can only conjecture about the

Table 5.13

PERU: A TYPICAL SEQUENCE OF LOANS BY A COMMERCIAL BANK FOR THE PERIOD 1965-1970

Year of credit	Amount (millions of dollars)	Interest rate	Maturity (years)			Comments
			Grace	Amortization	Total	
1. 1964	12.5	...	...	...	3.0	A free disposition loan for general finance of the fiscal budget
2. 1966	12.5	1.5 + prime	0.5	4.5	5.0	Refinance of unpaid balance of credit 1 plus \$ 3.8 million in new money.
3. 1967	8.4	1.75 + prime	1.0	4.0	5.0	A new credit extended that is of free disposition for use in the fiscal budget. Overall term is the same as credit 2, but with extended grace period. The latter might be considered useful for a borrower with temporary cash flow problems
4. 1968	17.2	1.75 + prime	1.5	3.5	5.0	Refinance of unpaid balances on credits 2 and 3. Extended grace period again favourable to a borrower with tight cash flow
5. 1970	15.4	1.75 + prime	0.5	4.5	5.0	Restructured unpaid balance of credit 4. Note short grace period which requires more discipline from the borrower

Source: CEPAL on the basis of official data.

dynamics behind the process. It is suspected that the banks first began to refinance out of a desire to generate new loan business. 33/ It must be remembered that at the opening of the period Peru was viewed as being rather creditworthy by the banks and the loans for refinance of suppliers' credits were small in comparison with other loans being extended by these institutions. However, as the country's financial crisis deepened in 1967-1968, one is led to believe that the motivation to finance obligations due to suppliers was: (i) to remain in favor with their corporate clients and (ii) to cover promissory notes on suppliers' credit that had already been taken into the banks' portfolio.

Another interesting aspect of refinance in this period was that in 1968 and 1970 banks also were refinancing debts owed to official agencies such as the World Bank and U.S. AID. The need to refinance these "soft" loans with "hard" commercial credit is probably reflective of the various problems that Peru had encountered with one or several official agencies during the 1960s and early 1970s.

Turning to the second period, 1971-1976, one finds that the cost and maturities of refinance credits were in line with global averages. However, there was a higher than average frequency of flat fees and penalties on these loans and the rates employed also were higher than for all loans. The years in which refinance credits were most voluminous were 1974 and 1976, incorporating 65% of all such authorizations. Actually, in the period the government pursued a vigorous strategy of continuous refinance, with motivations changing over time.

In 1972, the government faced what it felt to be a continued debt service problem. Banks were willing to refinance their obligations and obligations of other entities to the sum of roughly 150 million dollars, even though the balance of payments maybe could have supported regular repayments. The banks' receptiveness undoubtedly was at least in part influenced by the growing talk of petroleum in Peru and the generally aggressive behavior of some banks with regard to expansion into LDC markets. Refinance also was attractive because, by being an uncertain

entity, the rate that Peru paid for such credit was 2.25% over libor. This was very much higher than the cost of refinance in the 1960's (1.75 over prime) and even higher than the average cost of all credit for that year (2.08 over libor), not to mention the fact that other LDC borrowers were paying considerably less for their commercial credit.

In 1973 and 1974 the motivation for refinance obviously changed. Here the government, interested in retaining resources for the development program, had also to be motivated by the generally easy access to bank credit and the remarkably more favorable lending terms provided by the banks. By 1974 margins on credit for refinance of older debt were down to 1.19% over libor and maturities were at 10 years. In this type of environment, Peru sought to repay its more expensive credit of 1972-1973 with the newer cheaper loans available to it in 1974.

In 1975 and in 1976 refinance credits stemmed more from considerations of debt service than anything else. With the balance of payments faltering and service on accumulated debt mounting, assistance was needed. In mid-1976 a historic arrangement was struck between the government and its commercial bank creditors. Peruvian officials, for political reasons, wished to eschew an IMF standby agreement and therefore approached commercial creditors for 400 million dollars in refinance credits, which for administrative reasons were formally termed balance of payments loans. As was seen in earlier chapters the banks reluctantly broke precedent by agreeing to refinance the government without the protection of an umbrella IMF accord. The finance secured was as follows:

United States banks	\$210 million
Canadian banks	\$ 30 million
European banks	\$ 90 million
Japanese banks	\$ 32 million
Swiss banks	\$ 24 million <u>34/</u>

and was roughly proportional to the annual payments falling due to each group.

As in the economic crisis of the 1960's, refinance loans were extended on very onerous terms. Maturities were only 5 years with a very short 2-year grace

period. The interest margin was a full 2.25% over libor and front-end fees exceeded 1.5%. Moreover, there was a unique form of conditionality based on the performance of the government's economic program. Given the importance of this credit, and the unusual conditionality applied to it, special in-depth analysis of the whole operation is reserved for the section dealing with bank conditionality in chapter 8.

#### 4. Other types of loans

Loans solely for the purpose of importing goods and not covered by guarantees of a foreign export credit agency were not very important in either period. Most unguaranteed finance for imports came via project lending which was indeed significant. The percentage of total lending for unguaranteed project finance rose from 5% to 15% between the two periods. (See again table 5.11.) The rather sharp rise in the share of project loans is another manifestation of the radical diversification of world banking in the 70's with regard to LDCs. One must be concerned, however, by the fact that average maturities on project loans were only 5.6 years in 1965-1970 and 6.9 years in 1971-1976. In general, one might suspect that these short maturities would scrape the bare minimum needed for commercial ventures and would be wholly inadequate for any investment of less than a commercial nature.

The above leads to a natural interest in knowing just what projects were financed by the banks. However, the whole subject of project lending is so intimately linked to the development program of the country that no further analysis will be carried out here, reserving a detailed view for the impact studies undertaken in Chapter 8.

#### G. CURRENCIES OF COMMERCIAL BANK CREDITS

As pointed out in Chapter 2, all loans have been converted into U.S. dollars for the purpose of generating comparable data. Nevertheless, as table 5.14 shows, dollars were almost exclusively the original currency of Peru's loans, accounting for 98% and 88% of authorizations in 1965-1970 and 1971-1976, respectively. This is not surprising in as much as Peru is in a dollar zone and, in any case, the US dollar was the principal world reserve asset and therefore the predominant currency used in international lending during these periods. It was not until after 1976 when sharp falls in the value of the dollar caused currencies such as the yen and D-mark to take on importance as media for international bank loan transactions. Data merely reflect Peruvian authorities preferences and common practices of the time with regard to choice of currency.

#### H. WHERE COMMERCIAL BANKS BOOKED THEIR LOANS

Commercial banks can book their loans in any number of places. The headquarters of the commercial bank is one logical place, but banks also may place a loan transaction in any one of their branches and subsidiaries throughout the world. There are various motives for placing loans in entities other than the headquarters of the banks. Some banks have a rather decentralized network and a branch or subsidiary could simply have taken initiative on a loan and booked it in their office. On the other hand, a parent may simply wish that a loan appears on the books of a subsidiary for reasons associated with marketing strategies, politics or convenience. But it has become common for banks to book loans in certain entities abroad for tax purposes.



Table 5.14  
PERU: CURRENCIES OF COMMERCIAL BANK LOANS, 1965-1976 <sup>a/</sup>  
(Percentage of total)

	1965-1970	1971-1976
U.S. Dollars	98.1	88.9
D. Marks	1.4	1.9
Swiss Francs	0.1	0.4
French Francs	-	2.9
Yen	-	0.5
Pounds	-	3.2
Lira	0.4	-
Guilders	-	1.5
Canadian Dollars	-	0.8
Other	-	-
<u>Total</u>	<u>100.0</u>	<u>100.0</u>

Source: CEPAL on the basis of official data.

<sup>a/</sup> All credits, guaranteed and unguaranteed.

Most international banks have established branches and subsidiaries in so-called offshore centers. 35/ Different centers may serve different purposes. Some centers may prove attractive basically as a locus for interbank deposits and funding. London, the seat of the Eurocurrency market is a case in point. Other centers may prove attractive because of their relative freedom from regulations, thus permitting banks to engage in activities that home government authorities restrict (e.g. Luxembourg). Other offshore centers, however, are unabashed tax havens where the main attractions for the banks are the absence of income taxes, the complete freedom to transfer funds according to the prerequisites of the bank, and a time zone which facilitates the global movement of funds around the clock. These centers serve as formal way-stations for bank assets and liabilities, but their branches and subsidiaries are often only shell offices with a nameplate and post office box. Actual transactions are undertaken by headquarters and movement of funds into and out of the center is merely a bookkeeping event undertaken by headquarters.

These tax havens can be used in various ways. One common way is to generate profits on foreign exchange transactions. For instance, a Brussels branch of a bank can sell foreign exchange to a Bahamas' branch at a loss and then the Bahamas branch can resell the exchange back to Brussels at a profit. All the transactions are internal to the bank, so no real profit or loss is realized. But the tax effects can be considerable. The Brussels' branch records a loss, which is convenient for a country with a high marginal tax rate. Meanwhile, profits are recorded in the Bahamas where there are simply no income taxes at all.

Another type of transaction which is of more relevance to this study involves loans. The value of booking a loan in a tax haven depends to some extent on tax regulations of the home country of the parent bank. For instance,

in the case of U.S. banks, tax officials permit their banks to credit taxes paid on foreign income in excess of the U.S. rate of 48% to other foreign income taxed at lower rates than the U.S. rate. 36/ Thus, U.S. banks have incentive to generate income in low tax areas and there is no better place to do so than in a tax haven. Two favorite tax havens for U.S. banks are the Cayman Islands and the Bahamas. Non U.S. banks also operate out of these centers. 37/

Table 5.15 breaks out areas where banks have booked their loans to Peru.

As is seen, in the first period, headquarters was the source of an overwhelming number of loans. This is consistent with the circumstances of the time. First, loans to Peru were small in absolute terms and therefore could be funded easily out of domestic financial centers. And banks would be inclined towards home country finance because the cost of funds usually is cheaper than in an offshore center like London with its high overhead costs. Second, medium term loans to LDCs were not yet commonplace, so such transactions probably were of personal concern to top executives at headquarters. Third, in the 60's expansion of branches and subsidiaries abroad for the purpose of building up an international loan portfolio was still at an early stage of development; moreover, banks were just beginning to realize the tax advantages of offshore banking centers.

The table shows a radical change in the booking of loans in 1971-1976. While headquarters remained the dominant station for loans, its share fell from 95% to 48%. Meanwhile, London rose in importance, as LDC loans became frequent enough to require the tapping of dollar pools in the eurocurrency market. 38/ Meanwhile, tax havens like the Bahamas came into vogue among bankers.

One might observe that bookings in the Bahamas are quite high at 17% of total authorizations, while Panama is quite low at 3%. This comes as something of a surprise since it was thought that an established offshore center like Panama might be a major station for loans to a Latin American country like Peru. This

Table 5.15

PERU: WHERE COMMERCIAL BANKS BOOKED LOANS, 1965-1976<sup>a/</sup>

(Percentage of total lending)

	1965-1970	1971-1975
Headquarters	95.1	46.9
London	-	14.1
Bahamas	-	17.4
Panama	0.2	3.0
Cayman Isles	-	2.1
Paris	-	0.7
New York	1.0	1.1
Luxembourg	-	5.4
Switzerland	-	0.3
Other	-	0.9
Unspecified <sup>b/</sup>	3.6	8.1
<u>Total</u>	<u>100.0</u>	<u>100.0</u>

Source: CEPAL on the basis of official data.

<sup>a/</sup> All credits, guaranteed and unguaranteed.

<sup>b/</sup> Unable to determine where booked.

suggests that the two centers play rather distinct roles for international commercial banks. It also suggests that the Bahamas may merit a detailed study as a financial center.

## I. SOVEREIGN IMMUNITY AND LEGAL JURISDICTION

In this last section of the chapter, one will review two legal aspects of commercial bank loans that have been a source of friction for LDC borrowers: waivers of sovereign immunity and local jurisdiction over credit agreements.

Lending to governments obviously is different from lending to private entities. The differences are reflected in the fact that bankers see not only commercial risks in lending to governments, but also sovereign risks. Sovereign risks stem from three special privileges that governments enjoy:

"First, they may not be sued without their consent, in their own courts or the courts of another country. There are some exceptions in some countries but, as a general proposition, a government or its instrumentality has an immunity against service of legal process. Second, the courts of one country will not ordinarily sit in judgement as to the acts or omissions of another country occurring within its own territory. Again, there are some exceptions, but, as a general proposition, even if a government can be sued, it may successfully defend on the ground that the propriety of its acts or omission in its own country is not open to question in any country. Third, property of a government or its instrumentality is immune. So, even if a government consents to be sued, and even if a court pronounces judgement against it, the judgement may not be enforceable. 39/

While banks may make an excellent assessment of the economic and commercial risks associated with a government loan, the element of sovereign risk is a highly uncertain factor that is difficult to control.

Bankers tend to protect their loans as far as possible. They generally like to resolve repayment problems without taking recourse to legal measures, but in the event that this proves necessary, bankers want to ensure that a

borrower cannot escape due process. Thus, banks usually seek disclaimers of sovereign immunity. This so called waiver of sovereign immunity is generally considered to be an indispensable protective clause.

On the other hand, developing country borrowers are notorious for their distaste for such waivers. Generally governments find the clauses to be an affront to their national sovereignty and a potential limitation on their freedom of action. Nevertheless, bankers wishes for this type of protection generally have prevailed and the waiver is almost a standard clause in loan contracts. In the case of Peru, the clause was most frequent. Because of the many ways such a clause can be incorporated into an agreement, it was difficult to precisely quantify the existence of waivers. But data in the study suggest that at a minimum one half of the value of all credit in 1971-76 carried disclaimers of immunity. Peru was not alone in this case, as just about all other developing country borrowers have had to face the same clause.

Only recently have some borrowers openly defied banks efforts to have them sign away their immunity to prosecution. However, success is far from generalized and waiver remains the rule rather than the exception. One cannot help but wonder to what extent such clauses are a needless irritant to developing countries. In the event that an open confrontation arises over a loan, if a government does not have the political will to settle the disagreement, no court inside or outside the borrowing country can force it to submit to the views of the bank. In the end, repayment rests on the good will of the government to honor its obligations. Any clause that makes a government waive its right to sovereignty is really a form of false security for the bank that covers over the real underlying forces behind repayment. This fact is aside from the consideration that there is considerable doubt about whether any court would agree to hear a case involving a sovereign government. 40/

The subject of legal jurisdiction of a loan agreement is not unrelated to the issue of sovereign immunity. It also is a focal point of disputes between the borrower and the lender.

Bankers, of course, prefer to have the legal jurisdiction over the loan contract in their home country or some other industrialized state. Thus, if a dispute is taken to court a bank can enjoy the familiarity of its country's legal environment. Sovereign governments, however, are usually loath to the idea of submitting to the courts of a foreign entity, for reasons which are obvious. Here again banks have prevailed in as much as it is almost a rule of thumb that an industrialized country, and particularly the home country of the lender or lead bank, be the legal site for adjudication. 41/

In the case of Peru, it is illegal for the government to submit to foreign courts. This is because article 17 of Peru's 1933 Constitution states that all contracts between the state and foreign entities must be under Peruvian legal jurisdiction. 42/ However, in almost all the loan agreements with Peru, the banks have been able to insert clauses establishing the legal jurisdiction in their home country. To take into account article 17, the jurisdictional statement is usually followed by a sentence such as this: "Only to the extent required by article 17 of the constitution of the Republic of Peru will the banks submit to the laws and courts of Peru".

The last hedge by the banks, which appears to be obligatory for a legal contract, would seem to imply that Peru could be the ultimate jurisdictional setting for any dispute. But if this is so, why do the banks insist on establishing their home country as the juridical site? Again this type of clause would appear to serve more as a needless affront to the government than a real form of security to the banks. It also might lead to confusion should a legal dispute actually arise.

The whole issue of legal jurisdiction could be worth reconsideration. After all, the jurisdictional clause is of little use if a borrower really wishes to take an independent position on a dispute. Moreover, banks, being transnational, would appear to be in a much better position to adapt themselves to the legal environment of the borrowing country than vice versa. And if a borrower should feel so strong about its position so as to distort the national juridical process in order to gain a favorable decision, it also is unlikely that it would accept a negative judgement from the courts of a foreign country. In the end it is the good faith of the government that secures a loan, so demanding legal jurisdiction that is alien to the borrower only may serve as ephemeral protection to the bank, and as lasting indignation to the borrower.

Despite the fact that there are serious reasons to question the utility of waivers of sovereign immunity and jurisdiction, one must understand the psychological comfort such clauses provide risk conscious bankers. If they were unable to have this security, bankers might become reticent to lend at all. Thus, it seems prudent to seek a compromise. Why not substitute the two clauses for some form of international arbitration should disputes arise? Indeed, a few European banks have adopted this measure and it might be worthwhile for other international banks to follow this practice as well.

#### SUMMARY

The preceeding analysis has graphically shown the radical changes in Peru's interface with its commercial creditors over the period 1965-1976. Not only was there a dramatic increase in the number of commercial creditors, but the nature of lending and mechanisms for finance also underwent a marked transformation. The next chapter will focus on a specific aspect of this transformation: the syndicated credit.



Chapter 5

FOOTNOTES

1. The amounts corresponding to the groups for 1971-1976 are larger than for 1965-1970 due to the greater volume of lending in the former, but in relative terms the scales for the two periods are approximately equal. The authorizations themselves include credits with guarantees of export credit agencies; however, where elimination of these "guaranteed" credits would change the group in which a bank is positioned, this is indicated in a footnote to table 5.1. The reader is warned that great caution is merited with regard to the classification of credit into guaranteed and unguaranteed loans. In some cases a borrower may not have been aware of the presence of an external guarantee on a commercial bank credit and therefore in such a case no record would be maintained to this effect. Another problem peculiar to the period 1965-1970 is that debt contraction and record keeping were exceptionally haphazard, generating the possibility that contemporary archival systems have only incomplete information on guarantees.
2. See Kuczynski, p. 257.
3. Up through 1976 U.S. banks had generally dominated lending to non-oil exporting developing countries like Peru. One estimate has placed their participation in lending to this group at roughly two-thirds of the total value of loans. See Wionczek, p. 184.
4. See The Banker, June 1970, p. 601.
5. The international rankings for each range of assets are different for the two periods because the independent variable is dollar asset size and thus the number of banks corresponding to any given range of assets varies according to the growth rates of the banks.
6. Obviously in practice someone had to initiate contacts with other banks. In the case of several sizeable multibank loans in support of the fiscal budget it appears that Manufacturers Hanover played this role. Incidentally, to the extent that Manufacturers was the main organizer of these credits, this would distinguish it from the other major lenders of the period and perhaps give it the title of being Peru's single most important creditor in the latter half of the 1960's.

7. For a good review of the role of the agent and the lead banks in loan syndication, see Moissi. Also see Bee.
8. It was not possible in all cases to establish the precise type of prime rate employed by the banks; however, information was available for a majority of the credits and suggests that the basic benchmark was the U.S. prime rate.
9. As was pointed out in Chapter 4, Peru was considered to be reasonably creditworthy by the banks, although in 1967-1968 they were obviously having second thoughts about their evaluation of risk.
10. One might be curious about how the floor/ceiling mechanism affected the borrower in practice. This is difficult to determine because, as will be seen later in the chapter, most loans were continuously being refinanced so that credit agreements rarely lived out their original term. Nevertheless, some indication is provided by reference to the memorandum items in table 5.6 and data in figure 5.1. Here it can be seen that the floor interest rate of  $6\frac{3}{4}\%$  and  $7\%$  did not really prejudice the borrower because the prime rate was never low enough to generate an overall rate (prime plus spread) that was less than the minimum established by the credit agreements. On the other hand, credits that bore the ceiling of  $8\frac{3}{4}\%$  could have been favorable to the borrower since in 1968-1970 the prime rate reached levels whereby a  $1.75\%$  spread would have generated costs in excess of the maximum established rate. The very results of the floor-ceiling rate arrangement contributed to its demise after 1970. For such practices to survive there had to be prospects of relative world price stability. But with world inflation accelerating, a floor interest rate had no practical benefits for a lender. On the other hand, in an environment of rising world prices, a ceiling rate on a medium term credit could only be highly prejudicial to a lender. Thus banks found it convenient to rely solely on a pure floating rate.
11. See Sanchez Aguilar, p. 171.
12. The regulation was the Voluntary Foreign Credit Restraint Program initiated in 1965. For details of the program see Aronson (1977) Chapter 4.
13. This is because of the severe asymmetry of information; while this study has generated rather comprehensive data on Peru's borrowing from commercial banks, similar data on other countries is rather sparse. Moreover, any comparison of Peru with data of other countries could suffer from discrepancies associated with methodology.

14. See Devlin (first half of 1978), p. 77.
15. To quote a public commentary of one of the world's largest commercial banks: "In this regard Brazil's delay in international adjustment has come as a disappointment. There, the growth in the aggregate demand, the reemergence of the fiscal deficit, and the acceleration of inflation (estimated at 40-50% for this year) have been inconsistent with the clear necessity for a current account adjustment". See Morgan Guaranty Trust Co., (October 1976), pp. 3-4.
16. In the early 70's U.S. banks accounted for roughly half of Mexico's liabilities with commercial banks; furthermore, these institutions have had an almost unlimited willingness to lend to the country (see Sanchez Aguilar, pp. 174 and 262). And as for the reason for this attitude, Aronson (1977, p. 175) has pointed out: "American lenders also are attracted by Mexico's contiguous border with the United States. Most creditors feel that the U.S. government is so involved with Mexico's economy that it would aid the Mexican government and U.S. lenders if disaster struck".
17. See CEPAL, Estudio Económico de América Latina 1975, p. 132.
18. One can see that Brazil consistently had longer maturities than Mexico, which is one reason for the former country's higher interest margins.
19. In a few loans to Peru banks actually prohibited prepayment.
20. In cases where penalties were scaled according to the year of prepayment, averages were taken by weighting with the number of years in which a particular rate prevailed. Of course, the presence of scaling makes averages understate the effective cost of prepayment penalties in the earlier years of a loan and overstate it for the later years.
21. See Lewis, p. 60.
22. These banks joined together in multibank agreements. Several other American banks variously tagged onto this core group of commercial banks to extend credit in lesser amounts. Of these secondary lenders, the most important was the Charter New York Corporation (Irving Trust) which provided 5 million dollars in a free disposition loan of 1967.

23. Kuczynski, p. 165.
24. Kuczynski provides some insight into the attitude of the banks just prior to signing of the agreement: "At 2 p.m. on July 31, a Monday, The Ambassador of Peru to the United States sat in the beautiful office of the former Chairman of the board of the Manufacturers Hanover Trust Company, then at 44 Wall Street, waiting to sign the U.S. \$40 million dollars loan agreed to by the banks ten days before. The bank representatives were gathered in the board room next door, supposedly finishing last-minute details in the loan agreement. But the week-end news from Peru had come in the morning, and some of the banks were now hesitant. Not only had the President been unable to make his annual state of the nation message, but there had been a new development in the International Petroleum Company case as the Peruvian Congress had declared the subsoil claimed by IPC at La Brea y Pariñas to be the property of the state. The possible attitude of Standard Oil of New Jersey, the owner of IPC, was obviously important to the banks, which were depositories of large Standard Oil funds. Some discussions followed with the Peruvian delegation, but the loan agreement had been negotiated two weeks before and could not be changed in Peru, where it had been approved by the Controller General. Finally, at 4.45 p.m., as some of the bankers began to fear that they would miss their trains home, the loan documents were signed", Ibid., pp. 167-168.
25. Bank of America, Bankers Trust, Chemical Bank, Continental Illinois, First National Bank of Chicago, Franklin National Bank, First Pennsylvania Banking, Crocker National Bank, Fidelity Bank.
26. As already mentioned in Chapter 2, the principal negotiator for the U.S., James Greene, was a high ranking official at Manufactures Hanover Trust. It is significant that his bank did not participate in the 76 million dollar credit.
27. Other banks were Credit Suisse, Union Bank of Switzerland, Swiss Volksbank, Banque Lev, and Privatbank Verwaltungsgesellschaft.
28. The Swiss later made this 10 million dollars a part of their contribution to a general refinance accord arranged with international banks that year.
29. The credits for the fishing industry were of somewhat different nature than the other nationalization credits. At the time of nationalization, the industry was heavily indebted both at home and abroad, suggesting that the banks, while ostensibly facilitating the government's purchase of nationalized

assets, were, to some extent, simply refinancing obligations due to them by the former private sector entities. All together, 86% of commercial bank credits directed towards the nationalization of the fishing industry was from American institutions. This is consistent with the fact that prior to 1972 U.S. banks were the dominant lenders to Peru and that U.S. firms were by far the most important foreign investors in the industry (see footnote 89 of chapter 3).

30. An official of one commercial bank has expressed this point of view as follows: "It goes without saying that refinancing is undertaken by most banks ... only very reluctantly and only for customers with whom ... (they) have excellent long term relationships". See Benny, p. 57.
31. Banks believe that rescheduling of their credit would cause a borrower to lose its creditworthiness. See Friedman, p. 69.
32. See Lewis, pp. 65-66.
33. Initially refinance of suppliers' credits was heavily concentrated on obligations of SOGESA, the state steel enterprise. In the early and mid-60's SOGESA underwent an ambitious expansion program in which Ferrostaal A.G. Essen was the main contractor. SOGESA, being financially weak, negotiated postponement or reduction of debt payments with Ferrostaal and in 1965-1967 many of the upcoming payments to Ferrostaal were financed by American, Canadian, and German banks, with a guarantee provided by the central government. For details on the SOGESA expansion program and the role of Ferrostaal see the Memoria for 1964 and 1965 of SOGESA.
34. The Swiss negotiated outside the general agreement with the other international banks. For methodological reasons this credit has been considered a 1977 transaction and therefore is outside the scope of the present study.
35. For information on the various offshore centers consult the Banker Research Unit. Also see Daggart.
36. For a full descriptive example of how U.S. banks use tax havens to their advantage, see Lissakers, pp. 18-21.
37. Different national banks tend to prefer different centers. For data on how various national groups of banks used offshore centers, see table A 5.3 of the statistical appendix.

38. For U.S. banks London became an essential element in the funding of massive LDC loans because the Voluntary Foreign Credit Restraint Program placed absolute limits on foreign lending from home offices. See Aronson (1977), Chapter 4.
39. Hartfield, p. 86.
40. See Sandeman, p. 77.
41. An exception is Colombia, which has successfully demanded that "the loan agreement will be subject to Colombian jurisdiction". See Ensor, p. 98.
42. See Ugarteche (1979), p. 15.

## Chapter 6

### SYNDICATED CREDITS TO PERU

Chapter 5 offered some observations on syndicated loans during the 1970's. Given the importance of these credits—they accounted for nearly 80 per cent of all bank finance in 1971-1976—and their rather complicated structure, special attention will be devoted to them here.

#### A. INTRODUCTION

In the 1960's most commercial bank loans in the eurocurrency market were arranged by individual banks and the amount of credit on any one transaction rarely exceeded 15 million dollars. However, as was seen earlier in the case of Peru, when lending from home markets some banks had found advantages in joining together in multi-institutional agreements; more credit could be extended to the borrower at less risk to the individual banks; there was one umbrella agreement for all participating institutions; greater leverage over the borrower, etc. In 1968 Bankers Trust extended the concept to the international market where it arranged a 100 million dollar euro-syndicated credit for the government of Austria. <sup>1/</sup> Then in 1970 Manufacturers Hanover headed a 200 million syndicated credit to the government of Italy. This loan had all the trappings that have become associated with syndicated credits: a 5 year medium term maturity, 3/4 per cent spread over libor, and front-end fees of one half per cent. <sup>2/</sup>

The 1970's saw the syndicated credit evolve into the dominant mechanism for the extension of international credit. As ever more banks became anxious to build up international portfolios, the magnitude of eurocredits exploded. It has been estimated that in the first half of the 1970's roughly 25 per cent

of the value of funds provided in syndication were in the form of transactions of \$500 million dollars or more. 3/

As noted earlier, syndicated credits are arranged by a lead bank which takes responsibility for negotiating with the borrower over the terms and conditions of a credit. Once an amount of credit is established and the lead bank feels that it has terms attractive enough to form a syndicate, it will seek bids from other banks to join in the operation. In order to inform banks—especially small and medium-sized institutions with limited ability to assess international borrowers—of the borrower's creditworthiness, the lead bank prepares a placement memorandum with details on the borrower, its creditworthiness, and the general terms and conditions for the loan.

In order to facilitate formation of a syndicate, the lead bank often offers some prospective participants the role of co-manager in the syndicate. This gives the prospective participants greater incentive to join the operation; not only is their voice in negotiations increased, but they gain publicity as an organizer of the credit and, most importantly, enjoy a share of the fees that, as was seen in the previous chapter, have become most common to commercial loans of the seventies. The lead bank also might offer a share of the fees to ordinary participants as well.

The dollar participation of the lead bank and co-managers in the syndicated credit will vary according to the management style of the banks and the market's response to the offer of syndication. If the loan is over-subscribed, the lead bank and managers can reduce their participation in the credit to a minimum, if desired, leaving income generation basically to the almost risk free front-end fees that accompany the credit. On the other hand, if the syndication bid is undersubscribed, the lead bank and co-managers must fill in the gap with a higher participation than originally anticipated, or declare the syndicate unrealizable, at least under the originally agreed terms and conditions. In a borrower's market such as that of the first half of the 1970's, the lead bank and



managers might very well decide to increase their participation above that which was originally planned in order to avoid the embarrassment of a failure to organize a credit. The banks then could contemplate selling off their unwanted participation at a later date. However, this latter strategy, which is not infrequent, requires a lead bank to be of some size; a small bank just would not be in a position to fill substantial gaps in syndication.

The whole process of organization of a credit can take up to 3 months for borrower of low status in international markets and as little as four weeks for a well known first rate client. The sequence of events in the formation of a syndicated loan is described in table A6.1 of the statistical appendix. 4/

Once the agreement has been signed, it is the role of the agent bank to administer and enforce the contract. While in theory the agent can be any one of the banks in the syndicate, in practice the role usually has been taken up by the principal lead bank, thereby giving it rights to the special administrative fees. 5/

#### B. THE GENERAL CHARACTERISTICS OF SYNDICATED LOANS TO PERU

As was noted in the previous chapter, syndicated loans first appeared in Peru 1971-1972, simultaneously with the process of general penetration of this market by international commercial banks. The basic characteristics of syndicated credits are outlined in table 6.1.

As can be seen, the average size of syndicated credits for the period 1971-1976 was 41 million dollars. 6/ This contrasts with an average size of \$5 million dollars on single bank loans in the same period. The average number of banks in each syndicated credit was 15 and the average participation was only 2.8 million dollars. This latter figure is very illustrative of how banks minimized their individual risk on large transactions. And as far as the

Table 6.1

PERU: BASIC CHARACTERISTICS OF SYNDICATED LOANS, 1971-1976<sup>a/</sup>

1.	<u>GENERAL</u>	
	a) Percent of all credit mobilized via syndications	78.7
	b) Average size of syndicated credits (millions of dollars)	41.2
	c) Average number of banks per syndicated credit	15
	d) Average size of the banks (assets, equivalent international rank) <sup>b/</sup>	27
	e) Average participation of the banks (millions of dollars)	2.8
2.	<u>LEAD BANKS</u>	
	a) Number of banks acting as lead banks <sup>c/</sup>	46
	(- as agent)	(22)
	(- as managers)	(35)
	b) Average size of lead banks (equivalente international rank) <sup>b/</sup>	17
	(of agent)	18
	(of managers)	15
	c) Percent of syndicated credit extended by the lead banks	35.1
	(by agent)	16.8
	(by managers)	18.3
3.	<u>PARTICIPATING BANKS</u>	
	a) Number of banks acting as participants in syndication <sup>c/</sup>	15
	b) Average size of participating banks (equivalent international rank) <sup>b/</sup>	41
	c) Percent of syndicated credit extended by the participants	64.9

Source: CEPAL, on the basis of official data.

a/ All credits, guaranteed and unguaranteed.

b/ See footnote c of table 5.3.

c/ Each bank has been counted only once for each category. However, since a bank could appear more than once as an agent, manager, and participant, the total number of banks exceeds the total number of institutions in the study. Also note that a manager that also was an agent was counted only as an agent.

average size of the banks—weighted by the value of their participation—involved in syndication, it was rather large; the average size based on assets was equivalent to 27 on a world ranking of 1 - 300.

Table 6.1 shows that 46 individual banks at least once played the role of agent or manager in a syndicated credit. However, assuming the agent as being the principal lead bank in syndication, the role of organizer of these loans fell into the hands of just 22 banks, or only 13% of the institutions in the study. This has implications which will be dealt with later in the subsection on Peru's lead banks.

As for the size of the lead banks, they tended to be very large institutions. The average international rank of the agents was 18 while it was 15 for the managers. This would support a priori notions that to be a successful lead bank one must generally enjoy the prestige of size and the broad international contacts that only large banks can have.

The agent and manager jointly accounted for slightly more than one-third of the credit in syndicated loans. Notably, the agent alone accounted for somewhat more than one-sixth of the credit. Managers, of which there may have been several in any one credit, or none at all, accounted for 18% of the value of syndicated loans. Given that there were many more managers than agents involved in transactions, each individual agent, (or principal lead bank), on average, obviously carried a relatively greater burden of loan commitments.

With regard to the participating banks, 155 institutions joined in a syndicated credit at least once. As would be expected, their average size was much smaller than the lead banks, equivalent to 41 on the scale of world rankings. And they accounted for the bulk of credit, with 65% of the total value of syndicated credits.

C. COST COMPARISONS BETWEEN SYNDICATED AND NON-SYNDICATED CREDIT

Syndicated credits clearly have an advantage over single bank loans with regard to the amount of resources that can be mobilized in any one transaction. But the question remains: how do syndicated credits compare with single bank credits in terms of cost? This can be determined by viewing the average terms on each type of credit that are presented in table 6.2.

It is seen from the table that syndicated credits generally had slightly higher labor spreads, somewhat longer maturities and significantly higher fees and prepayment penalties. These differences are more or less what one would expect and reflect the different nature of the two credits.

A syndicated credit is a rather impersonal transaction, as opposed to the very personal nature of a single bank loan. Thus in order to ensure that a syndicate is realized, an agent must sometimes set interest spreads at a rate high enough to attract marginal participants who have little to gain from the transaction but income. This situation also explains the relatively higher fees/penalties on syndicated loans. In contrast, in a single bank loan the lender can have motivations that are broader than income on the specific transaction e.g., image-making, support of a home country foreign supplier, etc. Also, fees can be lower because they do not have to be split among a number of institutions, as is the case of a syndicated loan.

Aside from a slightly higher interest rate, the longer maturity on syndicated credits is probably a function of the nature of the loans. In a single bank loan the lender cannot share the risk of the transaction as it would do in the case of a syndicated credit. Also, a single bank credit can involve a commitment that is large relative to what a commitment would be in a syndicated loan. (The average participation in a syndicate was 2.8 million

Table 6.2

PERU: COMPARISON OF AVERAGE TERMS BETWEEN SYNDICATED CREDITS  
AND LOANS ADVANCED BY A SINGLE BANK<sup>a)</sup>

		(averages)				
		1972	1973	1974	1975	1976
1.	<u>Average spread over libor</u>					
	Syndicates	2.08	1.68	1.13	1.79	2.19
	Single credits	2.01	1.61	1.15	1.72	1.96
2.	<u>Maturity (years)</u>					
	Syndicates	6.26	8.79	9.57	5.64	5.0
	Single credits	6.0	8.13	8.68	6.37	3.24
3.	<u>Flat fees (%)</u>					
	Syndicates	0.29	0.45	0.29	0.95	1.42
	Single credits	-	0.076	0.073	0.363	0.305
4.	<u>Prepayment fees (%)</u>					
	Syndicates	-	1.43	0.71	0.91	1.49
	Single credits	0.50	0.76	0.73	-	-

Source: Cepal on the basis of official data.

a) Averages are weighted by the amount authorized. Only for credits without guarantees of export credit agencies.

dollars, while that for a single bank loan was 5 million dollars.) All this would incline single lenders towards shorter maturities than would be available on a syndicated credit.

Seeing generally more favorable terms on single bank loans might suggest a strategy aimed at inducing more banks to lend on their own. However, in the end syndicated credits would appear to offer more advantages to the borrower. The longer maturity on these transactions are very important to LDC borrowers and could offset any disadvantages related to interest margins or fees. Moreover, syndicated loans—by virtue of their large size—probably are less taxing to the limited negotiating capacity of many LDC borrowers and certainly present less of an administrative burden than would the hundreds of individual credit agreements that would be needed to substitute syndicated credit flows.

#### D. THE LEADERS OF SYNDICATED CREDITS

The key personality in syndicated credits is the lead bank. Its good will is rather important to the borrower's success in maintaining a link to international capital markets. The drawing power of a lead bank can determine the costs and conditions of credit; moreover, the market's view of the borrower can be influenced by the evaluation of the country that is commonly found in the placement memorandum prepared by the lead bank. Also, the lead bank most often administers a signed credit and thus is the institution with which the borrower must deal in the event of problems during the life of a loan agreement.

Thus the lead bank adds another dimension to the role of commercial institutions in the Peruvian economy. It has been seen that some banks are rather important creditors to Peru. However, it is now clear that a bank can be even more important without having lent to the government at all by acting as a major lead institution in syndication. As it turns out, however, many of

Peru's important lenders are also important lead banks, making their leverage over the Peruvian economy that much more prominent.

A syndicated credit formally can have a number of lead banks. However, many managers in a syndicate often are institutions which have only a secondary role in the organization of a credit and many times they are designated as a manager simply as an inducement to provide a larger participation. (A manager benefits from fees and publicity.) In those cases where there are several managing banks in a credit, the principal lead bank most often is the manager that also is designated as the agent. <sup>7/</sup> Thus, table 6.3 presents Peru's agent banks under the assumption that they are also the country's main organizers of syndicated loans. <sup>8/</sup> Banks are ranked as agents of major, intermediate and minor importance according to the percentage of the total value of syndication that was mobilized by them. The table also shows the average participation of the lead bank in its own syndicates and the bank's position with respect to the top lead banks in world credit markets.

One sees that Peru's top lead banks are Citicorp and Wells Fargo, both of whom were classified in the previous chapter as major lenders to the government. By virtue of their top positions as lenders and mobilizers of credit on international credit markets for the government, these two banks stand out for their importance to Peru.

Considerably behind Citicorp and Wells Fargo as lead banks to Peru are Manufacturers Hanover, Dresdner Bank and Bank of Tokyo. All three fall into an intermediate level of importance as mobilizers of credit. As lenders, the first bank was classified as a major institution, while the latter two were classified as of intermediate importance.

One also sees a number of banks classified as minor mobilizers of international credit. Of this group, most were classified as lenders of intermediate importance to Peru. Chase Manhattan was, however, a major lender.

Table 6.3

PERU: AGENT BANKS ACCORDING TO THEIR IMPORTANCE AS MOBILIZERS OF CREDIT, 1971-1976a/

Amount mobilized by agent as a percent of the total value of all syndicates <u>b/</u>	Percent participation of agent in its own syndicates (average)	International Bank as lead bank in	
		1975 <sup>c/</sup>	1976 <sup>d/</sup>
<u>Major agents</u>			
1. <u>19 - 24</u>			
Citicorp	10.7	1	1
Wells Fargo	12.8	8	18
2. <u>14 - 18.9</u>			
<u>Intermediate agents</u>			
3. <u>9.0 - 13.9</u>			
Manufacturers Hanover	23.6	6	7
Dresdner Bank	16.4	...	5
4. <u>5 - 8.9</u>			
Bank of Tokyo	15.5	...	...
<u>Minor agents</u>			
<u>&lt; 5</u>			
Chase Manhattan	74.0	4	3
Bank of Nova Scotia	33.3	...	...
Bankers Trust	33.3	...	8
Banca Commerciale Italiana	50.0	...	...
Morgan Guaranty Trust	11.8	3	4
Crocker National Bank	10.0	...	...
Lloyds Bank	40.0	10	...
Swiss Bank Corporation	28.2	...	...
National Commercial Banking Group	17.3	...	...
Credit Lyonnais	50.0	5	9
Banque de L'Indochine et Suez	25.0	...	...
Algemene Bank Nederland	50.0	...	...
American Express	20.0	...	...
Compagnie Financiere de Paris Et des Pays-Bas	50.0	...	...
European American Bancorporation	10.0	...	...
First Chicago Corporation	8.3	12	21
Western American Bank Ltd.	16.3	...	...

Source: CEPAL, on the basis of official data; ranking of lead bank is as follows:

1975, the International Herald Tribune, November 1976;

1976, Euromoney (April 1978).

a/ All credits, guaranteed and unguaranteed.

b/ Total value of syndicates for which the bank was agent divided by the total value of all syndicates to Peru.

c/ Rank within the top 15 lead banks in world syndication.

d/ Rank within the top 21 lead banks in world syndication.



Looking at the international rankings in the same table, one notes the direct relation between the banks' position as lead bank for Peru and their position in world markets vis-a-vis major world lead banks in 1975 and 1976. It is seen that Citicorp was not only a top lead bank for Peru, but also for the world market. Wells Fargo also figured as a major world lead bank, but it was far down the list from Citicorp. Thus its role as lead bank in Peru was more than proportional to its position on a world scale, suggesting a behavior vis-a-vis Peru that was rather special. As will be seen throughout the course of the study, this is just one of many indicators of a special relationship between this bank and Peru.

With the exception of the Bank of Tokyo, lead banks of intermediate importance to Peru were also major lead banks on world markets. It can be seen that among minor lead banks for Peru, four were among the top lead banks in world syndication. Chase Manhattan stands out in this regard; it was a principal lead bank in world syndication, but only a minor lead bank for Peru. However, one should remember that Chase was the lead institution on the 200 million dollar syndicated credit for the privately-owned Cuajone copper mine, which does not figure in the data base of the study. If this credit were taken into account, Chase could then be considered a major lead bank of the country as well. It also is worthwhile to point that Lloyds Bank was a leader on a 23.5 million dollar credit to Cuajone.

The last and most important conclusion about the major lead banks for Peru is that a relatively few of them were responsible for a disproportionate amount of mobilized credit. The five top lead banks accounted for more than three-quarters of the total value of mobilized credit. This makes Peru's dependence on a few key institutions for access to international capital rather impressive and heavily conditions the earlier finding of chapter 5 that showed a great degree of dispersion in the sources of funding in the 1970's as compared

to the heavily concentrated commercial funding of the 1960's. Indeed, while the concentration of commercial lenders was dramatically reduced in the 1970's, it was a manifestation of increased possibilities for international lending that was generated by the emergence of syndicated credits. And syndicated credits brought a new form of concentration of economic power, as manifest by the handful of banks responsible for organizing Peru's international loans. This concentration of power incidentally also is present in international markets where a coterie large banks dominate of mobilization of syndicated credit. 9/

1. Lead banks grouped according to country of origin

Table 6.4 breaks out agent and manager banks according to their country of origin. The number of lead banks for each country, the percentage of credit mobilized by each country group and the percentage of participation in syndication also is presented.

It is evident that the dominate lead banks, both in terms of their number and the value of the mobilization of credit are U.S. institutions. No other country group comes near the U.S. in terms of their role in mobilizing international credit. It was found in the previous chapter that U.S. banks were still dominant as lenders to the government, notwithstanding the notable dispersion in the sources of funding in the period 1971-1976. But it would appear from an examination of tables 5.3 and 6.4 that this dominance is even more important from the standpoint of leading syndicated credits. Moreover, if leadership is defined as being the agent bank--which usually is the lead bank--than the dependence on U.S. institutions is rather overwhelming, both from the standpoint of the number of lead institutions and the total value of their mobilizations. Thus another example of how just looking at the absolute level of authorizations

Table 6.4

PERU: LEAD BANKS GROUPED ACCORDING TO COUNTRY OF ORIGIN, 1971-1976<sup>a/</sup>

Country of the banks	No of lead banks <u>b/</u>			Percent of all syndicated credit mobilized by lead banks <u>c/</u>			Percent participation of leaders in their syndicated credit		
	Total	Agent <u>d/</u>	manager	Total	As agent <u>d/</u>	As manager	Total	As agent <u>d/</u>	As manager
United States	14	9	13	76.0	68.8	29.1	27.2	15.3	34.9
Japan	6	1	5	15.0	7.5	11.7	15.9	15.5	10.5
Canada	5	1	5	18.6	1.7	16.9	16.7	33.3	15.0
United Kingdom	3	2	2	14.9	1.0	13.9	10.1	23.7	9.1
Germany	2	1	1	13.1	13.1	1.4	20.9	16.4	41.6
France	3	3	1	6.4	1.2	5.2	13.3	42.7	6.6
Italy	2	1	1	6.8	.3	6.5	9.3	50.0	7.1
Switzerland	2	1	1	4.4	2.7	1.7	22.4	28.2	13.3
Other	3	1	2	13.3	1.1	12.1	7.5	50.0	3.5
Consortium	6	2	4	12.3	0.8	11.6	8.9	12.8	8.6

Source: CEPAL, on the basis of official data.

a/ All credits, guaranteed and unguaranteed.

b/ A single bank is counted only once in the agent and in the manager columns. The total excludes repetition of a bank so that it can be less than the sum of the agent and manager columns.

c/ Since several banks can appear in the same syndicate as co-managers along with an agent, there is double counting of mobilized credit. Therefore, the sum of all mobilizations of all countries exceeds 100 percent of the total value of mobilized credit.

d/ An agent that also acted as manager in a syndicate has been only counted as an agent. Percentage sums to less than 100 because of one syndicate that did not have an agent.

of individual banks can understate the degree of dependence of the government on certain types of commercial institutions.

## 2. Lead banks grouped according to size

A good deal of prestige and financial muscle power could be an expected characteristic of lead banks. Table 6.5, which breaks out lead banks according to their size, confirms this with regard to Peru. Most lead banks, both in terms of their number and the total value of mobilized credit, were ranked in the top 91 of world banking. Banks of smaller size were not of great significance as leaders in syndication, especially when leaders are viewed as being the agent bank.

Interestingly, the concentration of leaders in large banks would have been even greater if Wells Fargo had not played such an important role for Peru in this regard. As a U. S. regional bank ranked as 69 (1975 on a world scale), Wells Frago gave group 3 of banks a high profile in the total spectrum.

## 3. Affinity groups among lead banks and participants in syndication

It would be interesting to see how lead bank organized credits to Peru. One might suspect that lead institutions might be more familiar with some banks than others, creating affinity groups, or clusters of banks, for each leader. Looking for such groups with regard to the experience of one borrower has its limitation. Not only are the number of observations for each lead bank very limited, but a one country case can support only forced generalizations. Nevertheless, establishment of affinity groups can be suggestive of the way certain lead banks operate on international capital markets.

Table 6.6 presents data on those banks that participated more than once in syndicated credits arranged by Peru's lead (agent) banks. It also shows the frequency of participation, i. e., the number of appearances of participants

Table 6.5

PERU: LEAD BANKS GROUPED ACCORDING TO SIZE, 1971-1976<sup>a/</sup>

Asset range of banks (billions of US\$) <u>b/</u>	International ranking <u>c/</u>	No of lead banks <u>d/</u>			Percent of all syndicated credit mobilized by leaders <u>e/</u>			Percent participation of leaders in their syndicated credit		
		Total	As	As	Total	As agent	As	Total	As agent	As
			agent <u>f/</u>	manager		agent <u>f/</u>	manager		agent <u>f/</u>	manager
1) 65 789 - 32 895	1 - 10	5	3	5	49.5	23.1	35.0	19.8	16.4	17.2
2) 32 894 - 16 448	11 - 46	21	10	16	61.7	43.8	36.6	25.7	19.2	20.3
3) 16 447 - 8 224	47 - 91	6	4	5	44.6	27.2	17.6	14.0	13.9	14.0
4) 8 223 - 4 112	92 - 147	5	3	2	13.6	1.5	12.1	6.1	16.8	4.7
5) 4 111 - 2 056	148 - 263	3	1	2	5.8	2.3	3.5	15.5	20.0	12.5
6) 2 055 - 1 634	264 - 300	1	-	1	3.4	-	3.4	8.3	-	8.3
7) < 1 634	> 300	4	1	3	11.9	0.3	11.5	6.4	16.6	6.1
8) Unknown	...	1	-	1	8.7	-	8.7	3.3	-	3.3

Source: CEPAL, on the basis of official data.

a/ All credits, guaranteed and unguaranteed.

b/ See footnote a of table 5.5.

c/ See footnote b of table 5.5.

d/ A single bank is counted only once in the agent and in the manager columns. The total excludes repetition of a bank so that it can be less than the sum of the agent and manager columns.

e/ Since several banks can appear in the same syndicate as co-managers along with an agent, there is double counting of mobilized credit. Therefore, the sum of all mobilizations of each group of banks exceeds 100 percent of the total value of mobilized credit.

f/ An agent that also acted as manager in a syndicate has been counted only as an agent. Percentage sums to less than 100 because of one syndicate that did not have a manager.

Table 6.6

PERU: AFFINITY GROUPS BETWEEN AGENTS OF SYNDICATED CREDITS AND PARTICIPATING BANKS<sup>a/</sup>

Frequency of participation (%)	Name of banks	Country	Frequency of participation (%)	Name of banks	Country
	Swiss Bank Corp.	Switzerland		<u>Wells Fargo (cont.)</u>	
100	Swiss Credit Corp.	Switzerland	33	Bank of Tokyo	Japan
100	Union Bank of Switzerland	Switzerland	33	Midland Bank Group	United Kingdom
100	Swiss Volksbank	Switzerland	33	Associated Japanese Bank	C
	<u>Manufacturers Hanover</u>	United States	50	Tokai Bank	Japan
67	Citicorp	United States	33	Commerce Union Bank	United States
67	Bankers Trust	United States	33	Kyowa Bank Ltd.	Japan
67	Charter N. Y. Corp.	United States	33	First Pennsylvania Corp.	United States
100	Royal Bank of Canada	Canada	33	Hokkaido Takushoku Bank	Japan
67	Wells Fargo	United States	50	United International Bank	C
	<u>Dresdner Bank</u>	Germany	50	Yasuda Trust and Banking	Japan
50	Banca Nazionale del Lavoro	Italy	66	American Express	United States
50	Toronto Dominion Bank	Canada	50	Banco do Brasil	Brazil
50	Banca Commerciale Italiana	Italy	33	Tayo Kobe Bank	Japan
100	Bayerische Hypotheken und Wechselbank	Germany	50	Krediet Bank	Belgium
50	Banque Nationale de Paris	France	33	Mitsubishi Bank	Japan
50	Banco de Santander	Spain	33	Rothschild International	...
50	Banque de la Societe Financiere Europeene	C		<u>Bankers Trust</u>	United States
50	Deutsche Bank	Germany	100	C.I.T. Financial Corp.	United States
	<u>Credit Lyonnais</u>	France		<u>Algemene Bank Nederland</u>	Holland
100	Banca Commerciale Italiana	Italy	80	Amro Bank	Holland
	<u>Wells Fargo</u>	United States		<u>Bank of Tokyo</u>	Japan
50	Western Bancorporation	United States	60	Banque Commerciale Pour L'Europe Du Nord	Soviet Union
66	Banca Commerciale Italiana	Italy	50	Tokai Bank	Japan
33	Royal Bank of Canada	Canada	80	Banque Europeenne de Tokyo	C
66	Toronto Dominion Bank	Canada	80	Fuji Bank	Japan
50	Lloyds Bank	United Kingdom	60	Mitsui Bank	Japan
50	Marine Midland Bank	United States	60	Sanwa Bank	Japan
50	Bancal Tristate	United States	60	Dai-ichi Kangyo Bank	Japan
50	Long Term Credit Bank	Japan	40	Kyowa Bank	Japan
50	Banque Europeene de Tokyo	C	60	Nippon Credit Bank	Japan
83	Banque Commerciale Pour L'Europe Du Nord	Soviet Union	60	Taiyo Kobe Bank	Japan
33	Industrial National Corp.	United States	80	Saitama Bank	Japan
50	Japan International Bank	C	40	Sumitomo Bank	Japan
33	Libra Bank	C	40	Daiwa Bank	Japan
50	C.I.T. Financial Corp.	United States	60	Hokkaido Takushoku Bank	Japan
66	Atlantic International Bank	C	80	Industrial Bank of Japan	Japan
50	Canadian Imperial Bank	Canada	60	Bank of Yokohama	Japan
50	Fidelcor	United States	80	Mitsubishi Bank	Japan
66	Fuji Bank	Japan	40	Hokuriku Bank	Japan
33	Italian International Bank	C		<u>Citicorp</u>	United States
50	Mitsui Bank	Japan	100	Bank of America	United States
33	Mitsubishi Trust and Banking	Japan	100	Chase Manhattan Bank	United States
66	Sanwa Bank	Japan	100	Bankers Trust	United States
66	Banco de Santander	Spain	100	Continental Illinois	United States
50	Dai-ichi Kangyo Bank	Japan	100	Manufacturers Hanover	United States
33	Seafirst Corp	United States	100	Philadelphia National Corporation	United States
50	Citicorp	United States	100	Morgan Guaranty	United States
			100	Wells Fargo	United States
			100	Chemical Bank	United States
			100	First Chicago Corp.	United States

Source: CEPAL, on the basis of official data.

a/ Agents are assumed to be lead banks of syndications. They were matched with banks that appeared more than one time with the agent in a syndicated credit. The frequency of appearance is merely the number of times a bank accompanied the agent in syndication divided by the number of syndicates headed by the agents. Results must be treated as tentative since the actual number of syndicates headed by each agent was very small.

b/ The symbol C for the country of a bank indicates a consortium bank.

divided by the number of syndicated credits arranged by the lead bank. A frequency of 50% or more would be very suggestive of a "working relationship" between the lead bank and certain participants.

It is seen that three big New York money center banks in the table —Manufacturers Hanover, Bankers Trust, Citicorp—show relatively few working relationships. This is undoubtedly a function of their enormous drawing power in international markets which makes the development of many working relationships unnecessary for the successful formation of syndicates. However, it is interesting that many of the working relationships that they had were with other big New York banks, or other U.S. institutions like Continental Illinois and First Chicago, that fall into the big money center bank category and have much experience as international lenders. This is not surprising because U.S. money center banks have a tradition of strong operational links; recent U.S. government studies have shown these institutions to be closely linked through interlocking directorates and ownership of each other's stock. 10/

Wells Fargo's affinity group is illustrative of how a smaller regional bank managed to become a major lead bank for Peru. Not having the drawing power of big money center banks, Wells Fargo had to develop a much wider array of working relationships to insure syndication. Notably, the degree of geographic dispersion of these relationships is large with respect to the other big lead banks and there is an obvious attention to exploiting the special links of the U.S.'s West coast with Japan. Another feature of Wells Fargo's affinity group is that, like it, many of the banks were relative newcomers to the international lending scene in the first half of the 1970's. (It will be seen in Chapter 7 that most of the affinity group also was willing to join Wells Fargo in undercutting market prices for loans to Peru.) In sum, it appears that in order to succeed as a lead bank, Wells Fargo had to "try harder" through innovation and the development of relationships with a far reaching number of banks.

The Bank of Tokyo—not a giant in the world organization of syndicates—also appears to have relied relatively more on working relationships to form syndicates. Moreover, its relationships were rather clannish in comparison with Wells Fargo as almost all the institutions were of Japanese origin.

Finally the Swiss Bank Corporation maintained a very strong working relationship with a few banks of the same national origin and Dresdner Bank—a giant in syndication—showed a fair number of working relationships which were very international in character.

#### 4. The relative international character of syndicates

Syndication of loans is symbolic of the internationalization of commercial bank activities. But how international are syndicates? Table 6.7 shows, for the period 1972-1976, the percentage value of syndicated credit coming from banks of a country origin distinct from that of the lead bank. It is seen that in 1972-1975 between 40% and 50% of the syndicated credit came from "international" sources, giving loans a reasonably multinational flavor. However, in 1976 loans had little international character.

The year 1976 was a special case and reflects the situation when a country is on the verge of losing its creditworthiness. As noted in earlier chapters, in this year Peru sought large refinance credits to stem the deterioration of its balance of payments. But given that the request was under conditions of economic duress, lead banks did not compete for the business; rather the transaction was seen as a bail out of the external accounts and therefore major creditors banded together in national groups,—U.S., Canada, Japan, etc.—to form coordinated syndicates with roughly \$400 million in rescue finance. As has been seen in Chapter 5, the terms and conditions of the credit were identical for all national groups, a further indication of absence of competition in syndication.



Table 6.7

PERU: RELATIVE INTERNATIONAL CHARACTER OF SYNDICATED LOANS, 1972-1976 a/

(Averages) b/

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	1972	1973	1974	1975	1976
Percentage value of syndicated credit derived from banks of a country origin distinct from that of the lead bank	50.2	46.9	42.3	49.5	17.3

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Source: CEPAL on the basis of official data.

a/ All credits, guaranteed and unguaranteed.

b/ Weighted by the value of the loans.

Thus, one can conclude that syndicates do enjoy a relative degree of international character when banks are actively competing for a client's business. But once a borrower loses, or is on the verge of losing, its creditworthiness, commercial banks appear to revert to a more clannish, or even collusive, behaviour. National groups are formed and coordination takes place to insure identical terms both within and among country groups. This arrangement undoubtedly facilitates communication among bankers in the working out of a mutually acceptable agreement. But the fact remains that the competitive advantages of syndication are lost to the borrower if it cannot maintain the confidence of its lead banks and other private creditors.

Chapter 6

FOOTNOTES

1. Financial Times.
2. Ibid.
3. Ibid.
4. For a more elaborate description of the process see Bee and/or Miozzi.
5. See Miozzi, p. 16.
6. The largest single transaction was the 210 million refinance credit extended by U.S. banks in 1976.
7. See Miozzi, p. 16.
8. For those interested in seeing a list of Peru's lead banks which incorporates all managers, see table A6.2 of the statistical appendix.
9. In 1975 the top 5 (Citicorp, Bank of America, Manufacturers Hanover, Morgan Guaranty and Chase) of the top 15 lead banks in eurocredit syndication accounted for 67% of the credit mobilization. See International Herald Tribune. In 1977, of the top 50 lead banks in syndication, the top 10 were responsible for nearly 60% of all credit mobilization. See Euromoney, april 1978.
10. See U.S. Senate (1974 and 1978).

Chapter 7

THE DIFFERENTIAL BEHAVIOR OF COMMERCIAL BANKS

One of the conclusions that can be drawn from earlier analysis of bank lending to Perú is that behavior has not been totally uniform. It has been seen that at the level of individual institutions, some banks have lent considerably more resources to the government of Peru than others. It also has been seen that a bank's importance cannot be determined just by its level of authorizations; in the age of syndication certain banks play important roles as lead banks which mobilize resources on international capital markets. Moreover, lead banks have shown different strategies for the organization of syndicated loans.

Likewise, when banks are viewed from the standpoint of national origin, there are perceived differences in behavior. In the case of Peru, American banks have been the overwhelmingly predominant lender, with Japanese banks a distant second. American banks also have stood out as the principal lead institutions in syndication, mobilizing the vast majority of credit.

And, finally, when viewed from the standpoint size, lending has clearly been dominated by very large institutions. It was seen in Chapter 5 that banks in the two largest ranges of asset size accounted for 78% and 58% of all lending in 1965-1970 and 1971-1976, respectively. Lead banks in syndicates also tended to be very large institutions. Smaller institutions certainly played a much more important role in 1971-1976 than in 1965-1970, but notwithstanding their large number, as a group they remained of secondary importance as both lenders and mobilizers of resources.

For developing country governments it is important to be aware of the differences in the behavior of its lenders. General policies of some banks or groups of banks vis-a-vis the borrower may be more favorable to its interests than the policies of other banks, taking into account, of course, that what is viewed as favorable may change over time according to the specific goals of the government and objective circumstances. Knowledge of behavior in deciding on which banks to approach for finance given certain circumstances can help to elucidate the relative strengths and weaknesses of both parties in any given bargaining environment. For instance, if a country has a project to finance, it may be wise to approach banks that have shown a special interest in that type of loan. If a country wants to reduce the cost of its credit, it might want to approach a bank that has shown a tendency to undercut market trends. In order to negotiate a loan under conditions of economic duress, it might be wise to approach banks that have a special interest in the health of the borrower, because, <sup>of</sup> for example, an unusually large commitment to the borrower, or important business interests in the domestic economy.

In order to ascertain the behavior of commercial banks, one must penetrate aggregate lending data. Up to now, any differences in the behavior of banks has come out implicitly in analysis of material of broader concern. It is the task of this chapter to focus more explicitly on revealed differences among banks. The word revealed is used because analysis is performed only on ex-post lending to Peru. To safely generalize one would have to have data on more countries and

detailed data on the global lending policies and attitudes of each bank in the study. Unfortunately, such an ideal research laboratory is unavailable for reasons which were already stated in chapter 2. Thus the more crude approach of analyzing behavior vis-a-vis Peru. The results, of course, are necessarily tentative in nature and subject to further research. And as will be seen during the course of this chapter, given the far less than perfect information on all the banks in the study, one is left on many occasions only to conjecture on the different modes of behavior and the motivations behind them.

As for the material to be covered, analysis will enter into both qualitative and quantitative aspects of behavior. The individual areas of analysis have been selected on the basis of the availability of data and are not necessarily interrelated. In the examination, observations will be made about individual banks as well as groups of commercial institutions. Frequently the terminology "aggressive" and "conservative" will be used to characterize lenders. These terms are not meant to impart a blanket assessment of the value of a bank (or banks) to the borrower. Each type of lender can have a more or less favorable effect depending on the objectives and characteristics of the borrower at any given moment in time. For example, to the extent that aggressive lenders introduce cheaper market terms, they have an apparent favorable policy from the standpoint of the borrower. On the other hand, if the willingness of aggressive lenders to finance any and all activities causes the borrower to become lax in its financial management, then conservative bankers might be the better

source of finance for the borrower. Thus one could use the classification of aggressive and conservative as being basically neutral, with positive or negative connotations being added only according to the particular circumstances of the borrower.

Finally, no attempt will be made to formulate a consolidated typology of bank behavior based on the partial analysis of this chapter. Such a typology, based on the more complete data of the study, can be found for a selected number of banks in the annexes of the document.

#### I. The relative commitments of commercial banks

In table 5.1 of chapter 5 one saw the relative importance of individual banks as lenders to the government of Peru in 1965-1970 and 1971-1976. However, the ranking of lenders was based on the total amount of gross authorizations and did not take into account the size of the individual lending institution. It therefore would be interesting to adjust total authorizations to the scale of \_\_\_\_\_

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the banks in order to detect the relative degree of commitment to Peru. This approach should reveal the degree to which individual banks have extended themselves in Peru and could be suggestive of marketing strategies. It also should be indicative of the leverage, if any, that Peru has over the banks.<sup>1/</sup>

In order to adjust data, gross authorizations in the period 1965-1970 were taken as a percentage of the assets of the individual lending banks, using dollar asset figures for 1969. A similar exercise was carried out for the period 1971-1976, with the exception that data on assets corresponded to the year 1975. In order to facilitate intra - as well as inter - period comparisons, coefficients were indexed. A coefficient of 0.5%, which happened to be the highest coefficient in the period 1965-1970, was taken as 100 and the rest of the data were indexed on this base. Then various ranges of the index were established, classified as high, intermediate and low commitments. Finally, banks were placed according to how their coefficient corresponded with the various ranges.

Before examining the table it is worthwhile to point out the limitations of the data. First, coefficients can possibly contain an element of overstatement because loans are based on gross and not net commitments. Also, data are for original commitments and account could not be taken of whether a bank subsequently unloaded the commercial paper onto secondary markets. Second, there is an important element of understatement because short term credits are excluded, as are bank loans for national defense purposes. On balance it is difficult to say just what the net effect of factors one and two were on the absolute and relative values of the coefficients. The reader



should bear these points in mind when using the data.

Table 7.1 shows that some of the banks classified as major lenders in Chapter 5 for the period 1965-1970 also were at the top of the scale of relative commitments for the same period. Bankers Trust, Continental Illinois and Manufacturers Hanover, all major lenders in terms of the value of their authorizations, also were the relatively most committed to Peru. The other major lenders - Citicorp, Chase Manhattan and Bank of America - were decidedly less committed, suggesting more conservative lending strategies with regard to Peru. Citicorp, which was in the highest group of major lenders, had a relative commitment that placed it only in the intermediate ranks of table 7.1. The relative commitments of Bank of America and Chase Manhattan also were significantly less than proportional to their positions as lenders based on the absolute level of authorizations.

As for the intermediate lenders, Bank of Nova Scotia and Franklin National Bank stand out for their very significant level of relative commitment to Peru. It would appear, then, that in the 60's these banks had a view on Peru that was somewhat more positive than many other lending institutions.

The other aspect of the relative commitments in the 60's is that no bank's commitment to Peru exceeded 0.5% of total assets. It is clear, then, that the absolute weight of Peru in the total portfolio was very low even for the most heavily committed lenders. This reflects the age old dictum of prudent banking that risk can be minimized through loan diversification.

Table 7.1

PERU: RELATIVE COMMITMENTS OF COMMERCIAL BANKS-TOTAL AUTHORIZATIONS  
AS A PERCENT OF TOTAL ASSETS, 1965-1970 AND 1971-1976<sup>a/</sup>

(100 = 0.499% of total assets)

1965-1970		1971-1976	
Level of commitments and names of banks <sup>b/</sup>	International rank of bank <sup>c/</sup>	Level of commitments and names of banks <sup>b/</sup>	International rank of bank <sup>c/</sup>
<u>HIGH</u>		<u>HIGH</u>	
<u>100-80.0</u>		<u>&gt; 668.9</u>	
Bankers Trust	11	Libra Bank	301(c)
Continental Illinois	22	Euro American Bank	301(c)
Manufacturers Hanover	5	<u>668.9-510</u>	
		Atlantic International Bank	301(c)
<u>INTERMEDIATE</u>		Asian and Euro American Bank	301(c)
<u>79.9-60.0</u>		<u>509.9-343</u>	
Bank of Nova Scotia	47	Banque Europeene de Tokyo	301(c)
Franklin National Bank	78	Associated Japanese Bank	301(c)
<u>59.9-40.0</u>		<u>342.9-175</u>	
Schroders Ltd.	197	Iran Overseas Investment Bank	301
Charter New York Corp.	39	Western American Bank	301(c)
CITICORP	a	Nippon European Bank	301(c)
First National Bank of Boston	59	Japan International Bank	301(c)
<u>39.9-20.0</u>		Banque de la Societe Financiere Europeene	301(c)
Chase Manhattan	3	Wells Fargo	69
Bank of America	1	<u>174.9-100</u>	
National Detroit Corp.	57	Italian International Bank	301(c)
Crocker National Bank	48	Bancal Tri-state Corp.	199
Toronto Dominion Bank	54	United International Bank	301(c)
<u>LOW</u>		Inter-Unión Bank	301(c)
<u>&lt; 20</u>		London and Continental Banks Ltd.	301(c)
Royal Bank of Canada	12	International Mexican Bank	301(c)
Banca Commerciale Italiana	25	European Brazilian Bank	301(c)
Morgan Guaranty Trust	6	American Express Int. Banking	223
Westdeutsche Landesbank Girozentrale	14	<u>INTERMEDIATE</u>	
Philadelphia National Bank	94	<u>99.9-60</u>	
Lloyds Bank	33	Bank of Nova Scotia	53
Western Bancorporation	8	Banque Commerciale Pour L' Europe Du Nord	195
Bank of Tokyo	26	International Commercial Bank	301(c)
		Crocker National Bank	79
		Fidelcor	203
		Philadelphia National Bank	144
		Toronto Dominion Bank	66
		Grindlays Bank	154
		Manufacturers Hanover	16
		First Pennsylvania Corp.	106
		C.I.T. Financial Corporation	210
		Banque Canadienne National	130
		Banque Continentale Du Luxembourg	301(c)
		<u>59.9-40</u>	
		Banque Europeene de Credit	301(c)
		Bankers Trust	32
		Orion Bank	301(c)
		Continental Illinois Bank	30
		Franklin National Bank	...
		CITICORP	2
		Royal Bank of Canada	22

Table 7.1 (concluded)

1965-1970		1971-1976	
Levels of commitments and names of banks <sup>b/</sup>	International rank of bank <sup>c/</sup>	Level of commitments and names of banks <sup>b/</sup>	International rank of bank <sup>c/</sup>
		LOW	
		<u>39-9-20</u>	
		Bank of Montreal	45
		Anthony GIBBS	301
		Industrial National Corp.	260
		U.B.A.F	301(c)
		Dresdner Bank	14
		Trade Development Bank	219
		Chase Manhattan	4
		LLOYD'S Bank	31
		First Chicago Corporation	35
		Bank of Tokyo	28
		Morgan Guaranty Trust	19
		Bank of America	1
		Shamut Corporation	248
		Nomura Securities	d/
		Cleveland Trust Co.	151
		Midland and International Bank	301(c)
		Banco de Santander	112
		Long Term Credit Bank	44
		Centran Corp.	258
		Marine Midland Bank	77
		Banque Francaise Du Commerce Exterieur	174
		Chemical Bank	23
		Banque Worms	286
		Schroders Ltd.	301
		Security Pacific Corp.	54
		Deutsche Bank	6
		Western BanCorporation	39
		Fuji Bank	13
		Swiss Volksbank	143
		<u>20</u>	
		The Remainder of the Bank in the Study <sup>e/</sup>	

Source: CEPAL, on the basis of official data.

a/ Exercise on authorizations without a guarantee of and export credit agency.

b/ Authorizations calculated as a percentage of bank assets. The asset size for the period 1965-1970 is based on 1969 data presented in The Banker, June 1970; asset size for 1971-1975 is based on 1975 data presented in The Banker, June 1976. Where a bank did not rank in the top 300 of world banking, asset size was determined from 1975 balance sheet data of the Banker Research Unit's Who Owns Whom in World Banking, 1976. Other sources used to determine asset size were the Japan Company Handbook and The Times 1000. Banks for which no asset data could be secured were excluded from the exercise (see footnote e).

c/ The ranks are based on the list of the top 300 in World Banking prepared by The Banker. The ranks for 1965-1970 are based on 1969 asset size presented in The Banker, June 1970; the ranks for 1971-1976 are based on asset size in 1975 as presented in The Banker, June 1976. Banks that did not figure in the top 300 are ranked as 301. The letter "c" in parenthesis designates a consortium bank.

d/ Not ranked in The Banker.

e/ For the following banks no asset data were available: Banque de L'Union Europeenne; Banque Internationale A Luxembourg; Balfour Williamson; Commerce Union Bank; La Salle National Bank; Rothchild Intercontinental Bank, Union Planters Bank; Banco Mexicano; Morgan Guaranty and Partners; Low Banking Corporation; Algemene Bank Nederland; ComCo International Bank; LTCB Asia Ltd.; Banque Arabe el Internationale D'Investissement; Trade Invest Bank and Trust Company; Banco Atlantico; Banco Nacional de Panama, Banco de Bogotá; First National Bank of St Louis; Bank Lew; Privat Bank and Verwaltungsgesellschaft; Bank für Gemeinwirtschaft; Industrial Multinational Investment Ltd; and Liberal Bank.

Turning to the second period, 1971-1976, one finds some striking changes. Most obvious is the fact that the scale of relative commitments by banks increased dramatically. Whereas 100 (equal to 0.5% of total assets) was the top absolute level of relative commitments in 1965-1970, in 1971-1976 twenty banks exceeded this mark, some by more than six times.

It can be seen in the table that almost all the banks that exceeded the base index of 100, and therefore were at the very high end of the period's scale of relative commitments, were consortium banks. All the consortium banks were classified as minor lenders in terms of authorizations; nevertheless, gross loans, as limited as they were in absolute value, were a considerably higher percentage of total assets than for regular banks. This indicates a rather aggressive lending strategy. A possible explanation behind the phenomenon is that consortium banks are relatively small institutions that operate under the umbrella of their parent banks. The parents effectively absorb the risks of a consortium's lending, which is not very great in terms of the size of the parents. Thus, a consortium bank can commit itself to a borrower to a degree which otherwise might be deemed imprudent. As will be seen shortly, consortium banks to some extent may have covered the increased risk through higher than average yields on loans.

Aside from the consortium banks, the only regular banks with indexes in excess of 100 were Wells Fargo, Bancal Tristate Corporation and American Express International.

Wells Fargo is a curious case. It was seen in Chapter 5 that this bank was classified as a major lender to Peru, its total authorizations placing it within the group of top 5 lending institutions. The bank's relative commitment - the highest of any regular bank - far exceeds the relative commitment of any of the other major lenders in the period, i.e., Citicorp, Manufacturers Hanover, Bank of America and Chase Manhattan. Thus, Wells Fargo stands out as having a behavior that is very distinct from its companions in the major lending group. In terms of Peru, Wells Fargo would appear to have had by far the most aggressive strategy of the major lenders. To achieve its business, the bank had to be willing to take on a position that was much more extended than any of the other major lenders. In fact, Wells Fargo's relative commitment was nearly three times larger than the next most committed major lender, Manufacturers Hanover.

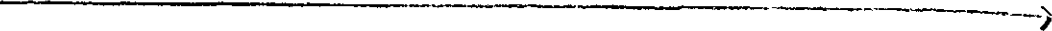
It is no secret that Wells Fargo had special interest in Peru. In the early 1970's the bank was interested in breaking out of its regional business in the West Coast of the United States and in developing an extensive international portfolio. Markets in the industrialized countries were heavily penetrated by the big established international banks. The most attractive LDC borrowers like Brazil and Mexico were already the center of vicious competition among the world's bankers. Thus the appeal of second and third line borrowers in developing areas. In 1972 Peru was ripe for penetration because many factors, described

earlier in Chapters 3 and 4, had made the established international banks reluctant to deal with the government. Moreover, for Wells Fargo Peru was logical terrain for a foray into the developing world; it had recently placed in a high executive post a well-known and prestigious Peruvian national who had been an important functionary in the Peruvian Central Bank during the prerevolutionary government. Using its special rapport with Peruvians, coupled with offers of substantial credit on terms which were favorable compared to that available from other institutions, Wells Fargo captured a share of the market quickly. Pursuing similar policies up through 1974 (which will be described in greater detail later), the bank came from nowhere to become a major lender to the government of Peru and an important lender for other LDCs.

As for the two other banks with relatively high commitments in Peru - American Express and Bancal Tristate Corporation - they were of intermediate importance in terms of the value of their authorizations. They too are likely to have had a generally aggressive lending policy towards Peru. Tristate, like Wells Fargo, is a U.S. regional bank and Peru was probably an easy way to break into the high profits generated by lending to LDCs. American Express International is a well-known late-comer which has had an aggressive attitude on expansion of international lending. Again Peru was probably a relatively easy mark to support its ambitions to become a major world lender. In the case of American Express, however, its high commitment might be more

similar to a consortium bank than a regular bank, since American Express International Bank is only a subsidiary of the much larger financial conglomerate, American Express Corporation.<sup>2/</sup>

The table shows that between 1965-1970 and 1971-1976 a number of banks changed the level of their relative commitments to Peru. A rise in the relative commitment may have been in response to an explicit shift in policy at a bank towards a more favorable attitude on the



government. But given the wide scale penetration of LDC markets by commercial banks during the first half of the 1970's, there is strong likelihood that any increase in commitment was merely a reflection of a more general expansion of developing countries' share of the bank's portfolio. On the other hand, greater suspicion can be attached to any significant fall in commitment level. In the aggressive lending environment of the 70's, any reduction in commitment to Peru would have required a conscious policy by the bank to counter general trends and restrain growth of lending. This in turn could very well be reflective of a more conservative attitude on the part of the bank towards the military government.

It was seen in Chapter 5 that two major lenders in 1965-1970, Bankers Trust and Continental Illinois, fell to an intermediate level of importance in 1971-1976. But it is seen in table 7.1 that there also was a rather sharp decline in their relative commitments to Peru between the two periods. This could very well be indicative of a change in attitude on Peru, involving a relatively more conservative policy with regard to lending to the government in the 1970s. Also, hidden in table 7.1 is a considerable fall in the level of commitment of Manufacturers Hanover in 1971-1976. Thus, while in terms of absolute authorizations this bank had a position as a major lender to the government in both periods, in the 70's it could have had a policy of relatively more restraint in lending.

It is interesting to note that other major lenders - Citicorp, Bank of America, Chase Manhattan, - appear to have had fixed limits on their lending to Peru throughout the 12 years.



While the volume of their lending increased substantially between the two periods, their relative commitments remained basically unchanged. In other words, none of these banks provide evidence of a special effort to expand the portion of their portfolio in Peru during the 70's. Rather, their lending in 1971-1976 would appear, on the basis of these limited data, to have been of a defensive nature, designed to maintain Peru's share in their portfolio.

With regard to banks of intermediate importance as lenders in 1965-1970, the Charter New York Corporation, the First National Bank of Boston and the National Detroit Corporation, all experienced rather drastic reductions in their relative commitments in the 1970's. Again this would be suggestive of a change in attitude towards lending to the government of Peru.

Finally, the one general observation that comes out of the data is that regular banks (as opposed to consortium banks) appear to have a very diversified portfolio in which Peru plays only a very small part. In no case did gross authorizations exceed one percent of total assets; in fact, for all but three regular banks gross authorizations did not exceed 0.5 per cent of total assets for the 12 years under study.

It has often been claimed by officials in the centers that commercial banks have become "hostage" of LDC governments through their lending to them.<sup>3/</sup> This would appear to be a serious exaggeration. Peru was a major LDC borrower (in 1975 it was the seventh largest LDC borrower) and its position in the portfolio of the banks vis-a-vis

other clients was relatively minor. True, a default by Peru might damage annual profits, put a severe pinch on reserves set aside to cover loan losses, and maybe even could threaten the viability of some smaller institutions. Thus because of both precedent and pain bankers would want to avoid default. But in the end most could accept default as a realistic alternative to further lending, especially taking into account the prospects of financial assistance from home government monetary authorities.

Thus a default by a single borrower like Peru would not be a threat to many banks and clearly would not represent any danger to the world financial system as a whole. On the other hand, a default could have very serious consequences for Peru, unless it made the prior decision to drop out of the western capitalist community. Not only would it find all credit cut off (due to cross-default clauses) and its purchases and sales abroad interferred with, but it also could face reprisals from the home governments of the banks. This would have disasterous effects on national political stability and development, thus making the borrower go to great lengths to meet the demands of its bankers.

So the concept of hostage would seem inappropriate; indeed, on balance the banks would seem to clearly enjoy greater leverage over single borrowers. Only in the case of a super borrower like Brazil or Mexico could a single borrower create real problems for the banks; and any problems that might arise would likely be specific to few over-committed institutions rather than national financial systems.<sup>4/</sup>

II. Bank behavior with regard to the pricing of loans

In a simple framework, commercial bank lending to a developing country can be expressed by the following function:

$$L_t = f (E_{t-1}, C_t, P_t)$$

where L = lending to country i in period t;

E = the level of exposure of the bank with country i in period t-1;

C = the bank's view of the creditworthiness of country i in period t;<sup>5/</sup>

P = the interest price of the loan taken in the broad sense to include interest spread and maturity. (The base interest rate would be determined by the interbank market.)

L in period t is then a negative function of E at the end of the previous lending period and a positive function of the current estimation of creditworthiness and the current price that the borrower will pay for credit. Since at any given time lending institutions would have different levels of E with Peru and different estimations of C, these differences could reflect themselves in either the volume of lending, the price of credit or both.

One has already seen that the volume of lending has differed among institutions. But the question remains: how have banks behaved with regard to price?

The advantage of using disaggregated data is that some approximations can be made in this regard. And to the extent that one found that some banks consistently offered better or worse terms than the general market trend, this would be indicative of bank policy and therefore could be very useful information for a developing country borrower.

Before preceeding to the examination, two caveats are merited about the scope and intent of analysis.

First, there are a limited number of years in which data can be observed. The periods 1965-1970 and 1971-1976 are very distinct ones for world banking and therefore must be viewed separately. Moreover, only in the second period was commercial bank lending dense enough to provide any potential for meaningful analysis of differential behavior, and even then one is really limited to the extremely narrow 5 years covering 1972-1976.

Second, while there is an adequate density of loans for the period 1972-1976, there is great dispersion among lending institutions. This means that the number of banks for which there are observations in each year does not exceed 25, a rather small group considering that there were 167 lending banks for the period. Fortunately, the banks for which data permitted analysis were mostly lenders of major and intermediate importance in terms of authorizations.

The above 2 factors place severe limitations on what can be expected from analysis. Nevertheless, examination of the data can still be suggestive of behavior and, additionally, can complement information generated in any future studies with similar objectives. It is these limiting conditions and goals that underpin the analysis in this section.

A. Examination of price behavior.

1. The testing procedure. In looking at the establishment of terms, two variables were considered: the spread over libor and the total maturity of the loan. For each year a bank was assigned an annual average

spread over libor and <sup>an</sup> average total maturity. Similar annual averages were calculated for all banks in the study taken as a group, using these global averages as the indicator of market trends vis-a-vis Peru. Equally paired observations<sup>6/</sup> between a bank and the global average were organized covering the 5-year period 1972-1976. A two-tailed Student's t evaluation was made on the data to test the hypothesis :

Hypothesis<sub>0</sub>: the average terms of the bank were the same as the market's terms.

against

Hypothesis<sub>1</sub>: the average terms of the bank were different from the market terms

at a confidence level of 90%.

As has been seen, the year 1976 was one in which Peru was on the verge of losing its creditworthiness; banks became very cautious towards the country and lending was motivated more to prevent default than to generate new business. Since the lending environment for this year was rather distinct from the previous four, a Student's t test was made on equally paired observations for the period 1972-1975. This had the disadvantage of reducing the already low number of degrees of freedom from 4 to 3. But as a positive element, more banks could be incorporated into the evaluation.

To complement the evaluation of the behavior of selected individual banks, a similar test procedure was carried out on banks grouped according to their country of origin and their asset size. The partial aggregation of data paralleled the similar exercises already presented in Chapter 5. Of course, in these latter tests all banks in the study were considered.

2. The results of the tests. The actual test results for all banks and groups of banks can be found in tables A7.1-A7.6 of the statistical appendix. Only the significant finding will be commented upon here.

The results of the tests might suggest that banks really do not discriminate on the basis of price. Among the banks tested there was a general uniformity in interest spreads and maturities of the loans. Banks would appear, then, to find it difficult to deviate from the market's price of loans, presumably because of competitive pressures.<sup>2/</sup> Under these circumstances the different levels of E and the different evaluations of C among the individual banks would reflect themselves not in the price of credit, but rather in the volume of lending, and perhaps non-price aspects. Thus, in general, the volume of bank lending that was adjusted to the size of the institutions in the previous section may be a reasonable reflection of how institutions perceived risk in Peru as embodied in considerations about exposure and creditworthiness.

While there was a general uniformity of trends with regard to the pricing of loans, in some cases significant deviations from market trends were found. These are worth commenting upon.

For the full 5-year period, 1972-1976, Manufacturers Hanover - a major lender to the government - displayed interest margins that were significantly higher than the market average. However, when the period was adjusted to eliminate the odd year of 1976, there was no longer a significant divergence from market trends. Thus evidence probably is not strong enough to suspect this bank of charging higher than average spreads on its loans.

Banque Commerciale pour L'Europe du Nord (Eurobank), an institution stationed in Paris, but owned by the USSR's State Bank and Foreign Trade Bank, showed for the adjusted period 1972-1976 a significant tendency to price above market trends. However, this bank - which was a minor lender to Peru - for the same period showed a tendency to extend longer than average maturities. The longer maturities offset the higher spread, making it impossible to suggest that the institution operated outside the market environment.

There was significant evidence that Bankers Trust - of intermediate importance as a lender - may have pursued a policy of extending maturities that were markedly shorter than the market terms. The divergence was significant at a 90% level of confidence for 1972-1976 and even more significant for the adjusted period 1972-1975. It also can be remembered that in the previous section it was found that Bankers Trust may have restricted its exposure in Peru during the 1970's. Thus the test results on its maturities would provide further evidence of cautious behavior on the part of this institution.

The Dai-Ichi Kangyo Bank - a minor lender to the government - provided evidence of longer than average maturities on its credit. Divergence from market terms was significant in both the 5 and 4-year periods.

Wells Fargo, a major lender to the government, provided significant evidence of offering longer maturities than the market for the 5-year period 1972-1976. However, this hypothesis could not be sustained when data were adjusted to the more normal period 1972-1975.

With regard to the tests on more aggregated data, few significant divergencies were found.

For the adjusted period 1972-1975 the third group of banks ranked according to size gave significant results to suspect that their interest margins were consistently higher than the market average. This group of banks incorporates institutions with international rankings between 47 and 91 on a scale of 1-300. In terms of their lending to Peru, these banks generated 19% of total authorizations.

In the country groupings, the miscellaneous category "other" showed significant evidence of extended maturities in both the long and adjusted periods. This group accounted for 8% of the total lending to the government in the 1970s and mostly represents minor lenders that are from countries outside the mainstream of international finance (see annexes for a list of the banks).

3. The role of fees. The previous analysis was applied on interest margins and maturities; it excluded flat fees because of data problems. In data collection there was no way of knowing in all cases the actual distribution of fees among the banks in syndicated credits. Thus fee earnings could not be assigned to individual institutions. This represents an unfortunate constraint because while fees are not reflective of the cost of credit for a bank, they do increase the yield on loans and therefore could be a factor in the pricing equation.

One way of by-passing the problem would be to assume that fees were equally distributed among all institutions in a syndicated credit. In effect, then, one would be testing the degree to which institutions were associated with loans carrying certain levels of fees rather than testing fee earnings per se. If an institution, or group of banks, persistently were associated with loans carrying fees higher than the



market average, this could also mean that the bank had been earning, or was seeking to earn, greater than average income from fees.

This rough and ready "guilt by association" technique was applied to the banks and student t tests were carried out in a fashion similar to that for interest margins and maturities. It is significant that both at the level of individual institution and for groups of banks there was a much greater degree of divergence from the market average than was found in the case of interest margins and maturities. This would suggest that non-interest prices such as fees may be less subject to market forces than their interest related counterparts and therefore used more liberally to counter exposure and risk considerations of individual institutions.

The statistical results of the tests can be found in tables A7.7-7.9 of the statistical appendix. However, it would be unfair to draw even tentative conclusions about the behavior of individual institutions on the basis of the rough and ready statistical technique used to test fee earning behavior. So no further micro analysis is justified here. However, it can be mentioned that results often were in line with a priori notions about behavior. For instance, data suggested that consortium banks pursued fees that were significantly higher than the market terms. And in the literature it is well known that consortium banks are especially geared to fee earning activities. This no doubt reflects their limited capacity to extend interest bearing loans, but it also must be remembered that it was shown earlier that these institutions had by far the highest relative commitments with Peru. Fees could then have been used to offset at least partially this higher apparent risk.

Finally, since the test raises suspicion that fees can be used to discriminate risk, greater efforts should be made to quantify and analyse these charges on bank loans. To date fees have not received the scrutiny that they would appear to merit.

B. Other considerations about pricing.

The statistical tests just examined above were on medium term periods and therefore would hide any role a bank may have had in creating an inflection point in market trends. For instance, a bank may have had average terms in line with the market, but at some particular point in time it may have been willing to lead the market by pricing above or below prevailing terms and thereby inducing other banks to follow. This phenomenon is not easily subject to testing, but can be found in the casual observation of data. Moreover, such observation is best done on syndicated credits which are large, generally gain much publicity, and can therefore have psychological effects on the market. While, of course, the participation of many banks make a syndicate possible, focus can be on the lead banks which were behind the organization of the loan.

In this context, two non-traditional lenders to Peru, Wells Fargo, and to a much lesser degree Dresdner Bank, stand out as especially important institutions. It would appear that these banks - aside from the level of their authorizations - played a critical role in Peru's gaining acceptance on international commercial bank markets and in lowering the cost of credit. A few descriptive examples will make this clear.

In early 1972 Peru was a highly uncertain entity from the viewpoint of the banks. Nevertheless, as was seen in Chapter 4, by this year the

banks had broken ranks with the international financial blockade and were beginning to extend significant amounts of finance to the government. However, terms were onerous with spreads of 2.25% over libor and maturities in the range of 4.5 - 6.5 years. These terms were much more severe than those being paid by other developing countries borrowing from international commercial banks. However, late in the year Wells Fargo headed a 40 million dollar loan for 7.5 years at 2% over libor and Dresdner headed a 30 million dollar loan for 7 years at 1.75% over libor. The Wells Fargo loan probably had the greatest impact on the market because, while the Dresdner Bank loan was for a project, which will be seen later to be a preferred form of finance for some banks, the Wells Fargo credit was for what could be considered a relatively less attractive refinance operation. Moreover, while there was a degree of geographic dispersion for the banks participating in both credits, Wells Fargo's credit incorporated 29 banks versus 14 for Dresdner's credit (see table 7.2). The greater number of banks in the former loan surely provided for a greater psychological impact on the market.

After the Wells Fargo and Dresdner credits in late 1972 the market tugged back and forth between spreads of 1.75% and 2% over libor, with maturities ranging between 6.5 and 7 years. Then, in April 1973, Wells Fargo led a 100 million dollar loan involving 61 banks; while the spread of 2% did not break new ground, the maturity of 8 years for a loan of free disposition was the longest tenor yet received on a syndicated credit. Then in the same month Wells Fargo, alone, extended 35 million dollars for refinance at  $1\frac{3}{4}\%$  over libor and an unprecedented maturity of 10 years.<sup>8/</sup> These two credits led the market and immediately thereafter

Table 7.2  
 PERU: A COMPARISON OF SYNDICATED CREDITS HEADED BY  
 WELLS FARGO AND DRESDNER BANK IN 1972

Country of participating banks	Wells Fargo		Dresdner bank	
	Number of participating banks <sup>a/</sup>	Percentage of credit <sup>b/</sup>	Number of participating banks <sup>a/</sup>	Percentage of credit <sup>b/</sup>
United States	8	38.8	-	-
Japan	8	23.7	5	30.0
Canada	3	11.2	2	13.3
United Kingdom	2	6.2	-	-
Germany	-	-	2	23.3
Italy	3	7.5	1	10.0
Switzerland	-	-	1	13.3
Other	2	3.7	1	3.3
Consortium	3	8.7	2	6.6
<u>Total</u>	<u>29</u>	<u>100.0</u>	<u>14</u>	<u>100.0</u>

Source: CEPAL, on the basis of official data.

a/ Includes lead bank.

b/ Does not sum properly due to rounding.

it was common for bank loans to carry a maturity of 9-10 years.

Some slippage in the prevailing libor spread occurred in September 1973 when a 24 bank syndicated credit headed by Manufacturers Hanover and Citicorp provided a 130 million dollar loan at a split interest margin averaging 1.6% over libor. However, it again was Wells Fargo which led the next fundamental break in the market's view on Peru. In December this bank organized a 31 bank 80 million dollar loan at 10 years and a spread of only 1.25% over libor.

In early 1974 Morgan Guaranty Trust headed the famous 76 million dollar credit associated with the Greene Accord; it carried an unusually low spread of only 1% over libor. Although the credit was clearly of a special nature, its political significance and relatively low price had a psychological impact on the market. Major large scale loans followed with 10 year maturities and spreads as low as 1.13 over libor. Subsequent lending by Wells Fargo and Dresdner Bank heavily supported the trends towards a lowering of interest margins.

In 1975 there was a general rise in spreads and a shortening of maturities. However, it is difficult to pinpoint which banks might have led or resisted the trend because the overall market conditions were highly unstable and mere access to credit, let alone cost, was a real preoccupation.

Thus, from the above, one gains another view of the special character of Wells Fargo in Peru's external finance. It certainly did lead favorable pricing trends in the market and occasionally with Dresdner Bank also was important in augmenting the volume of credit.

Finally, it might be added, that as lead banks, Crocker National Bank and the Bank of Tokyo often reinforced trends created by Wells Fargo by following with sizeable loans on similar terms.

Before closing this section, brief mention should be made of several other actors which were important in influencing the market's attitude on Peru in the 1972-1974 period. It might be recalled from Chapter 6 that in forming syndicates, Wells Fargo placed heavy reliance on Japanese banks, which contributed approximately one-third of the funds raised in syndication by this bank. Dresdner, Crocker National, and Bank of Tokyo also received heavy support from Japanese banks in forming syndicates. Thus Japanese institutions clearly were an important factor in the favorable turns in the market's attitude towards Peru. In the case of Wells Fargo and Crocker National, U.S. banks, particularly medium and small sized institutions, also were responsible for roughly one-third of the amount raised in syndication. Therefore, these institutions too should be considered as a key factor behind the favorable changes in market trends.

### III. Non-price forms of risk behavior

In a series of subsections that follow, analysis will focus on other apparent behavior of banks with regard to their lending to Peru. In contrast to the previous section, interest will be on the non-price aspects of commercial banks loans.

In the first major subsection, the nature of lending is examined. Analysis will be made on the revealed preferences of banks for certain types of loans and for lending to certain economic sectors, as embodied in their actual extension of credit to the government. Using a criteria outlined below, an attempt will be made to classify the nature of lending as being reflective of aggressive or conservative strategies.

The second major subsection focuses on another aspect of lending: the degree to which banks attempted to avoid risk by securing guarantees of home country export credit agencies. Heavy reliance on such guarantees would be indicative of a conservative strategy towards Peru, while the opposite situation would be indicative of a relatively more bold attitude.

In most instances, the data in the study were not dense enough to support analysis of the full 12-year period. Thus, the time frame covered here is only 1971-1976. Also, data generally were not adequate to support analysis at the institutional level, so accomodation had to be made for a greater degree of aggregation. The principal forms of aggregation are banks grouped according to their country of origin and their size based on assets.

A. Preferences in the Nature of Lending

As has been seen earlier, a bank's risk perception and strategy can be reflected in its relative commitments to Peru, and to a limited extent, in its pricing of loans. But it is also possible that bank behavior may be reflected in what types of loans they extend to a country and the sectors to which they decide to extend credit.

In broaching this subject there are some strong underlying assumptions which the reader should be fully aware of.

Banking should be viewed as having its traditions and its practices. Traditions are what bankers prefer to do and practice is what they actually do. The traditions incorporate the conservative dictums of prudent banks and represent a more cautious approach to lending. Many institutions attempt with varying degrees of success to remain within the confines of tradition. However, some banks may operate outside of tradition, either temporarily for reasons of penetrating markets, or more permanently because of some special insight into the shortcomings of traditional practice.

For the purposes of the statistical exercises that will be presented here, the reader should keep in mind the following observation by Aronson which aptly summarizes a tradition, or preferred behavior, of the banking community:

"Banks prefer lending for cash flow generating projects, which will allow borrowers to meet their obligations. They prefer not to finance consumption and infrastructure, are uneasy about financing payments deficits and would rather not refinance previous loans." 9/



Thus, even though commercial banks may have a sovereign government guarantee, they may not be indifferent about what types of loans they extend and the economic activities that they support. Banks cast in a traditional mold may pursue the banking dictum just cited above and attempt to maximize security by concentrating credit in loans and activities that customarily have been perceived as bearing less risk. In this regard a bank following such a practice can be deemed to be conservative. On the other hand, some banks for any number of reasons can ignore the traditional dictum, viewing it as nonsense or not in its immediate interests. This latter type of institution can be considered aggressive vis-a-vis the world banking community.

Using a criteria and technique outlined below, banks, relative to each other, are placed in a typology of conservative and aggressive lenders based first on the types of loans that they extended to Peru and then based on the types of economic sectors to which they knowingly lent resources. This is followed by an overall evaluation that presents a consolidated typology based on the two aspects of lending behavior.

Before entering analysis it is worth repeating the earlier statement that the terms aggressive and conservative are not meant to impart a value judgement about the worth of certain banks to a borrower. The value of being aggressive or conservative depends on the timing and circumstances. Aggressive banks may be willing to act in a way which reflects the immediate interests of the borrower,

but this can be a permissive influence on an undisciplined borrower just as it can be a boon to a sophisticated borrower. Conservative banks concentrating in project finance can be very favorable to a borrower wishing to finance a fixed investment. The mere point of the exercise is to show that there are indeed differences in behavior; it is up to the borrower to use the assigned behavior to its best advantage.

1. Preference for certain types of loans

In this particular subsection, interest will be on whether banks appear to have preferred some types of loans over others.

This assumes that there were risk considerations over and above the fact that loans carried a sovereign government guarantee; that there was a perception of further reduction in risks through careful selection of types of loans in which one became involved.

For instance, some bankers can view project loans as being a relatively more safe form of finance because such credits are tied to a precise activity in which there is an economic return <sup>to cover repayment</sup> that can be evaluated on an ex-ante basis. Moreover, project loans might be seen to carry a built-in discipline because the use of resources is tied to project proposals and project implementation also may benefit from the expertise of an established private foreign or local supplier or contractor. (If a supplier also is a major client of the lending bank, this is an additional incentive to lend). Characteristics similar to project lending also can be found in the finance of capital goods imports.

On the side of more risk could be found loans of free disposition and refinance credits. The most risky loan would be <sup>that of</sup> free disposition since a bank has no ex-ante insurance that the resources will be employed wisely and generate returns sufficient to promote repayment. With regard to refinance credits, although it has been seen that they made up the bulk of bank lending, bankers at least profess not to be eager suppliers of such finance, in part because of a belief in the primacy of repayment schedules.<sup>10/</sup> The greater risk involved in refinance is that a bank extends (perhaps reluctantly) a previous commitment to a borrower, sometimes under conditions of economic duress and on terms that from the bank's perspective can be less than commensurate to the risk involved.

certainly  
It is/debatable whether economic circumstances merit the above distinctions in loans; nevertheless, these considerations are often perceived as real relative risks by some banks. And if institutions display a tendency to favor one type of a loan over another, this could be indicative of a real lending strategy towards Peru, and even may be indicative of broader based management strategies. For instance, if a bank were to have a relatively high percentage of its total lending in credits of free disposition and refinance - types of credit that usually are very attractive to borrowers - this might be indicative of a rather aggressive lending strategy. A more conservative strategy would be suggested by a bank that tended to have a relatively higher percentage of its loans in project or capital goods finance. It is under these assumptions that the following analysis is pursued.

a) Preferences of banks when grouped according to country of origin

Table 7.3 shows how banks, grouped according to their country of origin, distributed lending, relative to each other, among the various types of loans in the period 1971-1976. The data presented are standardized variables of the deviation from the unweighted mean distribution for all the country groups in the table. <sup>11/</sup>  
Of interest here are the more extreme deviations for loans classified as capital goods, projects, refinance, and free disposition. Loans for "other imports" were of negligible significance in total lending. Credits for nationalizations also are not of direct concern because they are more indicative of a separate dimension - solidarity with home country investors - that is not fully linked to lending strategies vis-a-vis Peru.

Table 7.3

PERU: APPARENT PREFERENCES FOR TYPES OF LOANS BY BANKS WHEN  
GROUPED ACCORDING TO COUNTRY OF ORIGIN, 1971-1976<sup>a/</sup>

(Standardized deviations about the global mean)<sup>b/</sup>

Country of the banks	Import K goods	Other imports	Refinance	Free disposition	Projects	National- ization	Other
United States	33.3	...	0.8	66.7	-107.4	14.3	200.0
Japan	-41.7	...	-38.1	173.6	-30.5	-38.9	100.0
Canada	20.8	...	38.1	44.8	-31.6	-38.9	150.0
United Kingdom	279.2	...	11.1	-65.5	49.5	-38.9	-75.0
Germany	-66.7	...	69.0	-211.5	193.7	-38.9	-75.0
France	-66.7	...	28.6	43.7	13.7	-38.9	-75.0
Italy	-66.7	...	83.3	63.2	-76.8	-38.9	-75.0
Switzerland	-66.7	...	-254.0	-75.9	-118.9	296.0	-75.0
Consortium	-12.5	...	127.8	-50.6	-45.3	-38.9	-75.0
Other	-16.7	...	-64.3	11.5	153.7	-38.9	-75.0

Source: Derived from data in Table A7.10 of the statistical appendix.

a/ Excludes loans with guarantees of export credit agencies.

b/  $Z = \frac{X - \bar{X}}{S}$  where X is the percentage of all authorizations by a country group in a given loan classification;  $\bar{X}$  is the unweighted average of all loans by all country groups in a given loan classification and S is the standard deviation of  $\bar{X}$ .

Looking first at loans considered to be of a more risky nature, one sees that consortium banks, Italian banks, and German banks had the greatest relative inclination to refinance. The relatively least receptive seemed to be Swiss banks, <sup>12/</sup> and perhaps banks in the category of "other". With regard to what is possibly the most risky of loans - credit of free disposition - one finds that the Japanese banks stand out for having by far the greatest relative participation in this area. Meanwhile, German, and to a lesser degree, Swiss and British banks, appear to have had relatively less inclination to enter into this type of finance.

Project loans, deemed to perhaps carry a perception of greater security, (and carry benefits related to support of corporate clients' exports) were relatively most pursued by German and "other" banks. British banks, which also were the relatively most involved in capital goods finance, appear to have pursued this more secure route as well. The relatively most uninvolved in project finance were Swiss and United States banks. <sup>13/</sup>

What tentative conclusions can be drawn from this particular set of data? Since one is dealing in standardized variables, a net balance of aggressive and conservative lending can be developed. This is done in table 7.4 where the standardized variables of each country group are added together according to whether they reflect aggressive or conservative strategies. The net impact is determined by changing the sign of conservative score and adding it to the aggressive score. A positive balance suggests a strategy of aggressive lending and a negative score suggests a conservative strategy. As can be seen, using the criteria set forth earlier, Italian and Japanese banks were relatively the most inclined to extend risky forms of credit and therefore could be classified as having been rather aggressive. The most conservative lenders

Table 7.4

PERU: EVALUATION OF PREFERENCES FOR TYPES OF LOANS BY BANKS  
WHEN GROUPED ACCORDING TO COUNTRY OF ORIGIN, 1971-1976

	Agressive <sup>a/</sup> (1)	Conservative <sup>b/</sup> (2)	Balance <sup>c/</sup> (3)
United States	67.5	-74.1	141.6
Japan	135.5	-72.2	207.7
Canada	82.9	-10.8	93.7
United Kingdom	-54.4	328.7	-383.1
Germany	-142.5	127.0	-269.5
France	72.3	-53.0	125.3
Italy	146.5	-143.5	290.0
Switzerland	-329.9	-185.6	-144.3
Consortium	77.2	-57.8	135.0
Other	-52.8	137.0	-189.8

Source: Table 7.3.

a/ Sum of standardized variables for loans of free disposition and refinance.

b/ Sum of standardized variables for project and capital goods finance.

c/ Sum of the columns for aggressive and conservative lending after inverting the sign of the latter. A positive score is indicative of an aggressive posture and a negative score is indicative of a conservative posture.

were the British, German and "other" banks. In between the extremes there were other groups of banks with less extreme evidence as aggressive or conservative lenders.



b) Preferences of banks when grouped according to size

A similar exercise was carried out on the banks grouped according to their size. Tables 7.5 and 7.6 provide the standardized variables and net balances of aggressive and conservative lending, respectively. As seen there is no clear cut functional relationship between size and aggressiveness of lending, at least according to the ranges of assets set forth in the table. But it is interesting to note that the three groups of banks with the smallest assets had relatively high scores with regard to the degree of aggressiveness of lending. One might have expected just the opposite; that smaller institutions would have been inclined towards securer forms of lending. Momentarily a reason will be suggested for this behavior.

2. Preferences for economic sectors

Just as an apparent proclivity for certain types of loans can be suggestive of strategies of banks, so can their selection of where to lend. With the exception of freely disposable loans and general purpose refinance credits, banks know in advance the specific destination of funds when they decide to enter into a credit agreement. Banks, of course, could be perfectly indifferent as to where the country will employ the resources, especially given a government guarantee. But it is known that some bankers believe that security can be enhanced by approving credits for activities that can generate their own repayment of the loan. In the case of such a view, a bank might avoid lending for activities which were clearly unable to service commercial debt.

Following this line of thinking, primary economic activities (agriculture, mining, manufacturing, etc.) would generally offer the strongest support for repayment. In most instances these activities are commercial in nature and best able to support commercial repayment terms.

Table 7.5

PERU: APPARENT PREFERENCES FOR TYPES OF LOANS BY BANKS  
WHEN GROUPED ACCORDING TO SIZE, 1971-1976<sup>a/</sup>  
(Standardized deviations about the global mean)<sup>b/</sup>

Asset range (millions of dollars) <sup>c/</sup>	World rank range (1-300)	Types of loans						
		Imports K goods	Other Imports	Refinance	Free disposition	Projects	National- ization	Other
1) 65 789 - 32 895	1- 10	100.0	...	90.4	-41.7	-73.5	-54.9	-87.5
2) 32 894 - 16 448	11- 46	163.6	...	-71.1	45.8	-16.3	54.9	-
3) 16 447 - 8 224	47- 91	81.8	...	77.1	-27.1	-134.7	3.9	50.0
4) 8 223 - 4 112	92-147	-90.9	...	-113.3	-133.3	89.8	227.5	112.5
5) 4 111 - 2 056	148-263	-90.9	...	-57.8	-75.0	185.7	-25.5	200.0
6) 2 055 - 1 634	264-300	-90.9	...	157.8	-20.8	-108.2	-100.0	-87.5
7) < 1 634	> 300	-	...	48.2	31.3	6.1	-100.0	-87.5
8) Unknown	...	-90.9	...	-134.9	225.0	51.0	-7.8	-87.5

Source: Table A7.1 of the statistical appendix.

a/ Excludes loans with guarantees of export credit agencies.

b/  $Z = \frac{X - \bar{X}}{S}$  where X is the percentage of all authorizations by banks of a size range in a given loan classification;  $\bar{X}$  is the unweighted average of all loans by all size groups in a given loan classification and S is the standard deviation of  $\bar{X}$ .

c/ Asset range is based on dollar figures for 1975 as found in The Banker, June 1976. see footnotes a + b in table 5.5.

Table 7.6

PERU: EVALUATION OF PREFERENCES FOR TYPES OF LOANS BY BANKS  
WHEN GROUPED ACCORDING TO SIZE, 1971-1976

Asset ranges	World rank range	Aggressive <sup>a/</sup> (1)	Conservative <sup>b/</sup> (2)	Balance <sup>c/</sup> (3)
Group 1	1- 10	48.7	26.5	22.2
Group 2	11- 46	-25.3	147.3	-172.6
Group 3	47- 91	50.0	-52.9	102.9
Group 4	92-147	-246.6	-1.1	-245.5
Group 5	148-263	-132.8	94.8	-227.6
Group 6	264-300	137.0	-199.1	336.1
Group 7	> 300	79.5	6.1	73.4
Group 8	...	90.1	-39.9	130.0

Source: Table 7.5.

<sup>a/</sup> Sum of standardized variables for loans of free disposition and refinance.

<sup>b/</sup> Sum of standardized variables for project and capital goods finance.

<sup>c/</sup> Sum of the columns for aggressive and conservative lending, after inverting the sign of the column on conservative lending. A positive score is indicative of an aggressive posture and a negative score a conservative posture.

Considerably more risk might be perceived in loans to secondary sectors (water, sewerage, power, transport, etc.) because these activities often are not self-financing (this was certainly true for Peru) and therefore the capacity to repay loans must come from outside the sector itself. Also from the standpoint of risk, it might be even less attractive to lend to tertiary sectors, which in this case basically are social infrastructure. This is because social services are rarely profitable from the standpoint of private rates of return, and payouts (social or otherwise) generally are a very long term proposition. Thus, for repayment commercial banks also clearly would have to look to financial flows generated from sectors other than where the loan was placed.

One would suspect that some banks, in an attempt to enhance perceived security, might pursue what could be termed a relatively cautious lending strategy by favoring primary sectors over secondary and tertiary sectors. For an individual bank, this might be considered prudent policy. However, from the standpoint of the borrower, loans to secondary and tertiary activities could be viewed as being desirable and necessary because of the paucity of long term finance available from official institutions for these sectors. <sup>14/</sup> For this reason it is of interest to see what types of banks pursued a relatively more bold policy with regard to finance of secondary and tertiary activities.

a) Preferences of banks when grouped according to country of origin

Table 7.7 displays data similar to that of the previous section which help to highlight the apparent relative preferences of banks when grouped according to their country of origin. It is seen that the institutions relatively most committed to the safer primary sectors were British and French banks. In the more risky secondary and tertiary sectors, "other banks" were by far the most heavily committed in relative terms.

Table 7.8 presents the balance of conservative and aggressive strategies. "Other" banks stand out for their relatively greater willingness to lend to

Table 7.7

PERU: APPARENT SECTORAL PREFERENCES OF BANKS WHEN GROUPED  
BY COUNTRY OF ORIGIN, 1971-1976<sup>a/</sup>

(Standardized deviations about the global mean)<sup>b/</sup>

Sector <sup>c/</sup>	United States	Japan	Canada	United Kingdom	Germany	France	Italy	Switzerland	Consortium	Other
Primary	-	-63.8	20.7	144.0	-30.2	219.0	-19.8	-113.8	-86.2	-69.8
Secondary and tertiary	-96.4	3.6	-103.6	79.5	56.3	63.4	-73.2	-111.6	-33.9	217.0
(Secondary)	(-114.4)	(24.0)	(-126.0)	(118.3)	(93.3)	(69.2)	(-46.2)	(-87.5)	(-86.5)	(159.6)
(Tertiary)	(28.9)	(-55.3)	(39.5)	(-89.5)	(-89.5)	(-2.6)	(-89.5)	(-89.5)	(136.8)	(202.6)
Unclassified <sup>c/</sup>	60.3	39.1	51.4	-143.0	-15.6	-181.6	58.1	143.6	77.1	-90.5

Source: Derived from Table A7.13 of the statistical appendix.

a/ Excludes loans with guarantees of export credit agencies. Only accounts for credits where both borrower and lender had ex ante agreement on destination of credit.

b/  $Z = \frac{X - \bar{X}}{S}$  Where X is the percentage of all authorizations by banks of a country group in a given sectoral classification;  $\bar{X}$  is the unweighted average of all loans by all country groups in a given sectoral classification and S is the standard deviation of  $\bar{X}$ .

c/ Loans that went to a number of undesignated sectors. These are basically general refinance credits.

Table 7.8  
 PERU: EVALUATION OF SECTORAL PREFERENCES BY BANKS WHEN GROUPED  
 ACCORDING TO COUNTRY OF ORIGIN, 1971-1976

Country of banks	Agressive <sup>a/</sup> (1)	Conservative <sup>b/</sup> (2)	Balance <sup>c/</sup> (3)
United States	-96.4	-	-96.4
Japan	3.6	-63.8	67.4
Canada	-103.6	20.7	-124.3
United Kingdom	79.5	144.0	-64.5
Germany	56.3	-30.2	86.5
France	63.4	219.0	-155.6
Italy	-73.2	-19.8	-53.4
Switzerland	-111.6	-113.8	2.2
Consortium	-33.9	-86.2	52.3
Other	217.0	-69.8	286.8

Source: Table 7.7.

a/ Standardized variables for lending to secondary & tertiary sectors.

b/ Standardized variables for lending to primary sectors.

c/ Sum of standardized variables for columns of aggressive and conservative lending, after inverting the sign of the latter. A net positive balance suggests an aggressive posture, while a net negative balance suggests a conservative posture.

secondary and tertiary sectors. German, Japanese and Consortium banks also pursued significantly aggressive strategies in this regard. On the other side, French and Canadian banks had the most conservative scores.

b) Preferences of banks when grouped according to size.

When the subject is viewed from the standpoint of the size of the banks, no clearcut functional relationship is found (see tables 7.9 and 7.10). There is, however, a notable concentration of conservative strategies in group 4 and group 6 of the banks. Also, it is interesting that the group of smallest banks (7) had the most significant aggressive score.

### 3. Overall evaluation

Taking the two aspects of lending and combining the results would provided for an overall typology of behavior based on the nature of lending. It is still convenient to view separately banks when grouped according to country of origin and size.

a) Banks when grouped according to country of origin

Table 7.11 presents a summary typology of the nature of lending. It is seen that the relatively most aggressive lenders were Japanese banks. Somewhat behind these institutions were Italian and Consortium banks, followed by "other" banks and American institutions. The most conservative lenders were British banks. Considerably behind the British banks in terms of conservativeness were German and Swiss banks. Following them were Canadian and French lending institutions both of which had rather marginal conservative scores.

The behavior of Consortium banks with regard to the nature of their lending provides further credence to the notion that they were very aggressive lenders to Peru. As was seen earlier in the Chapter, they tended to have the heaviest relative commitment to Peru, although this risk may have been compensated somewhat by their higher than average fees on loans. In addition to the relatively

Table 7.9

PERU: APPARENT SECTORAL PREFERENCES OF BANKS WHEN  
GROUPED ACCORDING TO SIZE, 1971-1976<sup>a/</sup>

(Standardized deviations about the global mean)<sup>b/</sup>

Sectors	Asset size (millions of dollars) <sup>c/</sup>							
	65 789- 32 895	32 894- 16 448	16 447- 8 224	8 223- 4 112	4 111- 2 056	2 035- 1 634	<1 634	Unknown
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Primary	-25.9	-59.5	-88.8	112.1	-41.4	203.5	-112.1	10.4
Secondary and tertiary	-9.9	-41.6	-24.8	-5.9	115.8	-218.8	101.0	81.2
(secondary)	(-41.1)	(-4.1)	(27.4)	(13.7)	(80.8)	(-237.0)	(116.4)	41.1)
(tertiary)	(50.0)	(-97.5)	(-112.5)	(-40.0)	(145.0)	(-120.0)	(42.5)	(130.0)
Unclassified <sup>d/</sup>	44.8	126.4	149.4	-143.6	-80.5	-18.4	31.0	-109.2

Source: Derived from data in table A 7.13 in the Statistical Appendix.

<sup>a/</sup> Excludes loans with guarantees of export credit agencies. Also, only accounts for credits where both borrower and lender had ex ante agreement on the destination of credit.

<sup>b/</sup>  $Z = \frac{X - \bar{X}}{S}$  where X is the percentage of all authorizations by banks of a size range in a given sectoral classification;  $\bar{X}$  is the unweighted average of all loans by all size groups in a given sectoral classification and S is the standard deviation of  $\bar{X}$ .

<sup>c/</sup> Asset range is based on dollar figures for 1975 as found in The Bankers, June 1976. See footnotes a & b of table 5.5.

<sup>d/</sup> Loans that went to a number of undesignated sectors. These are basically general refinance credits.



Table 7.10

PERU: EVALUATION OF SECTORAL PREFERENCES OF BANKS WHEN  
GROUPED ACCORDING TO SIZE, 1971-1976

Asset range	World rank range	Agressive	Conservative	Balance
		<u>a/</u>	<u>b/</u>	<u>c/</u>
		(1)	(2)	(3)
Group 1	1 - 10	-9.9	-25.9	16.0
Group 2	11 - 46	-41.6	-59.5	17.9
Group 3	47 - 91	-24.8	-88.8	64.0
Group 4	92 - 147	-5.9	112.1	-118.0
Group 5	148 - 263	115.8	-41.4	157.2
Group 6	264 - 300	-218.8	203.5	-422.3
Group 7	> 300	101.0	-112.1	213.1
Group 8	...	81.2	10.4	70.8

Source: Table 7.9.

a/ Standardized variables for the secondary or tertiary sectors.

b/ Sum of the standardized variables for the primary sectors.

c/ Sum of the columns for aggressive and conservative lending, investing the sign of the later. A positive score suggests an aggressive posture, while a negative score suggests a conservative posture.

Table 7-11  
PERU: SUMMARY EVALUATION OF BANK PREFERENCES FOR TYPES  
OF LOANS AND ECONOMIC SECTORS, 1971-1976

(Net standardized scores)<sup>a/</sup>

Banks	Banks grouped according to country of origin		Total
	Type of loan	Sectoral lending	
United States	141.6	-96.4	45.2
Japan	207.7	67.4	275.1
Canada	93.7	-124.3	-30.6
United Kingdom	-383.1	-64.5	-447.6
Germany	-269.5	86.5	-183.0
France	125.3	-155.6	-30.3
Italy	290.0	-53.4	236.6
Switzerland	-144.3	2.2	-142.1
Consortium	135.0	52.3	187.3
Other	-189.8	286.8	97.0
Banks grouped according to size			
	Type of loan	Sectoral lending	Total
Group 1	22.2	16.0	38.2
Group 2	-172.6	17.9	-154.7
Group 3	102.9	64.0	166.9
Group 4	-245.5	-118.0	-363.5
Group 5	-227.6	157.2	-70.4
Group 6	336.1	-422.3	-86.2
Group 7	73.4	213.1	286.5
Group 8	130.0	70.8	200.8

Source: Table 7.4; 7.6; 7.8; 7.10.

<sup>a/</sup> Net balance of conservative and aggressive aspects of lending, evaluating type of credit extended and the sectoral destination of credit. A positive score is indicative of aggressive lending and a negative score is indicative of conservative lending.

heavy commitment, they are seen here to have had one of the boldest strategies with regard to the nature of their lending. The strategy undoubtedly was influenced by what was seen earlier to be the umbrella security provided by the parents of the consortium banks. Another reason for the relatively more bold style could have been related to size. Because of their small size, consortium banks cannot extend loans in absolutely large amounts. Therefore, in the formation of syndicates, they may be "pushed out" of more attractive (and over subscribed) loans by banks willing to take on a relatively large participation. Thus, consortium banks, in order to expand their portfolios, may have found it necessary to have a higher proportion of their lending in loans with a character of greater relative risk; in these types of credits lead banks might have been more receptive to small credits that would help to successfully syndicate the loan.

The relatively aggressive performance of Japanese banks is really not a surprise; as latecomers in international lending, they have been known for their aggressive strategies 15/ and ~~these~~ <sup>plus findings in the previous section,</sup> data on Peru, merely confirm this impression. Italian banks generally are not discussed in the same light as Japanese banks, but the nature of their lending to Peru suggests that they very well might merit a position in the camp of bold lenders. The fact that U.S. banks received an aggressive score can be attributed in part to the behavior of newcomers to the international scene like the regional institutions and a few very large money center banks that were far less than traditional in their behavior.

The group titled "other" banks obtained a significant score on the aggressive side of the ledger, basically because they tended to have a relatively high incidence of lending in more risky secondary and tertiary sectors. They also, as was seen in section II of the Chapter, extended longer than average maturities. Thus, these banks were bold with respect to areas which may be very important to developing country borrowers. The motivation for such behavior could be a variant of that just suggested for consortium banks: while showing a preference for safer project lending, their marginal position in international

financial flows caused them to have a greater willingness to enter into secondary and tertiary sectors where bidding for loans may have been less keen.

b) Banks grouped according to size

With regard to the largest banks (groups 1-3), it is seen that groups 1 and 3 had significant aggressive scores. All the intermediate-sized banks (groups 4-6), on the other hand, had net conservative scores. And, finally, the smallest banks groups 7 and 8 (assuming 8 is basically smaller institutions) had net aggressive scores.

If one remembers earlier in the Chapter, group 3 of the banks was found to charge a significantly higher than average libor spreads on their loans. This may have effectively offset much of the greater <sup>perceived</sup> risk taken on the nature of their lending, leaving only the very largest banks (group 1) with clear evidence of an aggressive strategy. And this aggressiveness, which is by no means overwhelming in terms of the net score, probably is a function of a risk perception conditioned by their enormous size and great experience in international lending.

As for the rather aggressive scores of smaller banks, one suspects that the explanation is similar to that given above for consortia and "other" banks; indeed, these two groups of institutions are, to a large extent, located in groups 7 and 8 of banks grouped according to size.

B. Preference for Home Country Export Credit Guarantees

Up to now analysis only has been on lending where the banks have borne the full risk of the credit. However, most home countries of commercial banks have agencies which guarantee loans that are in support of the home country's exports. One already has seen in Chapter 5 that loans carrying such guarantees usually carry terms that are more favorable than unguaranteed commercial credits. This stands to reason because a bank, by obtaining such a guarantee, essentially avoids all risk on the guaranteed portion of its credit. In order to gain such a

guarantee, a bank must be willing to finance the purchase of the home country's goods and services, and the export credit agency must have a favorable enough attitude towards the borrowing country to assume the risk.

Banks which were exceptionally risk conscious with regard to their lending to Peru, could have limited their exposure in absolute terms and where possible orient finance towards loans that would pass the risk onto home country governments. A bank that had a proclivity to pursue such a strategy could be considered to have had a conservative view towards Peru, and a perhaps cautious attitude to LDC governments in general.

Table A7.14 of the statistical appendix lists the banks that lent under export credit guarantees. Banks for which guarantees made up a significant part of total lending were all classified in Chapter 5 as lenders of intermediate or minor importance to Peru; no major lender took heavy recourse to such guarantees.

When these banks are grouped according to country of origin (table 7.12), it is seen that those institutions that had the relatively greatest reliance on external home country guarantees were British, French, and "other" banks. Other country groups appear to have taken little or no recourse to such facilities.

It already has been seen that British and French banks pursued a rather conservative lending strategy on the loans for which they bore the full risk. The fact that they also were the most inclined to seek support from home country export credit agencies gives further support to the notion that they were cautious lenders. The other conservative lenders, Switzerland and Germany, did not take much use of such guarantees. Of the banks classified beforehand as aggressive in their lending policy only "other" banks made extensive use of export credit guarantees. While this adds a conservative dimension to "other" banks, it lends further credence to the aggressive posture attributed to the remaining banks. 16/

A priori grounds would suggest that reliance on guarantees might be a function of size, i.e., the smaller the bank the more likely it would be to seek the security of an export credit guarantee. Data on guarantees (see table 7.13) provided some limited support to this thesis as the degree of reliance on guarantees was less marked for very large banks (groups 1-3) than smaller

Table 7.12

PERU: LOANS WITH A GUARANTEE OF AN EXPORT CREDIT AGENCY GROUPED ACCORDING  
TO COUNTRY ORIGIN OF THE BANK, 1971-1976

(Percent)

	Guaranteed credits of country group as a percent of guaranteed credits of all banks	Guaranteed credits as a percent of all credits granted by banks in the country group
United States	8.5	1.4
Japan	-	-
Canada	-	-
United Kingdom	26.1	39.0
Germany	-	-
France	26.4	59.6
Italy	0.1	0.5
Switzerland	1.0	3.7
Other	37.9	49.2
Consortium	-	-
<u>All banks in the study</u>	<u>100.0</u>	<u>9.7</u>

Source: CEPAL, on the basis of official data.

a/ Represents loans where it was possible to detect a guarantee. It is important to note that the borrower may not always be aware of the presence of a guarantee and this could cause the above data to understate protected credits.

Table 7.13

PERU: LOANS WITH A GUARANTEE OF AN EXPORT CREDIT AGENCY ACCORDING  
TO THE SIZE OF THE LENDING BANK, 1971-1976<sup>a/</sup>

Asset range <sup>b/</sup> (millions of dollars)	World rank range (1 - 300)	Guaranteed credits of size group as a percent of guaranteed credits of all banks	Guaranteed credits as a percent of all credits granted by banks in the size group
1) 65 789 - 32 895	1 - 10	9.2	5.1
2) 32 894 - 16 448	11 - 46	31.2	7.4
3) 16 447 - 8.224	47 - 91	16.5	8.7
4) 8 223 - 4 112	92 - 147	22.5	28.4
5) 4 111 - 2 056	148 - 263	9.1	12.8
6) 2 055 - 1 634	264 - 300	1.8	25.6
7) < 1 634	> 300	5.5	10.5
8) Unknown	...	4.2	15.5
<u>All banks in the study</u>	...	<u>100.0</u>	<u>9.7</u>

Source: CEPAL, on the basis of official data.

<sup>a/</sup> See footnote a of table 7.12.

<sup>b/</sup> Asset range based on 1975 data in The Bankers, June 1976. See footnotes a & b of table 5.5.

banks. However, after that the relationship is not clean as one group of intermediate-sized banks had a reliance on guaranteed credits that was more than double that of some smaller banks. So again there is further evidence that intermediate sized banks may be relatively more cautious than their smaller rivals.

Finally, unlike the country groupings, when banks are viewed from the standpoint of size, there is no evidence of an outstanding reliance on export credit guarantees by any single group of banks.

#### IV. The Lending Behavior of Banks with Branches, Subsidiaries and Affiliates in Peru

One might think on a priori grounds that international banks with direct interests in Peru, e.g. a branch bank or subsidiary, would behave somewhat differently than banks which had ties to Peru only through international loan flows. There are a number of reasons why this might be so.

First, a bank with, say, a branch in Lima would have capital in Peru itself; in 1970 branches had a minimum capital requirement of \$60,000,000 soles (about 1.5 million dollars). <sup>17/</sup> In addition, there would be accumulated assets from business with private firms in Peru; indeed, business with local foreign and, secondarily, national firms probably was the principal motivation for establishing a branch in the first place. Thus, an international bank in this situation might have relatively greater interest in cultivating the good will of the national government whose policies could affect the operations of the branch bank. This might manifest itself in a relatively high profile in the external (and internal) lending to the government, as well as a greater proclivity to develop an image of a good citizen through the extension of highly visible finance, e.g., support of projects of a social character on relatively favorable terms.



A second reason for special behavior, which really is a variant of the first, is that an unhealthy Peruvian economy may be adverse to the bank's branch operations. For instance, a foreign exchange crisis could mean that the branch and its clients would have trouble servicing their foreign lines of credit; thus the parent would be interested in helping to keep the country's balance of payments afloat. Under these circumstances a bank might be more inclined to extend balance of payments finance, even in times of extreme economic duress.

A third reason why these types of banks may behave in a somewhat special fashion is that establishment of a branch or affiliate in Peru would provide for a familiarity with <sup>the country</sup> / that would be unavailable to banks with no offices within the national frontiers. Direct familiarity with the local economy and public officials could make for a different perception of risk than if a bank had to rely on secondary information and sporadic "on-site" visits to the country for the formulation of its attitude on Peru.

Finally, special behavior may be brought about by government decree. In the case of Peru, this latter factor was relevant. In a special 1970 law on foreign branch banks, the revolutionary government decreed that branches (or their parents) had to provide the government with a foreign currency line of credit of no less than double their assigned capital. The line had to be over and above regular lending and on terms suitable to the government. At the same time, foreign branches at the end of each quarter had to extend another foreign currency line of credit to state banks in an amount equal to the increment in the branch's deposits. The interest rates on such lines could not exceed the parent bank's prime rate. 18/

It is with these considerations that the following analysis on banks with operations in Peru is undertaken.

A. The banks with interests in Peru: importance as lenders

Table 7.14 presents a list of international banks with bank branches or subsidiaries/affiliates in Lima, the date of establishment the Peruvian operation, the importance of the international banks as lenders to Peru, their relative commitments to the country, and their importance as leaders in syndicated credits to Peru.

As can be seen, the most established foreign branch bank in Peru pertains to Citicorp, which has had an office in Lima since 1920. Lloyds Bank also has had a long relationship with Peru. On the other hand, Bank of America and Bank Tokyo are relative newcomers, with their offices opening in the mid-60's. Two European banks, Banca Commerciale Italiana y Credit Lyonnais had subsidiaries in Peru until the banking reform laws, when their participation in the subsidiaries was reduced to below 20% (although management remained decidedly oriented towards the old parents).

The table also displays 3 banks which had operations in Peru prior to 1971. As noted in Chapter 3, Chase Manhattan bought majority control of a local bank in 1965. It was nationalized in 1970, but on terms highly favorable to Chase. Prior to 1966, Chemical Bank's relationship with Peru was basically limited to lines of credit to local banks, but in 1966-67 it became a major shareholder in Banco Internacional. The purchase proved to be unwise, however; it generated resentment, was a key factor behind a mid-1968 law calling for Peruvianization of banks, and ended up in nationalization in 1970 under the revised banking reform laws. <sup>19/</sup> Lastly, the Royal Bank of Canada, which had the second oldest foreign branch in Lima, closed its office at the end of the 1960's, presumably due in part to the controversy over Peruvianization of the local banks.

Of all the banks with direct interests in Peru, Citicorp stands out for its importance. It was a major lender to Peru throughout the 12 years; it was a major lead

Table 7.14

PERU: BANKS WITH BRANCHES, SUBSIDIARIES OR AFFILIATES IN PERU AND THEIR  
IMPORTANCE AS LENDERS TO THE GOVERNMENT, 1965-1970 AND 1971-1976

Name	Date of establishment	Importance as a lender to Peru <u>a/</u>		Relative commitment to Peru <u>b/</u>		Importance as lead bank <u>c/</u>	
		1965-1970	1971-1976	1965-1970	1971-1976	As agent and/or manager	As only agent
<u>Branches</u>							
Citicorp	1920	Major	Major	Intermediate	Intermediate	Major	Major
Lloyds Bank	1936	Minor	Intermediate	Low	Low	Intermediate	Minor
Bank of Tokyo	1965	Minor	Intermediate	Low	Low	Intermediate	Intermediate
Bank of America	1966	Major	Major	Intermediate	Low	Intermediate	-
<u>Subsidiaries or affiliates</u>							
Banca Commerciale Italiana <u>d/</u>	...	Minor	Intermediate	Low	Low	Minor	Minor
Credit Lyonnais <u>e/</u>	...	-	Intermediate	-	Low	Minor	Minor
<u>Banks with firms in Peru until 1970</u>							
Chase Manhattan <u>f/</u>	1964-1965	Major	Major	Low	Low	Intermediate	Minor
Chemical Bank <u>g/</u>	1966-1967	-	Intermediate	-	Low	Intermediate	-
Royal Bank of Canada <u>h/</u>	1920's	Minor	Intermediate	Low	Intermediate	Intermediate	-

Source: CEPAL, on the basis of official data.

a/ Based on gross authorizations in each period as presented in Chapter 5.

b/ Based on gross authorizations scaled to size as presented in Chapter 7.

c/ Based on data on syndicated credits as presented in Chapter 6.

d/ Major foreign owner of Banco de Crédito. Date of established ownership unknown. Before banking reform laws this institution, through its affiliate Sudameris, owned 62% of the local bank's stock. This was reduced to less than 20% under the banking reform laws.

e/ Had a large holding in the Banco de Lima. As a result of the banking reform laws its share was reduced to less than 20%. Date of establishment unknown.

f/ Bought 51% of Banco Continental. Was nationalized in 1970 by the government under the banking reform laws.

g/ Was a major shareholder in Banco Internacional. Bought out by the government in 1970 under the banking reform laws.

h/ Closed its branch in the late 60's.

bank and agent in syndicated credits, and its relative commitment to Peru was of an intermediate level. The bank of next importance would be Bank of America followed by Bank of Tokyo, and then Lloyds Bank. Of distinctly less importance than this former group are the two banks with subsidiaries/affiliates in Lima.

B. Did Direct interests in Peru affect the behavior of the banks?

It is difficult to establish a causal relationship between operations in Lima and a bank's behavior as an international lender to the government. Nevertheless, some observations can be made in this regard.

1. The volume of lending

It was seen earlier that there is some evidence that banks discriminate among borrowers through their volume of credit rather than through their pricing of loans. It would be interesting to know whether the presence of a branch or affiliate in Lima caused a bank to lend more to Peru than it might have in the absence of such a direct relationship. The question is somewhat problematical without complete information on a bank's portfolio and management strategy. Thus what follows is necessarily more conjecture than fact and the reader should take this into account when absorbing the material.

It would seem significant that the banks with branches in Lima had generally greater importance as lenders than banks with subsidiaries and affiliates. The stakes in branches and financial benefits derived from their activities presumably are greater in the former than the latter. Thus, one would indeed expect that if there was any causal relationship between direct interests in Lima and the volume of foreign currency loans by a bank that institutions with branches in Lima would have relatively greater profiles in lending to the government. But the question remains as to whether volume was unusual for the bank and whether behavior was attributable to its direct relationship with the local economy.

The fact that Citicorp was a major lender and a major lead bank in itself reveals no special behavior towards Peru. Citibank is the second largest banking institution in the world; it is known to be perhaps the most "internationalized" commercial bank in the world; it has been a rather persistent lender to LDCs, particularly in Latin America; and it has been ranked at the top of major lead banks in world syndication. 20/ Thus its dominant position in Peru—a country that was generally acceptable to the market after 1971—could be only reflective of the bank's overall position in world finance. 21/ The only hint of a special relationship with Peru is that its relative commitment is of an intermediate level with regard to all banks in the study. Citibank is known to pursue a policy of greater diversification (low relative commitment), consistent with its somewhat bold global lending strategy. 22/ But its level of relative commitment was higher than any other bank with direct interests in Lima; indeed it was seen in table 7.1 that it was higher than almost all other superbanks lending to Peru. Thus, one suspects that Citibank may have had a somewhat heavier commitment to Peru vis-a-vis its overall portfolio in LDCs. This conclusion would even seem logical given that the Lima branch is one of the oldest in the Citicorp network, giving Peru the distinction of being one of the bank's most familiar LDC clients.

On the basis of volume, one cannot see a relatively more favorable attitude on the part of Bank of America. Although it is a major lender to Peru, this may be just a function of its enormous size (Nº 1 in the world) and dedication to international lending. Its intermediate position as a lead bank actually suggests a conservative attitude towards Peru because on a world scale Bank of America has been ranked near the very top of lead banks in syndication. 23/ Also, its low level of relative commitment may be indicative of a conservative attitude since this bank—which has a low risk, low yield management policy—is known for less diversification than many other banks. 24/ Thus if Peru had merited special attention by the bank, one might have expected a somewhat higher relative commitment.

Since the study has less supportive information on the Bank of Tokyo and Lloyds Bank, evaluations become even more difficult for them. Nevertheless, both banks are large (N°s 28 and 31, respectively) in world terms, but not so large as to make their position as lenders of intermediate importance seem unduly low. This is even more true given that Latin America, and Peru in particular, have not been heavily oriented towards England or Japan (although the latter has recently grown in importance) in the post-war period. The intermediate position of Bank of Tokyo as a lead bank is not inconsistent with its world position in this regard. The intermediate position of Lloyds Bank, however, may be relatively lower than expected given that it has ranked in the top 10 lead banks of world syndication. 25/ The above factors, coupled with the low level of relative commitments for both banks, on face value would not lend support to the thesis of a special behavior towards Peru.

As for the two banks with affiliates in Peru, their role as lenders and lead banks are not exceptional, and their relative commitments are low. Credit Lyonnais would seem to have had the least committed position of the two, given that it was the seventh largest bank in the world (1975) and has been in the top 10 lead banks of world syndication. 26/ One could argue, however, that without the affiliates in Lima their presence as lenders would have been even less significant due to the fact that Peru is not generally considered to be in the mainstream of French or Italian geopolitical-business interests.

It would be interesting to see whether the change in government policies in general, and towards local banks in particular, after 1968 affected the lending behavior of foreign banks with operations in Lima. Overall it would appear that there was no adverse effect after the initial breaking of the financial blockade in 1972.

With regard to banks currently with operations in Lima, their importance as lenders to Peru either remained the same or increased between 1965-1970 and 1971-1976

And only in the case of Bank of America did relative commitments fall; however, this was only relative to other banks as the absolute level of commitment was roughly the same in the two periods.

In this context it might be more revealing to view the reaction of banks that had to close their operations in Peru as a result of the policy to Peruvianize the local financial market. It can be seen in Table 7.13 that there were no apparent adverse impacts on lending to the government; indeed, Chemical Bank and Royal Bank of Canada actually became more important lenders in 1971-1976 and even increased their relative commitments to the government.

Notwithstanding the above, there is reason to believe that at least Chemical Bank had a relatively strong reaction to the military government's policies in general, and nationalization of its subsidiary in particular. While most major international banks had returned to lending to the government by 1972, and most certainly by 1973, Chemical Bank, number 23 in the world in terms of size (1975) was conspicuous by its absence. It did not extend any significant medium term credit to the government until the first half of 1974. Moreover, on this occasion it entered the market in a very symbolic way by participating in the syndicated credit associated with the Greene Accord, which, of course, marked the formal establishment of peace between U.S. political-business interests and the government of Peru. This observation also coincides with information from industry sources which claimed that for many years high ranking Chemical Bank officials were openly bearish on the military government of Peru.

## 2. Terms of lending

All the banks with operations in Lima, except Credit Lyonnais, figured in the student's *t* tests on average terms that appeared earlier in the chapter. It may be recalled that in general little significant deviation was found from market trends. However, a rough statistical technique did hint that Bank of America had a tendency to price flat fees under the prevailing market terms (see table A7.7). However, it is doubtful that this is a reflection of special behavior towards Peru. It is known to be an institution with a low risk, low yield strategy on lending. <sup>27/</sup> Therefore the lower fee structure may be a reflection of a general management strategy that does not put much emphasis on increasing yields through aggressive pricing of fees.

With regard to creating favorable inflection points in market trends, only the Bank of Tokyo could fall into this category. As seen earlier, in the first half of seventies it played a moderate role in the lowering of spreads and lengthening of maturities on government loans. However, this is probably more reflective of the general strategies of Japanese banks in the period than any special behavior towards Peru.

Another aspect of pricing which was not examined earlier, but would be of concern here is the degree to which banks extended fixed interest rate loans. It has been seen that fixed interest rate loans pass the risk of inflation onto the lending institution, while variable rates cause a borrower to bear such risk. It is possible that a bank with direct operations in Lima might be more inclined to extend fixed interest rate loans to the government in order to gain favor and protect its local business.

Table 7.15 displays the distribution of loans for banks with operations in Lima according to whether they were priced with a fixed or variable (libor and prime spreads) rates.

In 1965-1970 a number of banks tended to carry out a greater proportion of their lending in fixed interest rates than was the norm, as measured by the average for all banks in the period. Bank of Tokyo and Banca Commerciale Italiana extended all their loans with fixed rates. However, both banks lent relatively



Table 7.15

PERU: DISTRIBUTION OF LOANS ACCORDING TO WHETHER PRICED WITH FIXED INTEREST RATE, LIBOR SPREAD OR PRIME SPREAD FOR FOREIGN BANKS WITH OPERATIONS IN PERU, 1965-1970 AND 1971-1976

(Percent)

	1965-1970				1971-1976			
	Fixed rate	Libor spread	Prime spread	Total <sup>a/</sup>	Fixed rate	Libor spread	Prime spread	Total <sup>a/</sup>
<u>With branches in Lima</u>								
Bank of America	30.2	-	69.8	100.0	0.9	97.5	1.6	100.0
Citicorp	12.5	-	87.5	100.0	-	98.8	1.2	100.0
Bank of Tokyo	100.0	-	-	100.0	20.3	76.0	3.7	100.0
Lloyds Bank	-	100.0	-	100.0	-	94.7	5.3	100.0
<u>With subsidiaries/affiliates in Lima</u>								
Banca Commerciale Italiana	100.0	-	-	100.0	-	100.0	-	100.0
Credit Lyonnais	-	-	-	100.0	-	100.0	-	100.0
<u>With operations in Lima until 1970</u>								
Chase Manhattan	14.5	-	85.5	100.0	2.5	97.5	-	100.0
Chemical Bank	-	-	-	100.0	-	100.0	-	100.0
Royal Bank of Canada	-	-	100.0	100.0	-	83.0	17.0	100.0
<u>All banks in the study</u>	<u>15.8</u>	<u>3.4</u>	<u>80.8</u>	<u>100.0</u>	<u>1.3</u>	<u>94.1</u>	<u>3.5</u>	<u>100.0</u>

Source: CEPAL, on the basis of official data.

<sup>a/</sup> May sum to less than 100 due to the presence of interest rates distinct from those cited in the table.

little resources in the period, making it difficult to conclusively attribute to them a special strategy involving fixed interest rate loans to the government.

The only other bank to extend an unusually high proportion of fixed interest rate credits was Bank of America. This may have been due to general policy since the bank is known within the industry to be more inclined than most to extend fixed interest loans. <sup>28/</sup> However, given that it was attempting in the mid 60's to open a branch in Lima, there is a greater likelihood that the high percentage is directly linked to prospective business operations in Peru. Indeed, all the fixed interest credit was extended in 1965, a year in which the bank's application for a branch was being considered by the government.

Turning to 1971-1976, in this period there is little support to the thesis that banks with operations in Lima might have been more inclined for reasons of public relations to extend fixed interest rate loans. Only one bank—Bank of Tokyo—had an unusually high percentage of fixed interest credits. Without more information on this institution's global strategy, however, it is difficult to determine whether such behavior was a reflection of special interests in Lima or a more generalized policy of aggressive lending to LDCs.

The relatively low percentage of fixed interest credits extended by Bank of America might be viewed with some surprise. As just mentioned, it has the reputation of extending a greater percentage of fixed interest credits than the industry average; however, this is not reflected in its loans to the government of Peru, even though one might have expected some consideration given a branch operation in Lima. This may be another indication of a relatively conservative view on Peru during the period 1971-1976.

### 3. The nature of lending

Another point worth considering about banks with operations in Lima is whether the nature of the parents' external lending was in any way conditioned by their direct relationship with Peru. Again, without complete information

on a parent bank's portfolio and management strategy, any determination in this area is of necessity inconclusive. However, there is nevertheless some indication that patterns of lending were determined by broader considerations than those underlying loans by banks without a direct operational link to the country.

It was thought that parent banks might show a tendency to extend, to a more than usual degree infrastructural project loans. This is because of their high public visibility. Also, loans of free disposition were thought to be another type of loan that these banks might have been more inclined to extend because of the favorable impression it could make on government authorities. As far as sectors are concerned, one might have expected the parents to have been relatively more committed to secondary, and especially tertiary sectors, again for reasons of good image.

While some of the banks with offices in Lima did have lending with one or more of these characteristics, data did not show any conclusive tendencies in this direction. Only the Bank of Tokyo might have come close to the defined behavior. However, there were specific instances where the kind of lending undertaken was clearly related to image and concern about local operations. Three examples of this type of behavior are given below.

One clear case of where a loan to the government was direct offshoot of a foothold in the local market is reflected by actions of Bank of America. In 1965 it had an application pending for a new branch in Lima. In support of its application the parent bank approved a "showcase" loan, i. e., a highly visible credit that under normal circumstances probably would not have been attractive to a lender, especially in the generally conservative environment of the 60's. The loan was a rather large 10 million dollar credit to the Municipality of Lima for improvement of the city's road system. The money carried a fixed interest rate of 6.5% for 6½ years. Such a credit clearly had its risks, notwithstanding the presence of a guarantee by the Central Government. The dollar resources were to cover the basically local costs of a project that had the capacity to generate neither foreign or local resources for repayment.

Another example of where local operations induced foreign currency credits to the government was in 1972. In that year parents of all foreign branches in Lima extended credits for  $1-1\frac{1}{2}$  million dollars each for the import of cattle. The terms were very favorable for the period, ranging from 1.5% over a prime to 1.125 over libor, with maturities ranging from 5 to 9 years. Both the terms of the credit and its destination would not indicate that it was an exciting venture for the banks. However, the banks clearly had motives external to the loan itself: (i) the credit was formally conditioned by the continued existence of branches in Lima and (ii) the value of the loan could be accounted towards the minimum capital requirements of the branches.

The last example involves finance of the transandean oil pipeline. As will be seen in the next chapter, the government encountered some resistance in the finance of the project. However, in the final loan package Citicorp, Lloyds Bank and Banca Comercial Italiana (through SUDAMERIS) all were present as important lenders in the venture.

These are three examples of where there was clear evidence of the parents' foreign currency lending being influenced by concern for business operations in the local economy. It is possible that with more complete information on the decision making of the banks that greater evidence of this nature could be uncovered. Unfortunately, the paucity of published data on specific activities of the banks is a reality that this study had to confront.

The above analysis of the foreign currency lending of banks with business entities in Lima, as sketchy as it may be, leads one to believe that some banks did, in varying ways, alter the general pattern of their behavior to accommodate broader considerations than found in banks without a direct link to the country. But the evidence is far from overwhelming and much less than expected. This may mean that banks are more likely to accommodate their interests in the local market through the local currency lending of their branch or subsidiary; only

limited image making (or gains for the government) seem to be manifest in the foreign currency lending of the parents. Actually, this type of strategy would make sense from the standpoint of the banks since local currency loans to the government would be subject to less risk than those in convertible currencies.

Chapter 7

FOOTNOTES

1. One must remember that gross authorizations of a bank do not necessarily reflect outstanding commitments.
2. In 1975 the assets of American Express International were valued at 2.6 billion dollars, while the parent American Express Corporation had assets close to 9 billion dollars.
3. See Lissakers, p. 58.
4. Bankers do not even see the two superborrowers as a threat, unless they were to default simultaneously, which is a highly unlikely event (see Watson, p. 50). Hardy (p. 191) has pointed out, however, that a default by Brazil might be very damaging to Citicorp.
5. Creditworthiness is a catchall term used to express a bank's assessment of default risk. Generally speaking, a bank's view of creditworthiness is heavily weighted by indicators of a country's external liquidity, i.e., exports, international reserves, etc., and the policies that determine their performance. For more information on how banks assess creditworthiness see Goodman, Asian Finance, Brackenridge, Anderson, and Wolfe.
6. The equal pairing of observations was necessitated by the fact that lending terms were affected by time, i.e., the market environment showed considerable year-to-year flux.
7. Kapur, in aggregated inter-country comparisons, found that banks did not use price to discriminate among developing country borrowers.
8. The terms on this credit conflict with the reporting of the World Bank's Borrowing in International Capital Markets, which sets the maturity at 7 years.
9. See Aronson (1977), p. 177.

10. See Devlin (1979).
11. The standardized variable would be  $Z = \frac{x - \bar{x}}{s}$  where  $x$  is the percentage of a country's loans in a given loan category,  $\bar{x}$  is the unweighted mean for all countries in the loan category and  $s$  is the standard deviation.
12. Data understate somewhat Switzerland's refinance credits because the study's sample does not take account of Swiss participation in the general refinance agreement of 1976.
13. These banks also were the most involved in credits for compensation of nationalized assets. More than anything else, this is an indication of strong links with firms and investors in the home country.
14. As noted in previous chapters, there was no real growth of official finance in the years 1965-1975. For Peru the situation was complicated by the financial boycott.
15. See Wellons (1977), p. 24.
16. It should be noted that U.S. banks had only a limited opportunity to secure their loans with export credit guarantees because from 1968 to mid-1974 the U.S. Export-Import Bank had its doors closed to business with the Government of Peru.
17. See D.L. 18351 in Ley de Bancos.
18. Ibid.
19. Chemical Bank decided to buy into Banco Internacional because of its interest in "going international" and because participation was a convenient way to resolve the failing Peruvian bank's arrears to Chemical. However, the purchase was ill-timed and inept. As pointed out by Kuczynski, problems arose because the purchase was planned precisely at the time when "there was a growing political feeling against foreign control of banks. Still, Chemical went ahead, but without adequately informing the Peruvian authorities until after the event. In the small setting of Lima, this omission caused resentment". The

purchase was the straw that broke the camel's back and provided the necessary political support for the civilian government to introduce (under emergency Law 17044 of June 1968) in August 1968 a law calling for Peruvianization of local banks. The original law called for 66% national ownership (see Kuczynski, pp. 239-243). The military government later raised minimum national ownership to 75% in November 1968 and finally to 80% in 1971.

20. The observations on Citicorp are drawn from Wellons (1978) and Citicorp's annual reports. In 1975 and 1976 Citicorp was the number one lead bank in world syndication. See Chapter 6.
21. Of course, if the bank's loans to Peru led market trends, or enhanced the market's receptiveness towards Peru, this could be an indication of special behavior stemming from the familiarity generated by a local branch bank. There is, however, no indication that Citicorp led market attitudes towards Peru.
22. See Wellons (1978).
23. In 1975-1976 it ranked N° 2 behind Citicorp. See International Herald Tribune.
24. See Wellons (1978).
25. In 1975 Lloyds Bank ranked number 10; Bank of Tokyo did not rank among the top lead banks. See Chapter 6.
26. Ibid.
27. See Wellons (1978).
28. See Wellons (1978).



## Chapter 8

### THE IMPACT OF COMMERCIAL BANK LENDING ON THE ECONOMIC DEVELOPMENT AND POLICY OF PERU

The goal of this Chapter is to switch focus somewhat and evaluate the impact of commercial bank loans on the economic development of Peru. The scope of such an evaluation is potentially overwhelming, so an attempt has been made to restrict the analysis. Basically three areas will be covered. The first section will analyse the role of banks in the finance of projects, the latter of course being one of the more concrete manifestations of the government's development program. The second section will look at the evolution of commercial bank conditionality, which has direct implications for the direction of government policy. The last and final section will take a broader view of bank lending, developing a balance of positive and negative aspects of their involvement in the Peruvian economy.

#### I. IMPACT ON PROJECT DEVELOPMENT

When reviewing the impact of commercial bank lending on Peru, an obvious area of analysis is the impact on project development. Project loans, of course, are a direct link to real activity in the economy and involve investments which have both a present and future impact on growth and development. In the case of Peru, project loans carried more than usual importance given the State's drive after 1968 to expand its role in productive sectors of the economy. Chapter 5 analysed project loans from the standpoint of the banks; this subsection will focus on how commercial bank project finance supported the government's development program.

A. GENERAL

In Chapter 5 it was seen that projects accounted for 5% and 15% of total unguaranteed lending by commercial banks in 1965-1970 and 1971-1976, respectively. If project loans with guarantees of export credit agencies are included there is a significant change only in the latter period, where projects' participation in total lending rises to slightly more than a fifth.

One obvious question about bank support of project development is just where did the resources go. Table 8.1 provides a distribution of bank project lending among different sectors for 1965-1970 and 1971-1976. The table also presents a distribution of major government projects among the same sectors for the period 1968-1975. Since the State's investment program really did not begin in earnest until the 1970's, there is probably a considerable degree of temporal congruence between data for 1968-1975 and the distribution of bank lending in 1971-1976.

Remembering that bank lending for projects in absolute terms was relatively minor in 1965-1970, it is seen that in this timeframe just about three-fourths of all loans went for transport. This, incidentally, also was a priority area of public investment in the 60's. <sup>1/</sup> Projects related to energy were a distant second in terms of importance and mostly involved hydroelectric power systems.

Table 8.1 shows that in the 70's energy projects were of very high priority to the government, accounting for 45% of the total value of major projects. Within the rubric of energy, development of Peru's oil resources stands out as it absorbed more than half the resources dedicated in this area (the remainder basically was for hydroelectric power). It also is seen that within the various sectors of project development, commercial banks channeled 44% of their loans to oil related projects. Thus commercial banks

Table 8.1

PERU: DISTRIBUTION OF COMMERCIAL BANK PROJECT LOANS ACCORDING  
TO SECTOR, 1965-1970 AND 1971-1976<sup>a/</sup>  
(percent of total)

	Distribution of project loans extended by commercial banks		Distribution of all major public sector project <sup>b/</sup>
	1965-1970	1971-1976	1968-1975
Agriculture	3.0	3.2	17.7
Fishing	-	-	1.7
Mining	-	11.8	6.4
Manufacturing	6.0	20.5	15.8
Energy	10.2	46.5	45.3
(oil)	(-)	(43.6)	(26.2)
Water Sanitation	4.8	5.8	3.5
Transport	73.8	0.1	7.0
Communications	2.3	-	2.6
Services	-	12.2	0.1
(health)	-	(12.2)	(-)
(education)	-	-	(-)
Other	-	-	-
<u>Total</u>	<u>100</u>	<u>100</u>	<u>100</u>

Sources: Bank loans: CEPAL, on the basis of official data; public sector projects: derived from data in the Ministry of Finance, La Situación Económica-Financiera del País, 12 February 1976, table 9.

<sup>a/</sup> Credits with and without guarantees of export credit agencies.

<sup>b/</sup> Major projects only; accounts for about 40% of all public sector investment for the period, incorporating both local and foreign costs.

clearly gave more than proportional support to this national endeavor.

After energy, the second most important area of public sector projects was agriculture. Investments involved big and costly irrigation systems in Chira-Piura, Majes and Tinajones, which were designed to improve the productivity and well-being of families in coastal farming regions. Banks, however, were not much involved in these investments as only 3% of commercial bank project lending went into support of this type of activity.

Following agriculture, the next most important sector for government projects was manufacturing, which accounted for 16% of the value of major state investments. As was seen in Chapter 3, the government had a conscious policy to invest in productive activities that had been dominated by private (and especially foreign private) capital. Thus state activities in this sector were perhaps the best manifestation of the reorientation of government development policy after 1968. And it is seen that banks gave relatively strong support to the effort as more than 20% of all their lending went to manufacturing ventures, making it the second most important area of bank finance for projects.

Another area of importance for bank project lending was mining, where roughly 12% of the loans flowed. In terms of the government's major projects, mining accounted for 6% of the total value of investments. The copper project Cerro Verde I and II dominated activities in this area.

Also of significance with regard to bank finance of projects was health services. It too accounted for 12% of bank project finance. The projects mostly involved construction of hospitals. The relatively high profile of banks in this type of finance is surprising given that ventures in health services might be considered wholly uncommercial in nature.

Overall, the data would suggest that the banks were highly supportive of the government's investment program. With the exception of agriculture and hydroelectric power, bank finance flowed to projects of clear national priority. In relative terms, a considerable amount of finance even went to social services which are not usually considered to be an attractive area for commercial banks.

Another question about the project loans of the banks involves just what was financed. An attempt has been made to roughly estimate this by reviewing the nature of the projects financed and gathering official information on ex-ante (and to a lesser degree ex-post) plans on the sources and uses of project funds. By their very character, the resulting estimates are extremely tentative and can be used in an indicative way only. The data themselves appear in table 8.2.

The table shows that in 1965-1970, when project loans by banks were not very important in absolute terms or relative to all commercial lending, that a very high percentage of total funds (76%) went to local cost finance. In 1971-1976, when project loans indeed were of some magnitude, at least 26% of all lending was for local costs, and considerably more is likely given an unidentified element of local cost finance in 27% of the value of project loans.

From at least one standpoint, the relatively high percentage of local cost finance was very favorable to Peru. Such finance freed local government resources for other domestic uses, thereby expanding the investment capacity of the government and adding overall flexibility to the development program. Local cost finance also could be used as back door balance of payments assistance. Additionally, such finance permitted the government to promote domestic sourcing of supplies and manpower. On the other hand, financing local costs with foreign currencies enhanced the risks of difficulty in transformation of resources for debt service, thereby placing greater responsibility on the shoulders of public economic managers.

Table 8.2

PERU: DISTRIBUTION OF COMMERCIAL BANK LOANS ACCORDING TO  
WHETHER FOR COVERAGE OF FOREIGN OR LOCAL COSTS<sup>a/</sup>

(Percent)

	1965-1970	1971-1976
1) Goods and services with some local costs involved	76.0	52.5
(identified as all local costs)	(76.0)	(25.6)
(identified as containing an unspecified element of local costs)	(-)	(26.9)
2) Goods and services exclusively with foreign costs	23.2	43.3
3) Unspecified	0.8	4.2
4) <u>Total</u>	<u>100</u>	<u>100</u>

Source: CEPAL, on the basis of official data.

a/ For credits with and without export credit guarantees. Data are rough estimates and should be used with caution.

The lending behaviour also shows that banks were just not a conduit of business for foreign suppliers of goods and services. The high percentage of local cost finance in project loans means that support for foreign suppliers may not have been the overwhelming consideration in decisions to finance projects; that banks, especially in the 70's, were interested in business for its own sake and that willingness to finance local costs was an easy and convenient way to encourage governments to expand their reliance on foreign commercial bankers in the 1970's.

#### B. EXAMINING THE ROLE OF BANKS IN PROJECT FINANCE

In reviewing the nature of commercial bank finance of projects, no mention has been made of the precise role of these institutions in support of investment programs. Do banks support whole projects or do they play some other role in overall finance?

In order to see how bankers view their role in projects, it is useful to quote an observation made by a high official of one major global bank:

"When banks directly contribute to financing a project it is with loans that complement institutional and export agency credits and augment domestic financing of construction costs. In this regard ... (banks) ... are risk takers in the more classical sense of banking. But ... (bank) ... loans are not long term support. They are not speculative'... (banks) ... expect to be repaid on the strength of the cash flow, but before long term lenders are repaid, and certainly before co-venturers reduce their 'risk' capital or support" 2/

The same individual went on to describe the banks' loans as being one of the many "layers" of financing derived from a number of private and official sources. 3/

Given the general impression that international commercial banks have had a dominant position in LDC finance in the 1970's, this is an important clarification. It clearly states that banks do not have a primary role

in project finance, but rather are only a supportive element in a larger overall resource package. Unfortunately, there has been little empirical evidence to support this observation, or any other for that matter, leaving quite vague the precise position of these institutions in the direct investment activities of LDCs. Thus, in the course of this study research was undertaken to construct a more complete picture of how Peruvian projects were financed from abroad. Of interest was the role of banks vis-a-vis other financial institutions both with regard to the amounts and terms of lending, plus the relation of all institutions to suppliers. Information of this nature on a selected number of public sector projects, of varying degrees of size and importance, is presented in table A8.1 of the statistical appendix.

A summary of the relative importance of banks in the 13 selected projects is presented in table 8.3. It is seen that their participation varied greatly from a low of 1% of total foreign finance, to a high of 100% of total finance. However, if one considers credits guaranteed by home country export credit agencies to actually be government loans, then the aforementioned observation that commercial banks are only 1 layer of a multi-layered financial package would appear to be accurate. Leaving aside very small projects, the only project in which banks had a very large unsecured participation was N° 10 — the Cerro Verde copper mine—and this was roughly 40% of the total foreign resource package. Otherwise commercial bank participation was a fifth or less, with the remainder being covered by some combination of foreign suppliers, governments, multilateral agencies, etc.

The observation that banks are just medium term suppliers of project finance already has been confirmed in Chapter 5; as was seen in table 5.12 unguaranteed project loans had an average maturity of only 6.9 years in the period 1971-1976. When guaranteed bank credits are incorporated, the average



Table 8.3

PERU: RELATIVE IMPORTANCE OF BANKS AS FOREIGN FINANCIERS OF  
SELECTED PUBLIC SECTOR PROJECTS, 1972-1977

Projects	Total value of foreign loans (millions of dollars or equivalent)	Distribution of loans (%)							Total
		Commercial banks			Suppliers	Government	Multilateral	Other	
		Guaran- teed <sup>a/</sup>	Unguaran- teed <sup>a/</sup>	Total					
No 1	2.8	-	100	-	-	-	-	-	100
No 2	2.8	64.3	-	64.3	14.3	21.4	-	-	100
No 3	1.2	-	100	100	-	-	-	-	100
No 4	3.8	34.2	-	34.2	65.8	-	-	-	100
No 5	42.0	31.9	-	31.9	53.1	-	-	15.0	100
No 6	29.5	10.5	15.3	25.8	-	74.2	-	-	100
No 7	742.1 <sup>b/</sup>	1.6	22.3	23.9	30.7	34.1 <sup>c/</sup>	2.8	8.5	100
No 8	28.6	36.4	18.2	54.6	3.1	42.3	-	-	100
No 9	3.2	84.4	15.6	100	-	-	-	-	100
No 10	72.3	30.0	40.4	70.4	-	29.6	-	-	100
No 11	26.5	100	-	100	-	-	-	-	100
No 12	271.4	-	1.2	1.2	98.8	-	-	-	100
No 13	73.9 <sup>d/</sup>	0.7	6.1	6.8	87.8	5.4	-	-	100

Source: Table A8.1 of the statistical appendix.

<sup>a/</sup> Guaranteed credits are those with the support of home country export credit agencies.

<sup>b/</sup> Excludes loans for 0.6 million and 59 million D'marks.

<sup>c/</sup> Includes loan with unidentified participation of suppliers.

<sup>d/</sup> Excludes a bilateral loan for 5 million Finnish marks.

maturity rises only to slightly above 7 years. A casual look at table A.8.1 of the statistical appendix, however, might suggest that the effect of the relatively short bank maturities were assuaged by longer maturities on suppliers' credits and official loans. But in fact, as was seen in figure 4.3 of Chapter 4, in the 1970's only multilateral agencies consistently offered maturities that were very much longer than those on commercial bank credits; and these latter agencies had the absolute value of their credit to Peru limited by political and institutional constraints. Thus one suspects that projects with the participation of commercial banks had a less of a layered appearance with regard to maturities than they did with regard to the amounts financed by individual institutions. Although a more detailed study on project loans would be required in order to arrive at firm conclusions in this area, one can be concerned about the fact that average maturities on projects had a more of a medium term than long term character. This has adverse implications for broad-based project development and servicing of the foreign debt because the process of development is normally associated with activities that can have, for numerous reasons, long gestation periods.

#### C. THE OIL PIPELINE

Before closing the subsection on projects, it is worthwhile to comment on the role of banks in the transandean oil pipeline, which was one of the most important projects, and surely the most costly one, programmed by the government.

The transandean pipeline clearly was of the highest national priority. From the very early part of the 1970's there were expectations of considerable reserves of petroleum in the Amazon, which could be used to cover Peru's growing oil deficit and provide abundant export revenue. This in turn would

permit Peru to finance its development and cover external obligations. The problem was how to bring the crude to market.

One possible way would have been to barge the petroleum down the Amazon river through Brazil to the east coast. The petroleum could then be sold to Brazil or exported to third markets, using a fraction of these export receipts to purchase other petroleum to cover Peru's domestic needs which were not being met by land and offshore wells on the coast. The attraction of such an approach was its relatively minimal cost. However, aside from important strategic considerations, the plan was deemed impractical because of changing water levels on jungle tributaries which could have inhibited a steady volume of shipments via river barges. Thus, this option was discarded at an early stage in favor of the more costly oil pipeline.

The government moved ahead quickly with the program. By early 1973 it already had commissioned and received a feasibility study recommending a 850 kilometer pipeline between the jungle and the Bayovar port on the north coast of Peru. The pipeline would have a nominal capacity of 200,000 barrels a day, which could be sharply increased through the installation of additional pumping capacity. The initial estimate of cost was 350 million dollars and the construction time was estimated at 2 years.

Moving ahead so quickly with the project clearly was a calculated risk since at the time there was no firm idea about the magnitude of the reserves in the jungle. But as was seen in Chapter 3, the initial finds were very encouraging and the euphoria high, placing considerable momentum behind the project.

By early 1974 the government was intensively seeking to finance the oil pipeline. However, it encountered a less than enthusiastic reception. Costs were escalating sharply (to over 500 million dollars) and some doubted the quality of reports filed by 2 independent oil consultants confirming that the

proven reserves in the jungle were at a level sufficient to justify the massive pipeline venture. 4/ Peruvian authorities were politely turned away from many sources of finance, including those of a bilateral and multilateral type. However, through tenacity and the tapping of many different institutions, the pipeline was financed. Ultimately the government had to secure nearly 800 million dollars in foreign credit for the rapidly escalating costs of the project; in effect, the foreign loans on this one project were equivalent to nearly a fifth of the public sector's foreign debt at the end of 1976.

Table A8.1 in the appendix displays the myriad of foreign loans secured to cover foreign and domestic costs. It can be seen that the largest part of the finance came from the Japanese Government, which was especially concerned about securing petroleum. The problem of the debatable level of reserves was unimportant to Japan; it was to have claim on an assured portion of the crude coming through the pipeline as part of the agreement for repayment of the loans. 5/ Thus, for this lender, whether total reserves were sufficient to justify the pipeline or not was irrelevant; the only question of importance was that it could be confirmed that there was enough oil for sale to repay the credit.

From the standpoint of the study, it is notable that an important source of funds was private commercial banks, which extended over 150 million dollars in unprotected credits, equivalent to roughly one fifth of the total financial package.

The two syndicated credits by Wells Fargo were rather special transactions. Apparently in an attempt to fill a financial gap, authorities approached the government of Iran for special assistance. Iran agreed, but on the condition that commercial banks would act as intermediaries on the credit. Thus the Iranian government deposited 100 million dollars in an array of banks which in turn were organized into two separate syndicates under the leadership of Wells Fargo. The basic characteristics of these two syndicates are found in table 8.4.

Table 8.4

PERU: MAJOR COMMERCIAL BANK SYNDICATES FOR FINANCE OF THE TRANSANDIAN OIL PIPELINE, 1975

	Syndicate No 1	Syndicate No 2	Syndicate No 3
1. General			
Amount (millions of dollars)	50.0	50.0	24.4
Interest rate	1.75+Libor	1.75+Libor	2.0+Libor
Maturity	7 years	7 years	5 years
Flat fees	1.0%	1.0%	0.5%
2. Number of banks	22	18	4
3. A g. Int Rank of banks <u>a/</u>	76	27	14
4. Agent (names and percentage of credit extended)	Wells Fargo <u>b/</u> (2.0%)	Wells Fargo <u>b/</u> (2.0%)	Dresdner Bank <u>b/</u> (41.8%)
5. Managers (names and percentage of credit extended)	Iran Overseas Investment Bank <u>c/</u> (3.0%)	Long Term Credit Bank of Japan (12.0%)  Iran Overseas Investment Bank <u>c/</u> (2.0%)	Deutsche Bank (41.8%)
6. Participants (percentage of credit extended)			
United States	13.0%	14.0%	-
Japan	-	38.0%	-
Canada	4.0%	4.0%	-
United Kingdom	22.0%	10.0%	-
Germany	14.0%	6.0%	8.2%
France	4.0%	-	-
Italy	8.0%	-	-
Switzerland	-	-	-
Consortium	-	-	-
Other	30.0%	12.0%	8.2%

Sources: CEPAL, on the basis of official data; footnote (c) is from the Banker Research Unit, Who Owns What in World Banking 1977-1978, London, 1977.

a/ On a scale of 1-300 in world banking for the year 1975. See footnote c of table 5.3.

b/ Also manager.

c/ A consortium bank owned jointly by: Barclays Bank (6.25%); Bank Melli Iran (25%); Bank of America (6.25%); Bank of Tokyo (6.25%); Deutsche Bank (6.25%); Industrial Bank of Japan (6.25%); Industrial and Mining Development Bank of Iran (25.0%); Manufacturers Hanover (6.25%); Midland Bank Ltd. (6.25%); and Societe General, Paris (6.25%).

It is seen that in the two general credits Wells Fargo committed very little of its own resources, while enjoying the benefits of agent and management fees. With regard to the participants, the greatest contributions came from Japanese and "other" banks. 6/ This latter group is interesting because it was made up of a significant number of banks not in the mainstream of international finance (e.g. Banco Urquijo, Banco Atlántico, Bank Melli Iran, to mention a few). Reflecting the fact that the Iranian resources came through commercial intermediaries, the interest rate was steep at 1.75 points over the libor. The only basic condition for the loan was reports from 2 independent firms of petroleum consultants confirming the existence of sufficient oil to justify the pipeline.

The other major syndicated credit was headed by Dresdner Bank. It involved 4 institutions, but as seen in table 8.4 for practical purposes it was a two bank credit involving Dresdner and Deutsche Bank. The resources were destined to be used for purchase of pipes from a German supplier. The terms of the credit were by no means easy, with an interest spread of 2.0 over libor and a short maturity of 5 years.

Referring to table A.8.1 of the appendix one sees that the other banks with unsecured transactions were Citicorp and Crocker National Bank, the former, of course, having a branch facility in Lima.

It is clear, then, that banks played a key role in the finance of the pipeline, a project of high national priority. In particular, the loans are another example of the importance of Wells Fargo, Dresdner, Citibank and even Crocker National Bank to the government of Peru. The fact that little support for the project could be secured from official lenders underlies the flexibility of commercial banks and the key role that they played in the national development program. But there clearly was a cost for this flexibility, as measured in the relatively onerous interest spreads and short maturities of the credit. Also, the costs proved to be more burdensome than anticipated since petroleum output fell short of expectations, causing the pipeline to operate, at least initially, at only half of rated capacity.

## II. CONDITIONALITY: HOW IT EVOLVED OVER 1965-1976

When bankers extend credit to governments they naturally seek protection against losses. One can see two general forms of security.

One type is a direct form of security. This is done by requiring collateral from a borrower, e.g. holding in escrow a part of the receipts of a state enterprise, or even seeking a pledge of part of a country's gold reserves.

Other forms of security are indirect in the sense that they focus on the general repayment capacity of the government. One type of indirect security which has become almost standard in loan contracts is a pledge from the government to provide its "full faith and credit" to a transaction. This is a kind of global guarantee that a sovereign state will ensure repayment, even if an individual public sector entity is incapable of servicing a loan. Banks can further increase indirect security by adding positive or negative covenants directed to the individual borrower or the general state. These latter covenants often are not specific to the credit itself but rather influence policy parameters that actually affect the state's general capacity to service debt.

Indirect security that places restrictions on policy parameters can be termed as political-economic conditionality. Conditionality of this nature is particularly disagreeable to government officials because it represents an effective interference in the domestic policies of a sovereign state. In other words, its impact is generally not viewed upon as being favorable. For this reason most governments will attempt to avoid such conditionality and will submit to it only under duress, i.e. when there are no acceptable alternatives.

Direct security arrangements such as collateral may be viewed as commercial conditionality. This can be more palatable to governments because it has a rather limited impact on global decision-making. In some instances, commercial conditionality may be viewed with favor by central government authorities when it is placed on financially weak state entities; by escrowing resources, greater discipline is placed on the borrower, thereby reducing pressure on the central government which ultimately must guarantee the credit. Nevertheless, many government borrowers

probably would prefer to avoid collateral arrangements inasmuch as they reduce the maneuverability of assets.

As far as general guarantees are concerned, they are surely the most attractive from the standpoint of the borrower. When decentralized agencies are the borrower of record, many governments attempt to limit the guarantee to the agency itself. But in practice bankers usually insist on a general guarantee of the republic.

This section will be basically concerned about political economic conditionality imposed by commercial banks because this clearly has an impact on the direction of the economy. However, when dealing with governments, there often is a fine line between political-economic conditionality and commercial conditionality, with many gray areas where the two overlap. Analysis therefore also will deal with cases of collateral arrangements. Thus the reader should consider the following analysis to be an examination of protective conditions that place restraint on the actions of state borrowers. The review will be selective, focusing on those forms of conditionality that are perceived to have been the most influential on government actions. And for the sake of convenience, the review will follow a format involving three separate periods: 1965-1971, 1972-1975, and 1976.

#### A. CONDITIONALITY: ITS APPLICATION DURING THE PERIOD 1965-1971

The 1960's could be characterized as a period when bankers were highly conditional lenders to the government of Peru (and probably LDC governments in general). In addition to requiring general government guarantees, conditionality of a commercial, and of political-economic nature, was most common. Commercial conditionality was a common practice on loans to decentralized government agencies, while political-economic conditionality became commonplace when loans to the central government were obviously for the purpose of aiding weak fiscal and balance of payments situations.



1. Commercial conditionality

With regard to commercial conditionality, it was applied frequently in the 60's, especially with regard to loans to entities other than the central government. This type of conditionality always was in addition to a guarantee from the Republic of Peru. While it would be impractical to analyse every case of commercial conditionality individually, setting forth a couple of examples can be illustrative of how this type of protection was employed in the 1960's.

One interesting case involved a local government, which received the backing of a central government guarantee. The local entity had to secure a large foreign loan with its tax receipts. The arrangement required it to deposit in a special account at a local bank all receipts from a property tax until a balance was accumulated to the extent of 1 1/2 times the value of the next interest and amortization quota. If tax receipts were insufficient to generate the required balance, additional funds were to be taken from the public works budget of the government. And if this proved inadequate, the central government had to deposit funds sufficient to meet the required balance. The central government also had to guarantee access to dollars for repayment.

A second example of commercial conditionality involves a 5 million dollar loan to a State steel enterprise. The lending bank required that the corporation apply to repayment of the loan the unencumbered part of U.S. dollar royalty payments paid to it by Marcona Mines for exploitation of local iron ore deposits. The Central Bank was to hold these royalty payments in a special account and in amounts sufficient to meet annual interest and amortization payments.

The above examples are representative of the techniques employed by commercial banks when lending to state enterprises in the mid and late 60's. What is significant to note is that arrangements of this kind provided considerable nominal protection for the banks. Not only did they have central government guarantees of access to the general resources of the state for the purpose of debt service, but at the micro-level there often were a series of collateral measures designed to escrow resources. This was truly a very cautious lending policy on the part of the banks and undoubtedly provided for considerable psychological security. Whether such precautions over and above a general guarantee were effective is another matter; in general loans with collateral arrangements did not escape the need for repeated refinance, suggesting that in the end the real source of repayment was the general capacity of the government to service its foreign debt.

## 2. Political-economic conditionality

Political-economic conditionality on commercial bank loans began to appear in 1967, which more or less coincided with the open deterioration of the internal and external economic accounts. Prior to this year, the only tinge of this type of conditionality was a rather common requirement found in loan agreements that Peru be a member of the IMF. But then again, prior to this year bank lending to the government was very modest. Between 1965-1966 only one relatively large loan was arranged—40 million dollars—and most of the receipts were designed to refinance an earlier credit of 1964.

The intensity with which conditionality was applied was progressive.

The conditionality of 1967 appeared on a relatively large general purpose loan extended by a group of banks to the central government. At the time of the bank loan Peru was negotiating with the IMF for a new 42.5 million dollar

standby agreement for the period August 1967-1968. In general terms the banks conditioned their loan to Peru by the need to reach an agreement with the IMF and stipulated that Peru "use its best efforts" to comply with the terms and conditions of such a standby accord. Under the general framework of tying the loan to the IMF standby credit, some of the more specific requirements were that:

- (i) The government limit to a "maximum extent" the foreign borrowing of the Central Bank and State banks for the purpose of budget or balance of payments assistance;
- (ii) new loans—other than ordinary commercial transactions—have a minimum maturity of 5 years, with 2 years grace; and
- (iii) indebtedness of the Central Bank and State Banks with a maturity of less than 5 years be limited to not more than 100 million dollars at any time outstanding (excluding IMF credits and increases in lines of credit to meet seasonal requirements of productive activities).

The banks also required the government to provide them with copies of the IMF standby agreement and country reports. A copy of a 15 million dollar loan being negotiated with U.S. AID also was to be delivered to the banks. If Peru did not successfully negotiate a loan with the IMF, or its actions made it ineligible to receive IMF support, the banks had the option to revoke or call the loan.

How did the commercial banks' conditionality compare with the conditionality associated with the IMF agreement? While the scope of the conditionality applied by the Fund was much broader than that demanded by the banks, it is interesting to note that there were nearly identical restrictions with regard to conditions on debt contraction. According to the Fund Peru was to limit public sector borrowing abroad to loans with a maturity of at least 5 years, and in the case of suppliers' credits, to loans with a maturity of at least 10 years. And the banks' limit on borrowing mirrored the Fund's

restriction of 100 million dollars for outstanding loans with maturities of less than 5 years. Thus the banks were clearly following the Fund's lead in establishing conditions on their credit.

In 1968 political-economic conditionality on commercial bank loans became more generalized. By now the government was trying to refinance all the debt it could. This was being done in conjunction with negotiation of a new 75 million dollar standby agreement with the IMF for a 1-year period beginning in late August 1968. Moreover, since the banks' generally refused to go beyond 5 years on their refinance—leaving the early 70's with prospects of a very burdensome debt service—the civilian government also was seeking to negotiate a "standby agreement" with banks that would permit it to draw down funds pari-passu with the credit from the IMF. In fact just before the change in government in October 1968 an agreement was reached, providing for \$65 million from 11 North American banks and \$25 million from 33 European banks, that could be drawn down through June 1971. But the credit never came to fruition as no use of the funds was ever made. 2/

What is significant is that just about all commercial credits effected in 1968 carried some form of political-economic conditionality, most of which revolved around the IMF standby credit and the anticipated "standby" to be provided by commercial banks. While the individual and specific terms of the conditions attached to credits varied according to the numerous lending institutions, there was a commonality to conditionality, the sense of which can be summarized as follows:

- (i) that the government would maintain in effect (i.e. renew) its standby agreement with the IMF and do nothing to prevent the Central Bank from complying with the terms and conditions of the IMF accord;
- (ii) that the Central Bank would arrange the aforementioned standby credits from its major bankers on terms and conditions that would be roughly comparable for all institutions;

- (iii) that the Central Bank in 1968-1969 use its best efforts not to assume new debt in excess of that stipulated by the banks in their standby credits 8/
- (iv) that after such standby agreement with commercial banks shall have expired, the government use its best efforts to restrict foreign indebtedness (on a few occasions it actually was stipulated that debt at any time outstanding during any calander year shall not exceed an amount equivalent to one-sixth of the aggregate value of Peru's exports during the preceeding calander year); and
- (v) that the banks will receive periodic reports from the Central Bank on the country's external debt.

As far as the IMF agreement which underpinned commercial bank credits, it virtually stopped the contraction of new debt with maturities of more than 180 days and less than 10 years and placed severe limits on new debt with maturities between 10 and 15 years. There were no limits placed on debt with a maturity up to 180 days or more than 15 years.

Thus, the banks, in tying their refinance accords to the IMF agreement, essentially received the protection of the tough debt limits plus the broader macro-economic policy restrictions that come with later tranche IMF standby credits. By doing this they operated under the IMF umbrella, yet could avoid direct responsibility for the measures themselves. The banks also had foresight as they established their own debt limits in the event of the expiration of the standby agreements.

Up to mid-1969 the banks could benefit from the buffer of the IMF accords. But by this time the August 1968 IMF standby agreement had expired and the government had decided not to seek a new standby accord. Thus bankers now

were more or less on their own in handling Peru's debt service problems. Fortunately for them, the fiscal and balance of payments measures taken in 1968, coupled with the followup stabilization efforts of the new government, helped to considerably assuage financial difficulties.

Notwithstanding the expired IMF accord, the commercial banks continued to refinance and restructure upcoming payments due to them, perhaps in part because the government threatened non-payment if acceptable refinance agreements were not reached. But what is of interest here is that bankers continued to apply their own conditionality to the credits.

Efforts to restructure and refinance debt in 1969-1970 were successful. However, banks, working together, placed precise limits on the contraction of debt with maturities in excess of 18 months for the period 1970-1975. The construction of the limits was different than earlier practices which mirrored the IMF guidelines; instead of placing ceilings on outstanding indebtedness, annual limits were placed on aggregate payments of interest and principal on foreign debt related to loans with maturities of 18 months or more. Unfortunately it was not possible to establish the magnitude of the limits themselves. <sup>9/</sup> As for loans with a maturity of less than 18 months, no limits were established, except with regard to the Banco de la Nacion where lines of credit were restricted; in addition, Peru had to remain a member of the IMF; provide the banks with copies of the country reports from international organizations, and ensure that all terms on bank refinance agreements were not more favorable to one bank than another.

In 1971 Peru's traditional banks again agreed to restructure and refinance payments. In doing so they amended their earlier conditionality. Again debt limits focussed on service payments rather than on outstanding indebtedness. The period of restriction was 1972-1976 and the limits were 220 million dollars per annum

for the first two years and 200 million dollars per annum thereafter. Limits did not apply to short term lines of credit to the State Development Banks, but the Banco de La Nacion did have an absolute limit on its lines of short term credit. In addition to the above, the banks required Peru to maintain "a substantial" portion of its reserves on deposit at their offices.

There is no doubt that this conditionality was severe. By returning to the table on debt service in Chapter 3, one can see that Peru at this time already was near the established limits, making significant new debt contraction dependent on very long grace periods that would allow the government to postpone service payments until after the restricted period. But such long periods of grace were not common, which meant that the conditionality effectively placed absolute constraints on the government's foreign debt contraction. The severity of the restrictions can be even better appreciated if one remembers that the government had plans to embark on a massive investment program which would involve the need for external support.

What the above has shown is that up through 1971 banks were very aggressive in the establishment of political-economic conditionality that affected the management of the Peruvian economy. When the IMF was monitoring standby arrangements, the commercial banks smartly came under the Fund's wing and established formal links between their loans and the IMF Credits. And maintenance of the commercial credit agreements was dependent upon satisfactory compliance with the Fund's program. Frequently the banks would establish their own debt limits, which were not unsimilar to those stipulated by the IMF.

Interestingly, the commercial banks persisted in applying conditionality even when the Fund's protection was not available to them. This was clearly a more risky type of venture. But there is evidence that traditional commercial lenders were up to the challenge as their loans placed severe short and medium term limitations on the government's ability to contract foreign debt. This in turn placed a clear restraint on the government's desire to pursue its ambitious development objectives.

## B. CONDITIONALITY: AS IT WAS APPLIED DURING 1972-1975

Peru entered 1972 with successful refinance accords with its bankers. However, there was conditionality attached to these agreements and this restrained government policy-making ability, especially with regard to debt contraction for the investment program. But there was no choice but to heed these conditions; with the principal sources of bilateral and multilateral loans cutoff as a result of a financial boycott, Peru's traditional bankers were the only real potential source of new finance. Thus, while the government negotiated toughly with the banks, it had little choice but to accept their conditions and comply with their requirements, hoping that somehow the banks would become more flexible and provide new finance for the government's development program.

As it turned out, the structural changes being undergone in world banking, which were analyzed in Chapter 4, were making LDCs ever more attractive clients for commercial banks. In 1972, aided by publicity about petroleum in the Amazon, Peru began to enjoy some of the fruits of the changes in the world financial market.

As has been seen in earlier Chapters, prior to 1972 Peru's banking activities were dominated by a handful of traditional lenders. But by 1972 many non-traditional lenders were showing willingness to extend credit to the government. These banks—e.g., U.S. regional banks, Japanese banks, etc.—were relative newcomers to international finance and were actively seeking to expand their portfolios abroad. As a reflection of their interest in <sup>into</sup> breaking/new markets, they offered finance to Peru with no conditions whatsoever. As more banks attempted to penetrate Peru, competition increased further. By late 1972 and into 1973 there were enough offers of unconditioned credit for Peru to break the hold of its traditional banks by liquidating in full their



earlier loans that were laden with conditionality. The liquidation of the agreements unshackled government policy with regard to debt contraction. Moreover, traditional banks, in order to protect their market position, had to follow trends and provide unconditional finance as well. 10/

With the wave of bank lending to LDCs in the 1970's, not only was political-economic conditionality abandoned, but so too was commercial conditionality. Banks, in order gain the favor of governments, found general government guarantees to be adequate security. The nature of finance was of little import. If a bank was inclined to seek commercial security, or question the use of funds, it realized that there would be other institutions more than willing to provide no-questions-asked finance, thereby undercutting the banks competitive position with the government. Thus, in the 1970's banks usually paid little attention to the use of funds or special security arrangements; the only condition for finance was the sovereign government guarantee, the value of which many banks were unwilling or unable to assess. 11/ A good example of the relative freedom from conditionality was the bank finance of the oil pipeline. Despite a generally more conservative lending environment in the international market in 1975, the only requirement that the banks made for support of the project was two studies on proven petroleum reserves in the jungle. This was in contrast to official lenders and suppliers from Japan who secured their loans by putting claims on the petroleum itself.

#### C. CONDITIONALITY RETURNS IN 1976

The freedom from conditionality in 1972-1975 was a radical break with the past. Throughout the early 1970's the commercial banks unquestionably supported the Peruvian economy, even in the face of severe structural weaknesses in public finance and the balance of payments. This environment provided Peru with unprecedented opportunities for national self-determination. Moreover, the

banks extreme flexibility (some say irresponsibility) during the period contrasted sharply with the traditionally conditioned finance of official institutions. Unfortunately, the carte blanche provided by banks was withdrawn in 1976. One factor behind the change in attitude was external to Peru, i. e., that banks by now were generally very cautious lenders to LDCs. The important bank failures in mid and late 1974 raised serious doubts about the viability of current management practices in international banking. In addition, public officials, especially in the U. S., had been strongly criticizing banks for having imprudently over lent to LDCs. Reflecting the tense environment, many of the so-called newcomers to international lending had withdrawn from active participation in the market, giving the big, traditionally international, banks increased leverage over the patterns of global lending. The other important factor behind the changed attitude was intrinsic to Peru. The structural weaknesses in the Peruvian economy had been progressively intensifying over the years and so had the requirements for external support. With much less brilliant prospects for petroleum in the jungle, and Peru's financial requirements accelerating, the country's private creditors panicked. Peru could no longer count on its bankers for unconditional support.

Even with the economic package of corrective measures that Peruvian authorities introduced in January 1976, it was soon clear that further steps would soon have to be taken. The balance of payments gap was large and the banks were not extending new loans at the same pace as in previous years. Something had to be done.

From the very beginning authorities ruled out a standby accord with the IMF. This institution had long had the reputation among developing countries (and in many other circles) of being a harsh and overbearing entity that imposed inappropriate and socially costly stabilization programs on governments. 12/

Peru was no exception. Indeed, in Peru the distaste for the Fund was probably greater than average given this institution's open bias in favor of national and foreign private capital, which, of course, was quite distinct from the government's general philosophy. Reflecting this difference, since the expiration of the standby agreement of mid-1968, the government had been careful to limit its use of Fund facilities to those of nominal conditionality, i. e., the gold tranche, compensatory credits for short-falls in export receipts and the special Oil Facility established after the unprecedented OPEC price increase in late 1973.

Seeking needed finance in the Spring of 1976 Peruvian officials made informal contacts with U. S. banks in New York. Initial efforts were focussed on U. S. banks not only because they were the government's main creditors, but also because U. S. banks were leaders of the international market and their blessing was needed for any assistance from the world banking community. Meetings were organized by Manufacturers Hanover Trust, which had long and close relations with both the private and public sectors of Peru. Others participating in the meeting were Bank of America, Citicorp, Wells Fargo, Chase Manhattan and Morgan Guaranty—all, with the exception of Morgan, classified earlier as major lenders to the government in the 1970's.

The bankers were informed that without loans of some 350 to 400 million dollars Peru would be unable to meet its obligations. The bankers were not very enthusiastic about the request, especially when they found out that Peru was unwilling to undergo an IMF stabilization program. In the meetings the Peruvians confronted a general unwillingness among the bankers to extend any new credit without general IMF supervision of the economy.

During the course of events, the government was preparing its own stabilization program. Whether this program was developed at the initiative of the Peruvians, or was a response to the demands of the banks for Peru to

"get its house in order" has been a matter of debate. But causal factors would be difficult to untangle. Peru was facing a growing external gap that clearly required comprehensive policy measures. Something had to be done regardless of the opinions of the banks. Moreover, a government formulated stabilization program was a logical bargaining tool to help convince creditors to provide financial support in the absence of a program with the IMF.

The Peruvian-designed stabilization program was initiated in mid-year. The basic measures taken are reproduced in the appendices. As can be seen, among the measures taken were a 44% devaluation, cutbacks in fiscal expenditures, new taxes, adjustment of interest rates, etc. Generally speaking the program was very comprehensive. But whether the terms and conditions of the program were as stern as an IMF program is problematical since the Fund's accords are the outcome of bilateral negotiations. What is important is that the Peruvian program was presented to the banks as being equivalent to the traditional IMF adjustment policies. 13/

Both during the preparation and implementation of the national stabilization program the U.S. banks remained highly reluctant to extend loans without the buffer provided by the IMF. Peru was not the only one of their LDC borrowers encountering problems and there was a fear that attending to Peru's request would set a bad precedent. Also the banks were concerned about the political implications of providing direct support to the government's program. Then there was a problem of how to evaluate the program and what to do if it failed.

Notwithstanding these general reservations, as negotiations proceeded U.S. banks split into two camps. One group of major banks became advocates and decided that support of the program was the only way to keep Peru afloat. Another smaller group remained as adversaries—among them were reportedly Morgan Guaranty and Continental Illinois.

The adversaries, while not wanting to participate in a joint credit, did offer the Peruvians short rollovers of the upcoming payments due to them. However the Peruvian authorities rejected this proposal as being inconsistent with their medium term stabilization program. 14/ Thus the adversaries were faced with a dilemma. The advocates were unwilling to cover the adversaries claims on Peru; to do so would effectively have been a subsidy for this latter group of banks. It was clear, then, that if the adversaries rejected participation in a general refinance credit the whole rescue mission would be aborted. This in turn would ensure default. Thus these considerations, coupled with strong peer pressure, brought most major adversaries into the fold. 15/

With most important U.S. creditors more or less in agreement in principal to support the Peruvian program, in July other creditors were brought into the negotiations. In order to coordinate the bankers position a Steering Committee was organized. Citibank represented the U.S. banks, Dresdner Bank the Europeans, Bank of Nova Scotia the Canadians and Bank of Tokyo headed the Japanese Banks. Swiss Bank coordinated Swiss creditors, who negotiated outside the global agreement.

The negotiations focussed on whether all the banks should support the program in the absence of the IMF, and, if so, what would be the modus operandi for supporting and evaluating the program. Also at issue was the distribution of credit among the banks as well as the terms and conditions of that credit.

With regard to the distribution of the refinance credits, it was envisioned that it would be as follows: the United States, \$240 million; Europe \$120 million; and Canada and Japan \$50 million. The actual distribution more or less followed this pattern, except that the U.S. share was less than anticipated at \$210 million. The conditions of the credit were to be very stiff: a interest margin of 2.25% over libor; flat fees of 1.5% and a short 5 year maturity.

After arriving at a general consensus to go ahead without the IMF one of the major difficulties in the negotiations was how the banks would evaluate the

government's stabilization program, which, of course, was the justification for the credit. One problem was that many banks—especially those not in a position to professionally evaluate a stabilization program—were afraid of the implications of private banks monitoring a sovereign government's economic program. But the big banks which obviously could evaluate an economic program were more than willing to take on this responsibility and were able to override the concern of the smaller banks. Once it was decided that the banks should evaluate the program, a plan was worked out in which the government would voluntarily give periodic reports to the banks on the progress of the stabilization program and provide them with data that would facilitate their own evaluation of events.

As far as what to do if the program did not, in the view of the banks, proceed satisfactorily, the following unusual procedure was worked out. Loans would be made in two equal tranches, termed A and B. The A commitment would be disbursed immediately upon a formal agreement. The B commitment would be disbursed not before January 31, 1977. In order to secure the second tranche the banks would have to (1) receive a copy of the confidential 1976 IMF country report on Peru and (ii) banks making up at least 75% of the aggregate commitment had to express a willingness to make available the B commitment. It is the second condition that was the key to the agreement; it was implicit that the willingness of the banks to extend the second tranche would depend upon their opinion of the success of the stabilization program.

There was at least one other important element to the agreement: settlement of disputes with some transnational corporations, i. e., Marcona Mines and the Southern Peru Copper Corporation.

The former corporation had a long history of iron ore mining operations in Peru. In mid 1975 the government had expropriated its assets and declared that the situation was such that no compensation was merited. A conflict ensued, as Marcona, with considerable success, set up a world boycott of Peruvian iron ore shipments.

In the case of Southern Peru Copper Corp., the problem stemmed from a dispute in the interpretation of tax arrangements in the mining agreement.

The commercial banks made it clear that they were interested in seeing the disputes settled. On the philosophical level banks have always made clear that the mode of treatment of foreign investment was a key element in their evaluation of a country's creditworthiness. 16/ But on a more practical plane, many of the banks in the negotiations had close relations with the affected firms and were reluctant to support the government while these problems went unresolved 17/; in both cases the corporations own creditworthiness may have been affected by the outcome of the disputes.

During the course of negotiations for the refinance credits, the government of Peru reached settlements with the aforementioned corporations. At least formally the settlements were not a condition for the refinance credit; indeed the actual credit agreements made no mention of the disputes or their resolution. But there is no doubt that the banks' open concern about the matter placed pressure on the Peruvians to reach a quick settlement. Clearly the division among the banks with regard to supporting the stabilization program would have been much more difficult to overcome if the investment disputes had not been diffused. So in an implicit, if not formal, sense the resolution of the expropriation and tax issues was a condition for the 1976 refinance credit, demonstrating once again that commercial banks and TNCs work closely together. But how was Peru affected by these conditions?

In the case of Marcona, intense negotiations had been underway for a long time over the subject of compensation. The corporation's home country government was pressing hard for a settlement and prodding Peru for compensation. 18/ This was on top of the foreign company's organization of a boycott against Peruvian iron ore exports. Both this pressure and a changed domestic environment in Peru made a settlement likely in any case. The banks undoubtedly speeded up the process and maybe the settlement was more favorable to the expropriated

corporation than Peru would have liked. On the other hand the compensation was covered by the new refinance credits. Also a settlement permitted Peru to renew iron ore exports, which would help to support the stabilization program.

In the case of Southern Peru, the banks were really insisting that Peru come up with a final decision on the tax matter (as opposed the avoidance of taxes) and provide a credit to the corporation for any back taxes that might arise. As it turned out, the government interpreted the tax question in a way which was least favorable to the Corporation. The ensuing back taxes were paid over time. 19/

The above were the principal controversial elements of conditionality. Others, such as ~~wreiver~~ waiver of sovereign immunity, cross default clauses, membership in the IMF, etc., were rather standard conditions that appeared in most credit agreements.

#### D. A SUMMARY EVALUATION OF CONDITIONALITY

Given the scope of this section on conditionality, it is worthwhile to end the analysis with some summary observations.

It has been seen that with regard to bank conditionality, the subject turned full circle over the 12-year period. Banks began and ended their lending under circumstances of onerous conditionality. This is an important consideration because when commercial banks imposed conditionality on Peru in 1976 a world-wide uproar developed over the banks interfering in public policy. The reaction was as if banks had never done this before. Memories are short and clearly minds were glued to the brief period of unconditional lending of 1972-1975. But in reality commercial banks were really rediscovering their conservative practices of the 60's.

It is true that it was unusual for commercial banks to extend large credit without the IMF overseeing the economy. But in the case of Peru, this had already been done in 1969-1971 when, as has been just seen, large refinance



credits with conditionality were extended to the government even though no standby agreement was reached with the IMF. What was new, however, was that private commercial banks took it upon themselves to monitor and evaluate the performance of a sovereign government's macro-economic policy. Unlike the past, conditionality was not placed on a specific policy parameter such as external debt contraction, but rather involved the entire economy. In other words, they assumed the role of the IMF.

From the standpoint of Peru, a stabilization program with the banks could have made sense. The bankers were by far its major creditor. In contrast to bank finance, IMF standby credits were a pittance. Why go through the distasteful exercise of an IMF program when more resources and maybe less rigorous conditionality could be gotten from the banks?

And from the standpoint of the commercial banks it could have appeared sensible too. When lending for general refinance (balance of payments assistance), it is clear that the capacity for repayment is largely embodied in government economic policy. And since bank finance now dwarfed all official sources of funding to LDCs, these institutions had de facto leverage over economic policy of developing countries. The fact that banks had been entertaining ideas along this line is suggested in the following commentary by one major international bank in early 1976:

"... It is incumbent on banks to improve further their competence in appraising borrowing countries' economic and financial policies. The Fund (IMF) generally will be involved only in the critical cases where the necessity for internal adjustment is clearcut. But, in the less-than-critical cases, bank credit decisions also involve a judgement on the way an economy is managed and on the prospects for the balance of payments. In deciding whether to extend credits, and in setting the terms and conditions for loans, banks can influence the nature and timing of borrowing countries' policies. This is a heavy responsibility, and admittedly one which is difficult to carry out, particularly in the face of competitive pressures. However, from the viewpoint of the borrower, the discipline of the marketplace can have an important bearing on whether sound economic and financial policies are taken on a timely basis. 20/

Of course when presented with a concrete case where this philosophy could be applied in the extreme the banks understandably hesitated. But in the end the objective conditions of power and leverage prevailed.

As it turned out, the banks were more vulnerable than they had thought. Third parties were outraged by the prospects of commercial banks monitoring the affairs of a sovereign state, even if this was voluntarily agreed to by the borrower. Being private commercial institutions they clearly were open to charges of conflicts of interest e.g., foreknowledge of a country's exchange rate policy, credit and interest rate policy, etc., all could lead to questionable profit-making. Suspicions about the banks' role in the settlement of the investment disputes also added to the controversy. And as a final blow, internal problems in Peru made the national stabilization program falter.

Commercial lenders found themselves in a no win situation. Their private capital base made them sensitive to adverse public opinion. Their private capital orientation also gave them limited staying power, i.e., they could not support the Peruvian economy while it vacillated in the process of gaining domestic support for needed economic adjustments. Thus, the bankers withdrew to more familiar terrain: they told authorities that no more finance would be available until Peru reached a standby accord with the IMF.

As for Peru it was abandoned by its private creditors. As will be seen in the last chapter, the succeeding period involved numerous clashes with the banks and with the IMF as Peru attempted to find its way between the requirement of national political-economic policy and the demands of its foreign creditors.

Finally, all the above suggests as severe overstatement the often heard observation that commercial banks—unlike official institutions—are "standoffish and remote" and therefore provide developing country borrowers with a great deal of national autonomy. <sup>21/</sup> Under special historical circumstances of the unusually competitive period of the early 70's bank finance did approximate

a remote, arm's length market. But the recent history of Peru has shown that they can and do involve themselves in public policy, especially in moments of national economic weakness. This is an important qualification since developing countries are especially prone to economic difficulties due of a sensitive domestic-socio-economic milieu and volatile external markets.

### III. AN OVERALL VIEW OF THE IMPACT OF BANK LENDING ON PERU

Up to now analysis has focused on very specific aspects of the impact of bank lending on Peru. What is still required is a more general evaluation of the effects of commercial banks on the Peruvian economy. It is the task of this last section of the chapter to undertake such a review.

For the convenience of exposition, one can approach the matter by viewing both the positive and negative aspects of the banks' participation in the economy. The analysis will begin with the positive side.

#### A. BANK LENDING TO PERU: ITS POSITIVE ASPECTS

There are undoubtedly many positive elements in the banks' involvement in the economy. An attempt will be made to highlight some of those which were very important to the country.

##### 1. Breaking the grip of the financial boycotts

When the new government entered into power in 1968 its internal support was reasonably solid. But as seen in Chapters 3 and 4 the external environment was openly hostile, as manifest in the financial blockade initiated by official and private sources of external finance. (And it must be remembered that the prior civilian government also encountered problems, albeit of more modest proportions, from official lenders.) During 1969-1971 Peru's external finance was severely prejudiced by the reserved attitude of foreign financiers. The country's balance of payments remained afloat in no small part because of some extraordinary factors: favorable export prices, virtual stagnation of import volume, and a special law in 1970 that successfully repatriated capital held abroad by residents.

Commercial banks, and more specifically the newcomers to international lending, were a key in the breaking of the blockade. Prior to 1972 few banks would lend to Peru. The country's traditional bankers, whether because of objective economic circumstances or because of tacit cooperation with the boycott, limited credit to highly conditioned refinance operations. But when the new non-traditional banks began lending to Peru in 1972 this started a process, similar to a bandwagon effect, in which ever more commercial institutions—including the country's traditional bankers which reacted in a defensive manner—became disposed to lend to the government. As lending built up, so did the government's maneuverability and international prestige. By 1973 it became evident to the perpetrators of the blockade that their policy was increasingly unproductive. This, along with other considerations, led to the Greene Accord and the termination of the blockade, under conditions that were relatively favorable to Peru.

The banks' willingness to lend to Peru undoubtedly had something to do with internal factors such as the discovery of oil in the Amazon and the outward appearance of an improved balance of payments due to some conjunctural circumstances. However, this was only a part, and a small part, of the changed attitude of the banks. As was seen in Chapter 4, much could be attributed to historical timing; changes in the eurocurrency market itself caused banks to seek out new clients in order to absorb liquidity and facilitate a seemingly insatiable desire to expand abroad. The extreme competitive pressure to expand assets promoted a global as opposed to a national psychology; banks no longer went abroad just to serve the interests of their home country TNCs, but in the interests of internationalization for its own sake. Thus, most banks were willing to overlook Peru's treatment of foreign firms and eagerly provided "no questions asked" finance to the government up until 1976. This represented a sharp break with the past whereby commercial lending was conditioned by a country's attitude on private capital in general and foreign capital in particular.

These historical events had great implications for Peru (and other LDCs as well). Had the government faced a financial blockade of similar proportions in the 50's or 60's there would have been a greater likelihood of its domestic policies (especially the investment program) having been aborted by external pressures. In these years private non-financial firms (via direct investments and supplier credits) and official bilateral and multilateral agencies were the main providers of finance, and all these sources traditionally had close political links with each other. (Big international banks, of course, also were in this group, but at the time they were not heavily involved in the finance of LDCs.) In the case of Peru the links among the various external financiers could have been activated very easily because of the severe geographic concentration of the country's economic relations. Thus, any attempt to reorder foreign capital's role in the economy, at least on a scale similar to that which was actually realized, could have been very costly to the country and perhaps not even feasible without extreme political cohesion at home.

Thus in 1972-1975 finance from banks was abundant and independent of pressures from the industrialized countries' governments and TNCs. This produced an unprecedented plurality in developing countries' external finance. In turn there were much enhanced opportunities for national self-determination. There is no better example of the change in environment than Peru where banks effectively gave important support to a model based on state intervention and comprehensive reform of private capital.

## 2. The capacity to import

After 1971 banks were the principal factor behind a growing capacity to import goods and services from abroad. This was to some extent evident in Chapter 3; as was seen in table 3.3 and again in table 3.9, imports of goods and services were a sharply rising percentage of product, while exports were

a sharply falling percentage of product. This prolonged trend, of course, was feasible only because of support from external finance, which in the period was dominated by transactions between commercial banks and the government.

The impact of the banks on the capacity to import can be more clearly seen through formal analysis of the key elements behind the ability to purchase abroad. This type of analysis follows using constant 1970 U.S. dollars. Making a determination about the banks' role in the capacity to import involves a degree of inference because of limitations on data. While this study has generated information on the net flows of loans from banks, it is not derived from official balance of payments data and therefore is not necessarily consistent with such data. Moreover, official balance of payments data do not provide a very detailed breakdown of financial flows, so that there is no way to single banks out from total finance. Nor is there any way to distinguish bank flows to the public sector. But Chapter 4 pointed out that banks were easily the dominant lenders in the period 1972-1976, so that any movement of loan flows in the balance of payments for these years would mostly be attributable to them. It also is known that the public sector was the principal foreign borrower in the country. On this basis the capacity to import can be reviewed.

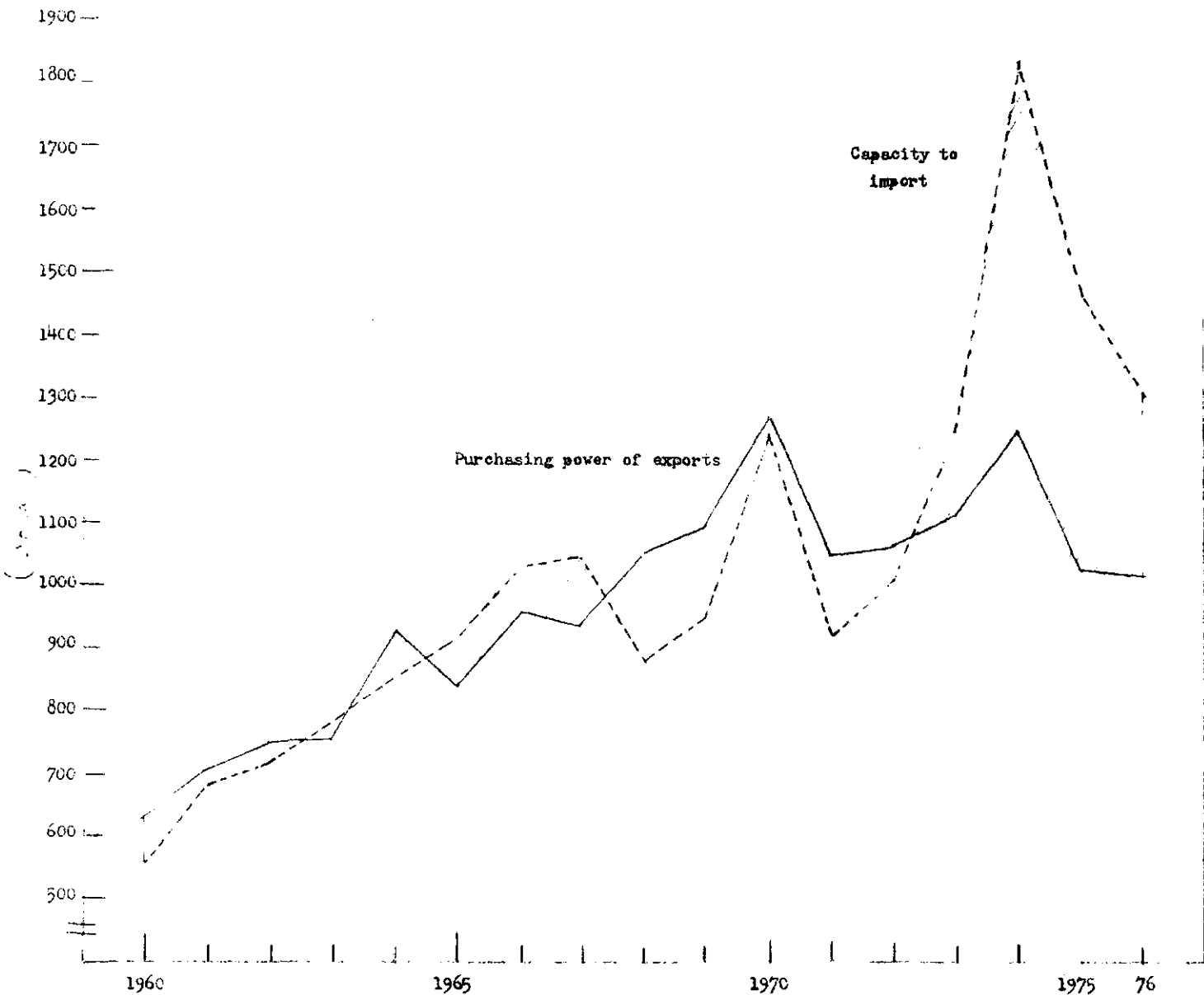
Figure 8.1 graphs the evolution, in real terms, of the purchasing power of Peru's exports and capacity to import over the period 1960-1976. 22/ One can determine the relative contributions of current account income and net financial flows by whether capacity to import was higher or lower than the purchasing power of exports. When capacity was higher, this meant that net financial flows added to total capacity, thereby enhancing the country's ability to import, or alternatively, to accumulate reserves. When capacity to import was below earnings from current transactions, this meant that there was a net outflow of

Figure 8.1

PERU : PURCHASING POWER OF EXPORTS AND CAPACITY TO IMPORT, 1960-1976 <sup>a/</sup>  
(Millions of 1970 dollars)

NET NON-COMPENSATORY EXTERNAL FINANCIAL FLOWS

- Positive
- Negative



Source : CEPAL on the basis of official data

<sup>a/</sup> Purchasing power of exports is export volume adjusted by the terms of trade. Capacity to import is purchasing power of exports + net Financial Flows, the latter being defined as net non-compensatory capital flows less net factor payments and amortization of compensatory loans.



autonomous funds that drained resources generated from exports. Thus, capacity to import in this latter case would be inferior to export earnings. Only to the extent that the government sought compensatory finance, or drew down on foreign exchange reserves, could this lost capacity be recuperated for purchases abroad.

What the graph makes clear is that there was a long run tendency towards a rising capacity to import. However it is striking that up until 1973 Peru's capacity to import was almost wholly dependent on earnings from export; indeed, except in 1965-1967, the net contribution of external financial flows was negative or marginal, subtracting from, or adding very little to, the country's real capacity to import goods and services. However, after 1972 there was a notable change in relationships. Exports provided no increment in capacity; indeed the 1970 peak in the purchasing power of exports was never regained and earnings from this source were flat throughout the 1970's. However, strong stimulus was provided from external financial flows so that capacity to import actually rose dramatically between 1972 and 1974; by the latter year the country's ability to purchase abroad, in real terms, was nearly 50% higher than the peak level achieved in 1970. While the capacity to import declined sharply in 1975-76, net financial flows still provided a very positive contribution and helped to assuage the effects of a dramatic decline in the purchasing power of Peru's exports. (In real terms, the purchasing power of exports in 1976 was below the level recorded in 1968.)

It is no coincidence that the noticeable rise in capacity to import in the 70's, and the overwhelming importance of external financial flows in this increase, corresponded to a period when commercial banks were most involved in the Peruvian economy. Indeed, as seen in table 8.5, loans, for which commercial banks were largely responsible, accounted for almost all the positive contribution derived from financial flows. Moreover, looking at total

Table 8.5

PERU: EVOLUTION OF CAPACITY TO IMPORT, 1960-1976

(Millions of 1970 dollars; annual averages)

Years	Purchasing power of exports <u>a/</u>	Financial flows (net) <u>b/</u>						Capacity to import <u>1+2)</u>
		Total (6+7)	Foreign flows				Other <u>f/</u>	
			Direct foreign investment <u>c/</u>	Loans <u>d/</u>	Other <u>e/</u>	Total (3+4+5)		
1960 - 1964	754	-38	-66	49	-	-17	-21	716
1965 - 1970	1 023	-15	-104	77	17	-10	-5	1 008
1971 - 1976	1083	210	19	368	20	407	-197	1 293

Source: CEPAL, on the basis of official data.

a/ Exports adjusted for the effects of the terms of trade. Includes non-requested transfers.

b/ Deflated by import price indexes.

c/ Net direct foreign investment less profit remittances.

d/ Gross non-compensatory short, medium and long term loans less amortization and interest payments.

e/ Net of donations, SDRs, and amortization of compensatory loans.

f/ Net movement of assets of residents and errors and omissions.

financial flows only understates the full contribution of non-compensatory loans because a significant part of the inflow was offset by an outflow on errors and omissions and national assets, designated as "other" financial flows in the table. 23/

The table also clearly shows that the purchasing power of exports underwent practically no growth in 1971-1976, as compared to the previous sexenium. Thus, loans were almost the sole factor behind the 28% rise in the average capacity to import. And even more importantly, ceteris paribus, if there had not been the dramatic increase in loan flows, the ability to import would have actually declined with respect to 1965-1970.

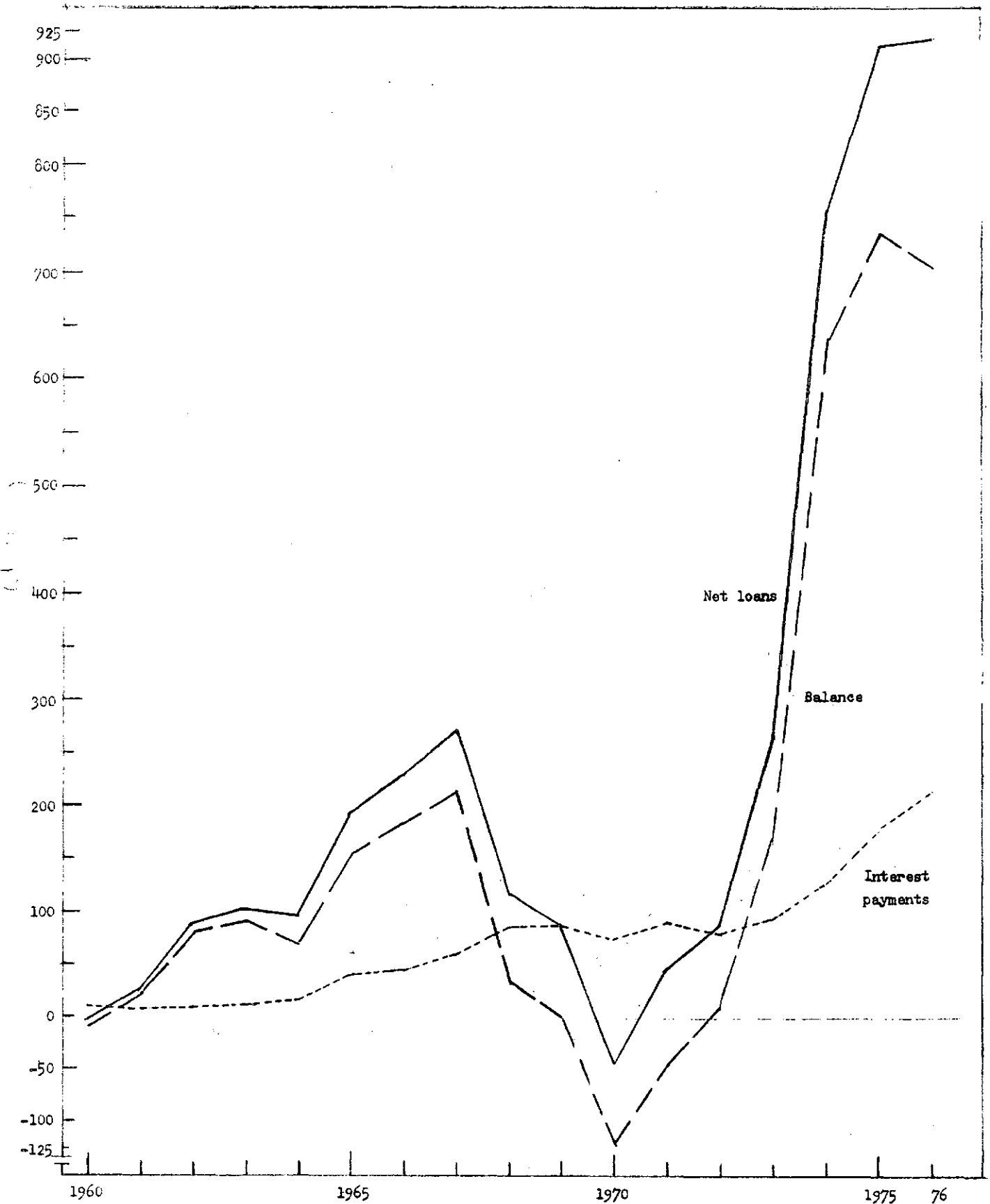
Figure 8.2 provides more information on how non-compensatory loans evolved. It is seen that in both net and gross terms loans rose in dramatic proportions from 1972. By 1975 the net contribution of credits was, in real terms, three and one-half times as large as the previous peak flow achieved in 1967. The figure also shows that after 1973 interest payments accumulated rapidly, absorbing considerably greater amounts of new disbursements of loan capital. Nevertheless, the transfers via loan capital were very considerable throughout the period.

It is clear from the above that without the massive influx of loan capital in general, and bank capital in particular, during the 1970's Peru would not have been able to realize an unprecedented growth of import volume, which averaged nearly 16% per annum during 1972-1975 (see figure 8.3). Neither export prices nor volume were up to this task, as manifest in the near stagnant purchasing power of the country's exports. This left nearly the full burden of growth on foreign capital. Thus, commercial bank loans were crucial to breaking what most certainly was a very debilitating external bottleneck.

Figure 8.2

PERU : BALANCE OF NET DISBURSEMENTS OF NON-COMPENSATORY LOANS AND INTEREST PAYMENTS, 1960-1976 <sup>a/</sup>

(Millions of 1970 dollars) <sup>b/</sup>



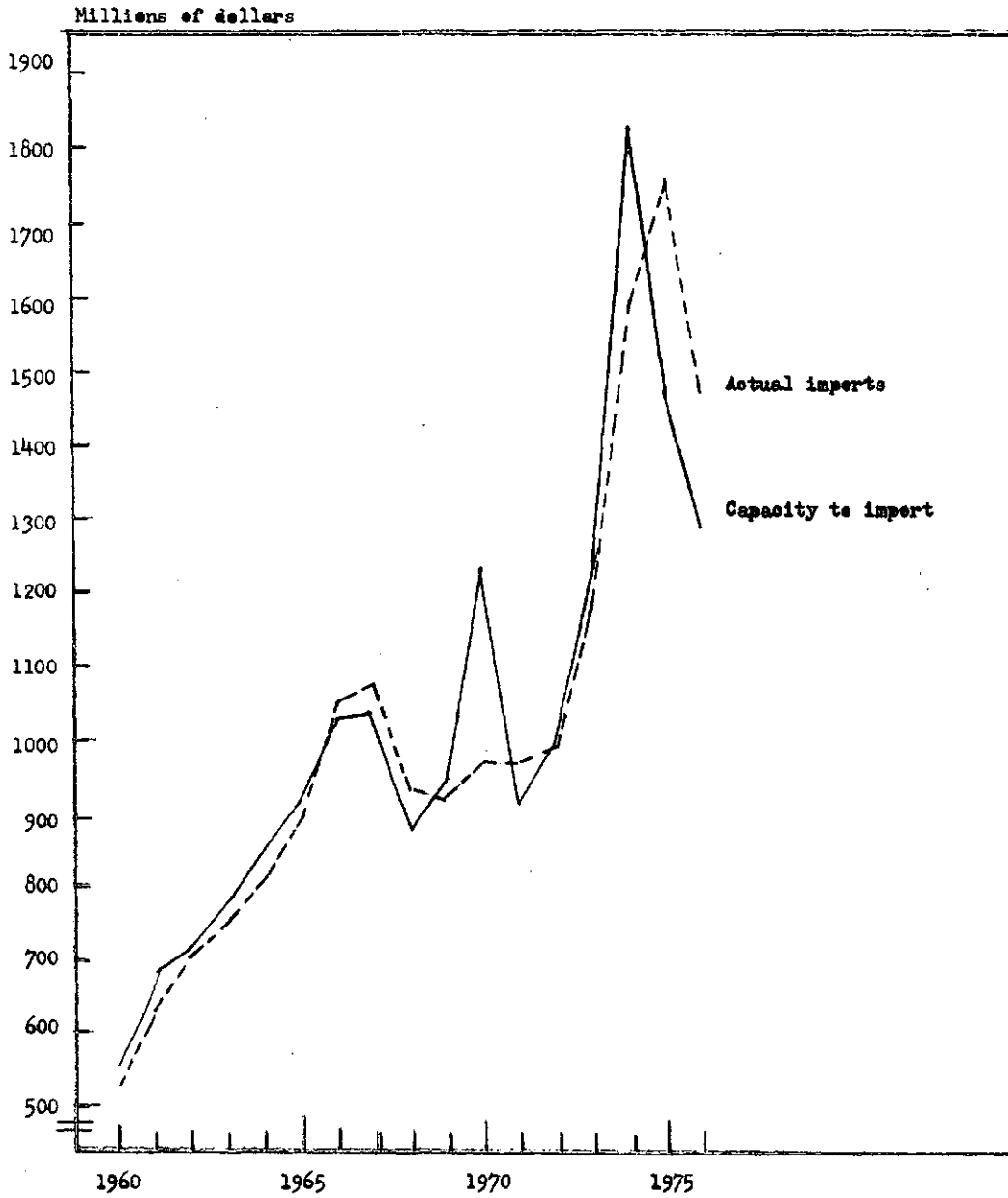
Source : CEPAL on the basis of official data

<sup>a/</sup> Loans are short, medium, long term.

<sup>b/</sup> Deflated by interest rates

Figure 8.3

PERU : CAPACITY TO IMPORT AND ACTUAL IMPORTS, 1960-1976  
(1970 dollars)



Source : CEPAL on the basis of official data

### 3. Impact on domestic demand

The growth of imports that was facilitated by bank loans during the period 1972-1975 had a very significant impact on the evolution of the domestic economy. This can be seen clearly in table 8.6.

The table shows that during 1972 to 1975 there was substantial increment in the growth of domestic demand with respect to the first 3 years of the military government. The 8.8 percent rate of growth experienced in 1972-1975 was more than one-fifth higher the rate recorded in 1969-1971. Within the components of domestic demand, there was a remarkable acceleration in the growth of private investment and a very sharp increment in the growth of public consumption as well as in the expansion of state investment.

The reliance of domestic demand expansion on imports is, of course, mirrored in the difference between the rate of expansion of domestic demand and growth of domestic product. It can be seen from the table that while the growth rate of domestic demand rose by more than 20% between 1969-1971 and 1972-1975, the rate of expansion of product actually slipped by nearly 10%. Thus the gap between the expansion of demand and product rose from 1.1 percentage points in the former period to 3.2 percentage points in the latter. Since import growth was heavily reliant on loans there is no better indication than this of the importance of external finance and banks in the overall performance of the domestic economy.

A further idea of the impact of bank finance on domestic demand can be given by viewing Peru's performance against that of the rest of Latin America.

Table 8.7 provides data on the growth of domestic demand and gross domestic product for the two entities during the period 1972-1975. (Since the original data for table 8.7 are in U.S. dollars, rates of growth are not comparable to those in table 8.6.) What the data show is that Peru enjoyed a markedly

Table 8.6

PERU: GROWTH OF DOMESTIC DEMAND AND PRODUCT, 1969-1971 AND 1972-1975<sup>a/</sup>

(Average annual rates of growth)

	1969-1971	1972-1975
1) <u>Total private sector</u>	<u>6.3</u>	<u>8.0</u>
Consumption	6.7	7.8
Fixed investment	3.1	10.2
2) <u>Total public sector</u>	<u>8.9</u>	<u>12.6</u>
Consumption	5.8	7.6
Fixed investment	18.4	22.5
3) <u>Domestic demand</u>	<u>7.3</u>	<u>8.8</u>
4) <u>Gross domestic product</u>	<u>6.2</u>	<u>5.6</u>

Source: CEPAL, on the basis of official data.

<sup>a/</sup> Based on market prices in 1970 Soles.

Table 8.7

PERU: GROWTH OF DOMESTIC DEMAND AND PRODUCT IN COMPARISON  
WITH LATIN AMERICA, 1972-1975<sup>a/</sup>

(Average annual rates of growth)

	Peru	Latin America
Consumption	6.9	5.5
Investment	13.9	12.0
<u>Domestic demand</u>	<u>8.1</u>	<u>7.0</u>
<u>Gross domestic product</u>	<u>5.6</u>	<u>6.5</u>

Source: CEPAL, on the basis of official data.

a/ Based on market prices in 1970 U.S. dollars.



higher rate of growth of domestic demand than did Latin America as a whole, 8.1% versus 7.0 percent for the region. However, Peru's expansion of product was just as markedly lower, 5.6% versus 6.5% for the region. Overall, the differential between growth of domestic product and domestic demand—which is reflective of reliance on imports—was 2.5 percentage points for Peru and only 0.5 percentage points for Latin America. Thus, growth of domestic demand in Peru was not only high relative to Latin America, but reliance on imports to sustain demand also was much more severe than other countries. And, of course, in the case of Peru, banks were a major factor underpinning growth of imported goods and services.

Another striking feature in table 8.7 is that consumption had an unusually high profile in domestic demand, simultaneously with a very high rate of growth of investment. While growth of consumption in Latin America was one percentage point inferior to the growth of product, in Peru, consumption rose at a pace that was 1.3 percentage points above the growth of the nation's domestic product. It is clear from this that the reform government was able—thanks in no small part to the finance provided by foreign banks—to pursue an unusual policy whereby a massive investment program for the future was accompanied by an especially buoyant present day consumption. Thus, bank finance helped in a significant way to support a push for rapid development that, for at least 4 years, involved no sacrifice of consumption; in fact this indicator of living standards rose, in the macro sense, very rapidly indeed.

Other manifestations of the evolution of domestic demand are found in table 8.8. It is seen that in 1972-1975 there was a very significant rise in employment and fall in underemployment and unemployment with respect to 1969-1971. Also it is significant to note that real wages expanded very rapidly between the two periods as well. This is another sign of enhanced well being during a period of bank involvement in the economy.

Table 8.8  
 PERU: EMPLOYMENT, UNDEREMPLOYMENT, UNEMPLOYMENT AND REAL  
 WAGES, 1969-1971 AND 1972-1975

	Average	
	1969-1971	1972-1975
<u>Percentage of labor force</u>		
Employment	49.5	53.3
Underemployment	45.5	42.4
Unemployment	5.0	4.3
<u>Total</u>	<u>100</u>	<u>100</u>
<u>Index 1970 = 100</u>		
Real wages of workers (index in 1970 soles)	98.6	110.4

Source: Employment: Schydrowsky and Wicht; real wages: CEPAL, on the basis of official data.

The above clearly shows that banks, indirectly through their support of Peru's capacity to import, had an important role in the evolution of domestic demand. Moreover, expansion of demand in the period of heavy bank involvement in the economy was unusually strong and involved rates of growth in investment and consumption that were considerably higher than product. A highly buoyant growth of consumption, both with respect to previous rates in Peru, and rates in Latin America for the same period, could suggest enhanced well-being for the populace as a whole. This is further supported by data on employment and wages. Whether these clear immediate benefits in the macro sense were reasonably well distributed among the members of nation is an interesting matter, but it would be beyond the scope of the study to take the investigation into this type of difficult terrain. 24/

#### 4. Impact on public finance

It has been seen in earlier chapters that bank lending to Peru has had a primordial impact on the country's fiscal budget.

During the fiscal crisis of 1966-1968, commercial banks extended timely loans to the financially strapped central government. Some of the loans were medium term general purpose credits, others were for refinance of prior obligations and an important unquantifiable part involved short term bridge finance designed to tide the government over until it could find more domestic resources.

While bank finance in 1966-1968 was decisive at the margin, and therefore more important for its timeliness than for its sheer volume, in 1972-1975 it played a pervasive role. Banks continuously refinanced upcoming debt service payments of government, freeing resources for the investment program. They provided a large amount of freely disposable funds which the government could

use to build up reserves or employ as it wished. And while banks were not overwhelmingly involved in project finance, it was seen that they were involved in very high priority national ventures, the most notable being the transandean oil pipeline (and, in the private sector, the Cuajone copper mine). Moreover the banks generally were not afraid to cover local costs, which again had the effect of freeing national resources for other uses.

It is difficult to empirically define the weight of bank loans in the total finance of the government's expenditure program because fiscal data do not provide a sufficient degree of disaggregation. However, as in the analysis of the capacity to import, the role of banks can be inferred from other data. In this case, one can look at the portion of expenditures financed externally and safely assume that at least for 1972-1975 the banks had a high profile in total flows. Also bank finance would have been significant, but not necessarily dominant, in 1966-1968.

Table 8.9 displays data on the central government budget for some selected periods. It is seen that external financial flows were very important relative to internal sources of finance in 1966-1968 and 1972-1975; in both periods roughly 50% of the budget deficit was covered by foreign resources. Of course, while banks had a role in the foreign finance of the former period, they clearly were the most important source of external finance in the latter. Moreover, it was in this latter period when the budget deficit to be financed was absolutely most significant, exceeding one-fifth of total expenditures. Thus banks would seem to have had considerable weight in central government finance during 1972-1975. 25/

Another way of looking at the importance of banks in finance during 1972-1975 is to look at growth rates of revenue and expenditure. Using data in table 3.2 of chapter 3, one can see that initiating with a deficit in 1971 expenditure (excluding amortization) rose by an average of 24% per annum in the period, but central government income rose by only 21% per annum. As just seen, more than half of the ensuing deficits were financed externally, in a period when commercial banks were the principal source of finance.

Table 8.9

PERU: CENTRAL GOVERNMENT FISCAL DEFICIT AND ITS FINANCE,  
1966-1968; 1969-1971; 1972-1975; AND 1976

	Average			1976
	1966-1968	1969-1971	1972-1975	
Fiscal deficit (billions of soles) <u>a/</u>	4.8	3.9	17.4	48.4
Deficit as percentage of expenditure <u>a/</u>	16.3	9.3	21.4	30.3
Finance of the deficit (net)				
Percentage externally financed	47.2	18.0	51.8	32.2
Percentage internally financed	52.8	82.0	48.2	67.8
<u>Total finance percentage</u>	<u>100</u>	<u>100</u>	<u>100</u>	<u>100</u>

Sources: CEPAL, on the basis of official data.

a/ Excludes amortization of the public debt.

Thus one can conclude that banks were very important to public finance during the early 70's.

##### 5. Freedom from IMF surveillance

An aspect similar to that just mentioned above involves the role of banks and the IMF. As was seen in Chapters three and four, the governments in power during the 1960's were under IMF scrutiny. This traditionally has not been looked upon with favor by authorities because IMF standby agreements are seen by many to be excessively harsh, and even counterproductive, to national development objectives. However, Peru, as well as other developing countries with external problems, usually could not avoid the IMF because it was the only major source of general balance of payments assistance; moreover, when there were obvious balance of payments problems manifest in a country, other sources of finance, both private and official, were accustomed to tying their resources to successful completion of IMF requirements.

The IMF standby accord of 1968-69 must have been particularly irksome to the military government, which was seen to have pursued a highly nationalistic political and economic program. However, given the state of the external accounts, the government had little choice but to continue the standby program agreed to by the previous government. The boom in export prices in 1970, coupled with a brief recovery of export volume, provided a sufficient boost to the balance of payments to permit the government to forego renewing the IMF agreement that expired in mid-1969. However, given the evolution of the purchasing power of exports in succeeding years, coupled with the burden of substantial debt service payments, the government may very well have had to exercise discipline in order to avoid returning to the IMF for assistance. But as it was, a wave of non-traditional lenders began approaching Peru in the 70's with unconditioned finance. This provided the necessary boost to the external accounts, not only facilitating rapid growth of imports, but also massive accumulation of foreign exchange reserves.

As shown earlier, by 1976 the banks had become less favorably disposed towards Peru, while simultaneously there was a severe deterioration of most internal and external economic indicators. The balance of payments disequilibrium was severe, and the banks were decidedly more cautious towards further extension of credit to the country; they also were encouraging authorities, for the first time in many years, to undergo IMF scrutiny. However, the government, for political reasons, had a great desire to avoid the IMF and therefore it negotiated intensely with the banks for a large 400 million dollar refinance credit that would not be tied to an IMF standby agreement. As has been seen the banks finally agreed to the Peruvian proposal, thus once again permitting the government to avoid the seemingly disagreeable scrutiny of the Fund. But the bank credit was not free of political costs or conditions. Moreover, the update provided in the last chapter will reveal that avoidance of the Fund only was temporary as the following year relations with the banks underwent serious deterioration, leaving the government no choice but to agree to an IMF standby accord in late 1977.

#### B. THE NEGATIVE SIDE

One has just seen what might be considered to be some of the positive aspects of commercial bankers' involvement in the Peruvian economy. This analysis will be counterbalanced by what might be considered less propitious effects.

1. Did abundant commercial bank finance lull economic authorities into a sense of false security?

It has been already seen that bank finance allowed the government the luxury of rapidly growing imports, on top of a sharply deteriorating export base. This also helped to support an exceptional expansion of domestic demand. On the fiscal side, the government was able to simultaneously expand very rapidly its consumption and investment in 1972-1975 (and in 1965-67) side-by-side

with marked erosion of its tax pressure. But the opportunities provided by finance may have been a mixed blessing.

One cannot help but ask whether the abundant flow of commercial bank funds in 1972-1975 lulled Peruvian authorities into a false sense of security, postponing until much too late a time the needed adjustments in external and domestic economic parameters, thereby making the devastating economic crisis of 1976 (and later) inevitable and more severe than necessary. Of course, attempting to answer such a question puts one on highly normative terrain where there is no clear empirical evidence. Also observations in this regard can take advantage of hindsight. But the question is an interesting one that merits exploration.

As was seen in Chapter 3, when the new government took over in 1968 there were severe internal and external economic problems. Aided by some of the measures adopted in the last days of the previous government (under emergency Law 17044) authorities successfully reordered economic affairs. As has been seen in earlier chapters, by pursuing a rather orthodox monetary and fiscal policy, and aided by favorable export prices, the budgetary and external accounts once again became respectable. Also, inflation fell back to tolerable levels. But importantly, as shown in table 8.6, these adjustments were accompanied by considerable growth in domestic demand; in 1969-1971 the only depressing feature of the economy was the sluggish expansion of private fixed investment. Reflecting the effects of rather buoyant demand, there were significant increases in employment and a lowering of the rate of unemployment as well.

The rather hostile environment for external finance in 1969-1971 undoubtedly was behind the restrained behavior of imports, as mirrored in the rather small difference between the rates of growth of product and domestic demand. Thus, even though handicapped by an unresponsive foreign financial community, the government, through discipline and deep resolve, was able to



mobilize domestic resources to achieve respectable rates of growth. And it must be remembered that growth was accompanied by comprehensive socio-economic reforms.

Undoubtedly there was an element of catch up in the growth rates of 1969-1971. But this was not necessarily an overwhelming element. As seen in table 8.10, from 1966 through 1971 domestic product expanded steadily; so did consumption. The only area in the economy where a clear element of catchup was involved was in fixed investment, which did not reach the previous (and somewhat extraordinary) peak level of 1966 until the year 1971. Of course, it is likely that any serious expansion of investment past 1971 would have placed greater demands on the external sector than it did in the immediately preceding years. Therefore either exports earnings, external finance, or some combination of the two would have had to expand; and as it turned out the full burden was placed on external finance. This in itself carried implicit costs and dangers. But additionally, external finance may have exceeded the real capacity of the nation to effectively absorb it for purposes of development, fostering an overheating of the economy, inflation and severe external disequilibrium.

The economy began to display signs of overheating in 1972, precisely when access to bank finance began to take place. The overheating itself is evident from data just presented (tables 8.6 and 8.7) on the evolution of domestic demand and product. Since a detailed analysis of the macro economics of the problem already has been prepared elsewhere by CEPAL 26/, it is best to focus here on some specific institutional aspects, which underlied economic trends in any case.

As was seen in Chapter 3, the Peruvian public sector was relatively inexperienced. Expansion of the public sector in the 60's was on a very small base, reflecting the national tradition of laissez faire economics. But the reform government of the late 60's enormously expanded its presence in the economy in just three short years, 1969-1971. When it began to implement its

Table 8.10

PERU: EVOLUTION OF EXPENDITURES ON GROSS DOMESTIC PRODUCT, 1966-1971

(Index based on 1970 soles with 1966 = 100)

	1966	1967	1968	1969	1970	1971
Private consumption	100	102.5	103.5	109.9	120.6	125.5
Public consumption	100	105.5	111.3	114.1	123.7	131.7
Fixed investment	100	92.5	78.7	80.9	90.1	99.2
Domestic demand	100	101.8	97.6	102.7	112.4	120.5
Exports	100	101.5	112.8	108.1	112.9	103.1
Imports	100	102.5	89.3	87.5	92.3	92.5
Gross domestic product	100	101.6	102.3	106.8	116.5	122.5

Source: CEPAL, on the basis of official data

investment program it found foreign finance readily available. Thus in programming investments, authorities were not constrained by considerations about foreign exchange availability. A young, ambitious, highly motivated, but inexperienced bureaucracy took advantage of the situation and designed a massive multisectoral capital intensive development program that had high reliance on imports.

One problem, as clearly pointed out in the aforementioned CEPAL study, was that most of the projects had a long gestation period, with payouts not coming on stream until 1977 and beyond. This was particularly true for export oriented projects such as those in mining. But perhaps the eagerness of banks to support the external sector provided an illusion of security which gave authorities little need to consider spacing out projects so that there was an adequate mix of short, medium and long term payouts.

Moreover, the abundance of finance gave little incentive to authorities to adjust economic parameters so as to screen imports and fully exploit existing export capacity (notwithstanding the loss of the anchovy). Bank finance supported an overvalued exchange rate that stifled the incentive to export. The overvalued exchange rate also made it easier for the private sector to over-import, whether because of speculation or a desire to pursue investments that would stave off worker control of their industries. 27/ Meanwhile, it was easier to import food than produce it. The overvalued rate also provided greater incentive to accept bankers overtures with regard to credit.

The abundance of external finance also could have contributed to a lax attitude on fiscal matters. As long as there was easy access to external credit, it was politically much easier to borrow abroad than to tax at home. When a significant part of the growth of government consumption and investment was covered by foreign credit, everyone could enjoy the benefits with little immediate cost. To pursue the same massive expansion via greater taxation would have been less feasible, as expenditures undoubtedly would have met resistance by those who had to finance them. And the resistance to increased

tax pressure would have disciplined expenditures and required an ordering of priorities and attention to import content. As it was bankers facilitated an economic environment where all was possible with little domestic discipline, as least for awhile.

Had Peru's international bankers been willing to provide unconditional finance ad infinitum an external economic nirvana could have been guaranteed. But by 1976 bankers clearly had changed their attitude towards Peru, and to a lesser extent towards LDCs in general. Suddenly bankers abandoned their carefree attitude on loans to LDCs; they rediscovered "prudent" lending practices and once again became preoccupied with economic policy. Peru's declining international reserves distressed the world bankers. The more reticent bankers became about new loans to the government, and the more onerous the terms of their credit, the more transparent became the veil of finance, showing behind it a structurally weak economy. Peru's creditors panicked and this made new finance difficult to attain.

More importantly, Peru found itself very vulnerable and in a poor position to defend itself. The country's export coefficient was half of its 1965 level and nearly a third of earnings was absorbed by foreign debt service. The strategy of long term development of export capacity meant that new exports would come on stream only gradually beginning in 1977. And the development of oil exports took on a much longer term character than had been originally anticipated. Meanwhile, over 40% of the country's imports were underpinned by external finance in 1976 (current account deficit divided by imports), compared to practically no dependence in 1969-1971. Moreover, since imports were structured around intermediate and capital goods, any sharp reductions in purchases would severely damage output and employment. In a country where large politically influential groups had become accustomed to fast rising

levels of consumption and even larger groups were at the margin of existence, any attempt at rapid adjustment would encounter strong resistance and tremendous social costs.

Thus, evidence suggests that the temporary period of buoyant commercial bank finance to LDCs in the early 70's lulled authorities into a position of severe vulnerability vis-a-vis the banks and foreign finance in general. This was in direct contradiction to the government's initially stated intention (see Chapter 3) to rely basically on internal resources for development. Ironically, while Peru successfully reduced dependence on TNCs and official lenders, it appears to have traded this dependence for another more complicated type involving foreign commercial banks. Whether one form of dependence is less negative than the other would be an interesting matter to study. But one thing is clear: eradication of foreign dependence was a major goal of government policy and this objective appears to have been undermined by an excessively permissive banking community.

## 2. Commercial banks: an ephemeral source of development finance

Private commercial banks entered into external finance en masse in the early 1970's, displacing official institutions as the principal source of development finance for LDCs. 28/ Ideally this displacement should have been accompanied by a responsibility to accommodate borrowers in good times and bad. Moreover, banks should have anticipated that lending to LDCs obviously would be qualitatively different than lending to TNCs and industrialized country governments; the former are particularly prone to bad times because of an unstable external economic environment and a generally sensitive domestic socio-economic structure. In the case of Peru, the issue of responsibility becomes all the more manifest when one takes into account the participation of the commercial banks in Peru's economic problems.

Commercial banks displayed an almost unlimited willingness to lend resources to the government up through 1975, despite the fact that, as shown in the aforementioned CEPAL study, there was evidence of inflated demand as early as 1972. The policy initiated in 1968 involving a fixed exchange rate without compensation for inflation had obvious consequences for growth of exports and imports. The composition of imports, which banks helped to finance, was fully known by all. By 1973 the country's export coefficient was already 40% less than 1968, and, of course, continued to decline thereafter. The large accumulation of reserves that occurred from 1972 onwards—making Peru appear very liquid—happened simultaneously with a sharply expanding current account deficit, meaning that growth of reserves was only a reflection of borrowing from abroad, and not the dynamic generation of real income.

To the extent that bankers were unaware of, or oblivious to, the underlying economic trends, then their own management of lending to Peru would have to be deemed to have been sloppy and reckless. If bankers were fully cognizant of the trends from the beginning, then they too must have been awaiting the results of the payout on the long term investments in mining, petroleum, etc. But whether banks lent due to overzealousness or on the basis of the calculated risks of future export earnings, their tacit or explicit support of government policies prior to 1976 would lead one to expect that ideally they would bear the consequences of their decisions and help Peru overcome its difficulties without grave social costs. As it was the banks quickly abandoned the authorities, leaving Peru to fend for itself.

One might argue that the abandonment of Peru resulted from the fact that the authorities' management of the crisis did not instill the confidence needed for bankers to ride out the storm. Maybe management of the crisis was not up to the expectations of the commercial bankers. But banks were not dealing with a rich government borrower or a TNC. Any difficulties in adjustment were a function of Peru's underdevelopment and the momentum found

in the economic policies which the bankers unquestionably supported through abundant finance. To put a break on past trends, no less reverse them, clearly would be a long and arduous process, involving not only changes in policy, but important psychological, political and social adjustments as well. Hesitation, resistance and numerous outright failures at correction could be anticipated, as could a desire to pursue adjustment gradually so as to avoid harsh social costs in an economy suffering from severe poverty (even in the best of times). 29/ But private bankers apparently were not able to assume the responsibilities that their dominant role in development finance implied. Private creditors showed little tenacity; when their initial willingness to support adjustment resulted in failure, they quickly withdrew their support of the economy, giving Peru no alternative but to submit to the IMF.

What one can conclude is that commercial banks have a low threshold for absorbing the problems encountered by developing countries. While the going was good, the banks were eagerly present, making the going even better. When the economics of the country turned sour, their staying power depended on the government quickly taking hard decisions that would squeeze foreign exchange out of the economy for payment of debt; decisions that also would be socially very costly and probably confront severe domestic resistance. As soon as it was apparent that the mixture of politics and economics was not yet ripe for harsh adjustment the bankers lost confidence in Peru.

Thus banks clearly were not able to satisfy one of the basic needs of development, i.e., a stable source of finance able to weather periodic internal and external difficulties that can be expected in developing countries. It is true that Peru's problems were unusually severe, but it is also true that bankers had given open-ended support to the policies that generated the problems, making them particularly responsible for ensuing difficulties. It will be seen momentarily that the banks' behavior fell short of the needs of development finance basically because of weaknesses intrinsic to its institutional makeup.





This presented developing countries such as Peru with a challenge, but not necessarily an insurmountable one. Loans had to be carefully used to ensure that returns on the resources were comparable to their costs. And the costs, after discounting inflation, usually were not outrageous; indeed in 1973-1975 the real cost of credit for Peru may have been marginal. <sup>31/</sup> Thus, rather than absolute cost, the real challenge probably is in the variability of the interest rate; sharp fluctuations make it difficult to program costs and therefore marginally profitable ventures could suddenly become unprofitable.

More serious than the variability of the interest rates is the short maturity of commercial credit. Peru's commercial loans for the whole period 1971-1976 averaged only 7 years. These are very short maturities suitable only for the most commercial of ventures. In contrast, a broad-based development program incorporates activities which necessarily have rather long gestation periods. On the commercial side, many projects involve infant industries that may have payouts that are much more stretched out than identical activities in industrialized countries. This is aside from prolongation of payouts due to mistakes and unforeseen events, such as falls in export prices. On the social side, infrastructure for social development can payout sometimes only over a whole generation.

Clearly, then, commercial bank maturities are not symmetric with the income flow of a broad-based development program. This places clear obstacles in the path of development. There are, of course, many ways for policy makers to confront the dilemma. However, in order to illustrate the gravity of the problem, matters can be simplified into two basic options for a country that is considerably indebted to commercial banks. The two options are:

- (i) formulate growth on a narrowly based development program that focuses on quick payouts and high private rates of return, leaving social development at the margin today and relying on a "trickle down" effect to satisfy these needs in the longer run or,

(ii) seek a balanced broad-based development strategy, mixing commercial and social ventures, hoping that banks will fill the maturity gap through refinance operations.

The first route would be attractive to conservative economic managers, but experience has shown that the "trickle down" strategy has tended to only postpone indefinitely social reforms and reasonably equitable income distribution; by the same token, it has been associated with the exclusion of broad segments of society from participation in political processes. The second option on the other hand, would appear to open more hope for real and immediate socio-economic development, but unfortunately it is likely to prove to be full of pitfalls for borrowers, making them inclined to move progressively in the direction of option 1. This latter phenomenon is elaborated upon below.

As was seen in Chapter 5, banks do refinance, and often, making option two theoretically feasible. But refinance is a terribly awkward way to accommodate the long gestation period of broad-based development programs. Because of the short maturities, borrowers must regularly undergo the scrutiny of their bankers in order to realize successful refinance. They then become vulnerable to the changing attitudes of bankers and the volatile conditions on international capital markets. If refinance needs develop during a borrower's market—such as 1972-1974—the results can be attractive with low margins and relatively long maturities (for commercial finance). But if a borrower happens to approach its bankers during a lender's market—such as 1975-1977—the results can be discouraging and counterproductive. Aside from very high interest margins, 32/ maturities contract to only the briefest tenor. 33/ This causes interest payments to buldge and distorts the maturity profile, generating more requirements for refinance and complicating debt management. In this type of environment debt service can appear more burdensome and bankers can become nervous, further aggravating the trends. Under these circumstances, in order to maintain the confidence of bankers, government authorities may make a decisive shift to conservative economic management that places socially-oriented programs—which weigh heavily on the balance of payments—at the margin of policy.

When a country under economic duress seeks to refinance in a lender's market the results can be disastrous for development programs. Peru is a case in point. In 1976, with clear external difficulties that were structural in nature and that could not be remedied quickly, banks offered to refinance only one year of Peru's debt service and on a very short maturity of 5 years, with only 2 years grace. This provided "short leash" relief and ensured that payments would pop up quickly again to cause problems. Moreover, the short maturities were accompanied by a very burdensome spread (2.25%) and unusually costly fees (1.5% flat). These rather harsh terms came when bankers were still formally supporting the government. When this support was withdrawn in 1977, refinance maturities became ridiculously short, sometimes as brief as several months. On top of all the uncertainty with regard to refinance, bankers seeing Peru's vulnerability, also became involved in the government's economic policy and even began to protect the interests of their TNC clients. The lack of finance and commercial bank scrutiny caused the government to cut back its development program and, ironically, halt projects (like Cerro Verde II) that would have aided its export capacity. Social expenditures were slashed and development came to a halt while authorities rushed back and forth between their bankers and the IMF trying to reach an agreement.

It should be made clear that the behavior of creditors could have appeared rational from the short term viewpoint of individual commercial banks. The year-by-year and month-by-month refinance on tight maturities reduced perceived risks and gave commercial bankers leverage over economic policy making, which was the real source of repayment. Had they adopted a multi-year rescheduling to smooth out debt service payments—as ideally they should have—this leverage would have been lost and perceived risk increased. Also, a rescheduling would spot the financial statements of the banks. Meanwhile high interest margins and fees on the loans to Peru covered the perceived higher risk of lending under circumstances of economic duress. And as far as the impact of bankers' policy on the country's development program is concerned, this was of secondary importance. Commercial banks

are not development institutions; their main concern was to protect depositors and shareholders by ensuring that authorities squeezed enough foreign exchange from the economy to service its debt.

#### 4. Final considerations

It is clear from the above that bank finance of Peru's development has been a double-edged sword. Benefits there were, but these were offset equally or more by liabilities. The basic problem with commercial bank dominance of the country's development finance lies in the observation just made above: commercial banks, as their name implies, are not development institutions. Their orientation towards profits based on private rates of return places severe limitations on their integration into a broad-based development process, which by definition is based on social rates of return. Moreover, because commercial finance is based on the short term deposits of other people, 34/ banks are exceptionally risk conscious and prone to conservative short term lending strategies. If banks depart from this mold—as they did briefly in the early 1970's—the contradictions, and criticism from regulatory authorities, build up, forcing them to eventually rediscover so-called prudent banking practices. And both the variability of lending conditions and the ultimate limitations of funding from short term private deposits are in direct contradiction to the bold requirements of development which are long term in nature and function best in a stable and predictable environment. 35/

It seems fair to conclude then that the role of banks in the development finance of Peru was misplaced. While ideally suited as intermediaries of short term funds (for trade, working capital, etc), they have become mistakenly enmeshed in the overall finance of LDCs, for reasons which are not all their own. Banks clearly are not an adequate substitute for long term official finance and access to private bond markets. And in the case of Peru they have acted as a very poor substitute. Peru has suffered the consequences and undoubtedly others will.

too. Clearly the international community should be seeking alternatives to the present system of bank dominated development finance, which has evolved in an ad-hoc fashion and which functions in a manner that is counter to the needs of broad-based socio-economic development.

Chapter 8

FOOTNOTES

1. See Kuczynski, p. 52.
2. See Canal.
3. Ibid.
4. See Aronson (1977), p. 166.
5. The loan was secured by assured sales of the crude to Japan. The controversial book by Ortiz de Zavallos Roedel has published the loan contracts and petroleum purchase agreements with Japan.
6. It should be noted that Lloyds Bank, which had a branch in Lima, participated in one syndicate with a 5 million dollar loan.
7. See Kuczynski, p. 257.
8. No information has been secured on the intent or scope of the limits on external debt that may have been part of the commercial standby agreements.
9. The limits were impossible to determine because they were fixed in a document which could not be located.
10. It could be argued that an improved economic situation made conditionality unnecessary. But how improved was the situation? Better overall economic indicators to some extent were a reflection of prices on international markets and increased bank lending itself. The underlying structural problems of the balance of payments (low export coefficient) and public finance remained unresolved and actually intensified in the 1970's.
11. See Cummings.
12. For one of the more caustic evaluations of the IMF, see PAYER.
13. It can be added that the program clearly was similar to an IMF accord in one respect—when implemented it provoked public riots in the streets.
14. Conversations with C. Santistevan.

15. In the end some adversaries just simply refused to participate. (It appears that Crocker National Bank and Bancal Tristate Corp. were in this group.) However, the negative block was sufficiently small to permit the U.S. banks to go ahead with a declaration of support.
16. See Friedman, p. 53.
17. Some banks had considerable investments in the Southern Peru Copper Corp. In 1973 Chase Manhattan Bank led a 200 million dollar syndicated credit for the Cuajone project. In addition to Chase, other powerful banks such as Citicorp, Morgan Guaranty, Bankers Trust and Chemical Bank participated in the credit. Meanwhile, in 1975 Lloyds Bank headed a 23.5 million dollar syndicate to the Corporation which involved big banks such as First National Bank of Chicago, Midland Bank, and Barclays Bank, all of whom were involved in Peru's 1976 negotiations for a refinance credit. Source: the published tombstones for the respective syndicated credits.
18. It should be mentioned that a high level government official of the U.S. State Department was an ex-president of Marcona.
19. Conversations with C. Santistevan.
20. Morgan Guaranty Trust Co., May 1976, p. 9.
21. See Diaz Alejandro, pp. 188-197.
22. The concept of capacity to import used here corresponds to CEPAL's traditional definition, i.e., the amount of goods and services that can be purchased with the annual net inflow of foreign exchange resources, excluding, however, inflows of resources under the heading of compensatory capital. Thus, capacity to import can be expressed as  $Z = X + EF$  where Z is capacity to import, X is the purchasing power of exports and EF is the net flow of financial resources, exclusive of inflows of compensatory capital. For the sake of clarification,  $EF = (AI - AO - Fa) - (CO + Fc) + (N + Fn) + E$ , where AI represents foreign autonomous capital inflows; AO, foreign autonomous capital outflows; Fa, factor payments on autonomous capital; CO, outflows of foreign compensatory capital; Fc, factor payments on foreign compensatory capital; N, net movement of assets held by residents of Latin America; FN, factor receipts on national assets; and E, the net errors and omissions entry of the balance of payments. Note: national assets include government transactions; thus there is an element of double counting in the data.

23. Errors and omissions of the balance of payments has been assumed to be a capital flow.
24. At least one study has suggested that the benefits of the policies of the reform government were most heavily realized by the urban sector and middle income groups in the formal labor market. The rural sector and informal labor market were, according to the study, relatively less affected. See Couriel.
25. These data exclude state enterprises. However public terms are linked to the central government budget through transfers on the capital account. Also, data in table 3.6 of Chapter 3 suggest that external finance, and therefore banks, were important in the finance of state enterprises during the 1970's.
26. See CEPAL (forthcoming).
27. See Schydrowsky.
28. By 1974 commercial banks accounted for roughly 33 per cent of the current account finance of non-oil exporting developing countries (see Watson, table 2). But for higher income LDCs this reliance was much more severe; e.g. in the same year for Latin America commercial banks accounted for two-thirds of the current account finance (see Massad and Zahler, table 2).
29. See Couriel.
30. See Hughes pp. 95-96.
31. Taking the average of the annual average 6-month eurodollar rates plus Peru's average interest spread for the period 1973-1975 suggests a cost, grosso modo, of 10.9 per cent for credit. Over this same period consumer prices in the industrialized countries rose by roughly 10 per cent.
32. In 1975-1977 LDCs commonly encountered spreads of 2 per cent or more.
33. In 1975, 75 per cent of all eurocurrency credits to LDCs had maturities of 6 years or less. See World Bank, Supplement, EC-181, August 1976.
34. In 1976, 61 per cent of Citicorp's total deposits had an average maturity of only 90 days. See Hardy, p. 192.
35. For a more comprehensive analysis of the asymmetry between the requirements of development finance and commercial bank finance, see Devlin (1979).



## Chapter 9

### UPDATE: PERU IN THE PERIOD 1977-1979

Of course the story of Peru and its bankers did not end in 1976. The drama intensified in succeeding years and the purpose of this Chapter is to provide the reader with a very brief update of the country's interface with its commercial creditors. 1/

#### A. THE FIRST STABILIZATION EFFORTS FAILS

The full scale stabilization program instituted in mid-1976 was short lived. By the beginning of 1977 it was clear that the goals of the program could not be reached because of, among other things, strong internal resistance to cutbacks in government expenditures. Peru's private creditors, now very frightened, forced Peru to negotiate with the IMF. However, "the IMF's persistence in quantitative targets practically unrealizable in a brief period and the profound fears of the government concerning public reaction impeded the materialization of an agreement". 2/

#### B. A SECOND ATTEMPT AT STABILIZATION

Around mid-year, again under pressure from its private creditors to meet the requirements of the IMF, attempts were made at introducing new austerity measures. However, resistance to price increases of popular goods, falls in real wages, etc. was so strong that it even brought a quick demise to a recently installed economic minister. The succeeding economic team attempted to moderate the program through a slight downward adjustment in prices of some key goods. 3/ Facing a severe foreign exchange crunch,

and the general refusal of banks to finance without the IMF, the government desperately arranged swaps with Central Banks of friendly countries in Latin America and with locally domiciled foreign firms. 4/ But the foreign exchange situation was so acute that the government felt that it had no alternative but to renew negotiations with the IMF. Hanging over the heads of officials was the fact that without the green light of the Fund the banks' would refuse to extend any credit, other than perhaps last minute rollovers to avoid formal default.

After the introduction of austerity measures to show its "goodwill" to the Fund, negotiations were undertaken and an agreement was finally reached with the IMF in the last quarter of 1977 for second and third credit tranches. The targets of the program were very severe, with a high social cost, and to many totally impossible to realize. 5/ The banks remained very cautious, restricting lines of credit to local banks and remaining non-committal to the government's efforts for new finance. At the insistence of the banks, the government sought and eventually received rescheduling of its debt with the Russian government. 6/

In the beginning of 1978 the banks realized that new credit (perhaps 260 million dollars) would have to be extended if default was to be avoided and formulas were being studied to this effect. Many of the U.S. Creditors were in favor of directly tying any new loans to IMF draw-downs in the on-going standby agreement, while many European institutions did not enjoy the political implications of such a close working relationship. 7/ By this time Citicorp had resigned as head of the Steering Committees, being replaced by Manufacturers Hanover. Until a formula could be reached, short monthly rollover credits would be provided to stave off the default that neither Peru or the banks wanted to see.

In February 1978 an IMF team visited Peru to evaluate the stabilization program. It found that the standby targets were not met and questioned the local accounting methods that stated to the contrary. 8/ One of the more publicized aspects of this latter accusation was a credit extended by Dresdner Bank at the very end of December 1978—to build international reserves up to end of year target levels—followed by repayment in the first week of January.

The Fund indicated that the next disbursement of the standby agreement could not be effected because of Peru's failure to meet target arrangements. The banks—strongly pushed by U.S. institutions—formally abandoned negotiations for new credit. The crisis environment deepened, complicated by continuous strikes and demonstrations against the expanding austerity measures.

The government faced severe difficulties. The private sector was becoming increasingly hostile over the continuing shortages of foreign exchange and the tight rein foreign commercial bankers maintained on foreign lines of credit. 9/ The prospects were that by mid-May all liquid reserves would be exhausted. So the government had little choice but to begin organizing a new austerity program to present to the Fund, which by now was being characterized as "uncompromising and anachronistic".

Government authorities continued their intensive efforts to prevent default. There was talk of an effort to arrange a Paris Club rescheduling, but immediate efforts were centered on avoiding default on commercial debt. While banks like Dresdner and Nova Scotia were in favor of going ahead with a 260 million refinance credit IMF or no, the U.S. institutions—the principal creditors—rejected this outright. Citicorp even went so far as to threaten to right off its Peru exposure rather than extend credit without the IMF. 10/

Thus, without a new standby arrangement, the most Peru could expect would be very short term rollover credits that would evade technical default, but that in no way would provide relief from the financial crisis.

### C. THE THIRD ATTEMPT AT STABILIZATION

In May 1978 new austerity measures were introduced. Street riots followed and marshall law had to be introduced. Meanwhile, authorities rushed around the globe trying to seek loans to bolster the almost depleted international foreign exchange reserves. Swaps and loans were secured from friendly governments and negotiations were undertaken with commercial bankers for a 45-90 day rollover credit as a bridge to an eventual settlement with the IMF.

In the middle of this environment a scandal broke out with one of Peru's major creditors—Chase Manhattan Bank. It had headed a large syndicate to the Cuajone copper project and wanted to establish legal control over the mine's foreign exchange earnings, which were held by the Peruvian Central Bank. Chase reportedly threatened that further cooperation from Chase and other banks around the world would be dependent upon Peru's acceptance of Chase's viewpoint on the legal issue. <sup>11/</sup> Peru strongly rejected the implications of the bank's actions and public criticism at both home and abroad made Chase back down from its original stance.

The government finally entered again into negotiations with the Fund. This time it strongly demanded targets which were feasible. Meanwhile, the IMF, now more sensitive to growing world wide criticism about its overly rigid stabilization policies, took on a somewhat more flexible posture. A mutually acceptable agreement was reached.

Armed with the IMF accord, Peru called a Paris Club meeting late in the year to reschedule its official debt. It successfully obtained relief on 90% of the payments falling due in 1979 and 1980. Effectively the payments would be stretched out over seven years.

After the Paris Club accord, Peru then approached its major private bankers. The agreement reached involved the following arrangements: 12/

- a) 185 million dollars which had been rolled over for 6 months in June 1978 would be paid as scheduled in January 1979.
- b) Half of the 185 million dollars due in January would be refinanced in a new one-year loan with a 1.75% spread over libor.
- c) Ninety percent of payments due in 1979 and 1980—about 360 million dollars each year—would be refinanced in separate loans. Payments in 1979 would be rolled over until early 1980 and converted into a 7 year loan at 1.875% over libor. Payments in 1980 would be rolled over until early 1981 and converted into a new 6 year loan at an interest rate to be determined just before authorization of the credit.

The commercial bank relief was qualitatively different than that provided by official lenders. While the rescheduling agreement effectively provided a committed 2-year restructuring of payments, the banks' refinance credits were a year-by-year relief operation. This very "short leash" approach would give the commercial institutions more leverage over government policy as there effectively would be a multi-staged (as opposed to one) approval process for relief.

#### D. THE UNCERTAIN FUTURE

The year 1979 opened with a problematic outlook. With the refinance accord of late 1978 Peru received its first real relief in payments to the banks since 1976. However, amortization was assuaged for only two years, leaving prospects for another big bulge in payments as early as 1981. Aside from the uncertainty surrounding the obviously stop-gap nature of the assistance provided by the banks (as well as official lenders), the pell-mell direction of events in the post-1975 economic crisis was very costly to an already poor economy. As Peru raced back and forth between its private bankers and the IMF in order to reconcile national objectives with the demands of foreign creditors, it suffered sharp and unaffordable setbacks in its economic development. Not only were projects halted or cutback (e.g. exploration of jungle petroleum), but there were sharp falls in per capita income (see table 9.1). Wages and salaries underwent serious deterioration and formal unemployment rose to alarming heights. Domestic unrest over prolonged austerity measures continued to be manifest. Meanwhile, after 6 years of continuing price increases by OPEC, international economic recession and stagflation, the world community still had not developed the needed alternative to commercial banks for the transfer of resources from surplus to deficit countries. Consequently, as of mid-1979 Peru's recovery from the effects of its full scale incursion into the world of commercial bank loans remained somewhat problematical.

Table 9.1

PERU: SELECTED ECONOMIC INDICATORS, 1976-1978

(Rates of growth)

	1976	1977	1978
Gross domestic product (1970 dollars)	3.0	-1.2	-1.8
Gross domestic product per capita	0.2	-3.9	-4.5
Unemployment (percentage)	8.4	9.4	9.8
Real wages <u>a/</u>	16.6	-23.5	-9.0
Real salaries <u>b/</u>	-1.3	-23.7	-14.1

Source: CEPAL, Economic Survey of Latin America 1978, Santiago, Chile.

a/ Blue collar

b/ White collar

FOOTNOTES

Chapter 9

1. For a rather detailed account of the economic stabilization effort of this period see Humberto Cabrera.
2. Ibid, p. 53 (author's translation)
3. Ibid, p. 54
4. See Moreyra, p. 95
5. For details of the program see Humberto Cabrera, pp. 55-60 and Moreyra, p. 95
6. U.S. banks feared that unless there was a rescheduling, any new loans by them would appear as indirect payment of Russian debt. See Andean Report (February 1978), pp. 22-23.
7. Ibid, p. 22
8. Andean Report (February 1978), p. 23.
9. Many local bankers were impressed by Manufacturers Hanovers' behavior during the crisis. It apparently stood out for a flexible and reasonable approach to the approval of foreign exchange lines of credit.
10. See Andean Report (April 1978), p. 63
11. See Andean Report (May 1978), p. 84 and Latin American Economic Report (May 1978), p. 154.
12. Sources are the Central Bank (1978) pp. 48-49 and unpublished data provided by the editors of the Andean Report.



Annex 1

NAMES OF BANKS IN THE STUDY

United States

1. American Express International Banking Corporation
2. Bancal Tri-State Corporation
3. Bank America Corporation
4. Bankers Trust Corporation
5. Centran Corporation
6. C.I.T. Financial Corporation
7. Citicorp
8. Citizens & Southern National Bank
9. Cleveland Trust Corporation
10. Commerce Union Bank
11. Continental Illinois Corporation
12. Crocker National Corporation
13. Charter New York Corporation
14. Chase Manhattan Corporation
15. Chemical New York Corporation
16. Fidelcor Incorporated
17. First Bank System Incorporated
18. First Chicago Corporation
19. First National Bank of Boston
20. First National Bank of St. Louis
21. First National State Corporation
22. First Pennsylvania Corporation
23. Franklin National Bank (went bankrupt in 1974)
24. Girard Company
25. Harris Bank Corporation Incorporated
26. Hartford National Corporation

27. Industrial National Corporation
28. La Salle National Bank of Chicago
29. Manufacturers Hanover Corporation
30. Marine Midland Banks Incorporated
31. Morgan Guaranty Trust Co.
32. National Detroit Corporation
33. Northern States Bancorporation
35. Rainier Bancorporation
36. Republic of Texas Corporation
37. Seafirst Corporation
38. Security Pacific Corporation
39. Shawmut Corporation
40. Union Planters National Bank
41. Wells Fargo and Co.
42. Western Bancorporation

Japan

1. Associated Japanese Bank (International) Ltd.\*
2. Bank of Tokyo Ltd.
3. Bank of Yokohama
4. Banque Europeenne de Tokyo S. A.\*
5. Dai-Ichi Kangyo Bank Ltd.
6. Daiwa Bank Ltd.
7. Fuji Bank Ltd.
8. Hokkaido Takushaku Bank
9. Hokuriku Bank
10. Industrial Bank of Japan Ltd.
11. Japan International Bank Ltd.
12. Kyowa Bank Ltd.

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\* Wholly Japanese consortium.

13. Long Term Credit Bank of Japan
14. Mitsubishi Bank Ltd.
15. Mitsubishi Trust & Banking Corporation
16. Mitsui Bank Ltd.
17. Mitsui Trust & Banking Corporation
18. Nippon Credit Bank Ltd.
19. Nomura Securities Company Ltd.
20. Saitama Bank Ltd.
21. Sanwa Bank Ltd.
22. Sumitomo Bank
23. Taiyo Kobe Bank Ltd.
24. Tokai Bank Ltd.
25. Toyo Trust & Banking Co. Ltd.
26. Yasuda Trust & Banking Co.

Canada

1. Bank of Montreal
2. Bank of Nova Scotia
3. Banque Canadienne Nationale
4. Canadian Imperial Bank of Commerce
5. Royal Bank of Canada
6. Toronto Dominion Bank

United Kingdom

1. Antony Gibbs & Sons Ltd.
2. Belfour & Williamson
3. Barclays Bank Ltd.
4. Grindlays Bank Ltd.
5. Hambros Bank Ltd.
6. Industrial Multinational Investment Ltd.

7. Lloyds Bank Ltd.
8. Midland Bank Group
9. National & Commercial Banking Group Ltd.
10. National Westminster Bank Ltd.
11. Schroders Ltd.

Germany

1. Allgemeine Deutsche Credit Anstalt A. G.
2. Bank Fur Gemeinwirtschaft A. G.
3. Bankhaus Hermann Lampe K. G
4. Bayerische Hypotheken und Wechselbank
5. Berliner Handels-und-Frankfurter Bank
6. Commerzbank A. G.
7. D. G. Bank Deutsche Genossenschaftsbank
8. Deutsche Bank
9. Dresdner Bank
10. Norddeutsche Landesbank Gironzentrale
11. Westdeutsche Landesbank Gironzentrale

France

1. Banque de l'Indochine et de Suez
2. Banque Francaise du Commerce Exterieur
3. Banque Nationale de Paris
4. Banque Wormes
5. Compagnie Financiere de Paris et des Pays-Bas
6. Credit du Nord
7. Credit Lyonnais
8. Societe Generale

Italy

1. Banca Commerciale Italiana Ltd.
2. Banca Nazionale del Lavoro
3. Banco Ambrrosiano
4. Banco di Roma
5. Banco Nazionale dell'Agricoltura
6. Credito Italiano
7. Euramerica International Bank Ltd.
8. Italian International Bank Ltd. \*

Switzerland

1. Bank Lev A. G.
2. Dow Banking Corporation
3. Privatbank & Verwaltungsgesellschaft
4. Swiss Bank Corporation
5. Swiss Credit Bank
6. Swiss Volksbank
7. Union Bank of Switzerland

Consortium

1. Asian & Euro-American Merchant Bank Ltd. (Singapore)
2. Atlantic International Bank Ltd. (United Kingdom)
3. Banque Arabe et Internationale d'Investissement (France)
4. Banque Continentale du Luxembourg (Luxembourg)
5. Banque de la Societé Financiere Europeenne (France)

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\* Wholly Italian Consortium banks.

6. Banque de l'Union Europeenne (France)
7. Banque Europeenne de Credit S. A. (Belgium)
8. Euro Latin American Bank Ltd. (United Kingdom)
9. European American Bankcorporation (United States)
10. European Brazilian Bank Ltd. (United Kingdom)
11. Inter Union Banque (France)
12. International Commercial Bank Ltd. (United Kingdom)
13. International Mexican Bank Ltd. (United Kingdom)
14. Iran Overseas Investment Bank (United Kingdom)
15. Krediet Bank N. . (Belgium)
16. Libra Bank Ltd. (United Kingdom)
17. London and Continental Bankers Ltd. (United Kingdom)
18. Midland & International Banks Ltd. (United Kingdom)
19. Morgan Guaranty & Partners Ltd. (Singapore)
20. Nippon European Bank S. A. (Belgium)
21. Orion Bank Ltd. (United Kingdom)
22. UBAF Bank Ltd. (United Kingdom)
23. United International Bank (United Kingdom)
24. Western American Bank Ltd. (United Kingdom)

Other Locations

1. Algemene Bank Nederland N. V (Holland)
2. Amsterdam Rotterdam Bank (Holland)
3. Banco Atlantico (Spain)
4. Banco de Bogota (Colombia)
5. Banco de Santander (Spain)
6. Banco do Brasil (Brasil)
7. Banco Hispano Americano (Spain)
8. Banco Melli (Iran)

9. Banco Mexicano S. A. (Mexico)
10. Banco Nacional de Panama (Panama)
11. Banco Popular Español (Spain)
12. Banco Urquijo (Spain)
13. Banque de Bruxelles Lambert (Belgium)
14. Banque Commerciale pour L'Europe du Nord (U.S.S.R)
15. Banque Internationale a Luxembourg (Luxembourg)
16. Comco International Bank (Luxembourg)
17. Commercial Bank of Kuwait (Kuwait)
18. Liberal Bank (Berirut)
19. L.T.C.B Asia Ltd. (Hong Kong)
20. Osterreichische Landerbank A. G. (Austria)
21. Skandinaviska Enskilda Banken (Sweden)
22. Trade Development Bank Holding S. A. (Luxembourg)
23. Trade Invest Bank & Trust Co. (Bahamas)

Unclassified

1. Guaranty & Credit
2. Pan American Credit Corporation
3. Rothchild Intercontinental Bank Ltd.
4. Wellington Overseas

Annex 2

STATISTICAL APPENDIX

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Table A3.1

## PERU: A SELECTED LIST OF NATIONALIZATIONS/PERUVIANIZATIONS OF FOREIGN FIRMS, 1968-1975

Local foreign firm	Foreign parent	Owners' nationality	Nature of operations in Peru	Initial date of takeover	Bank ties (where known or suspected)
1. W.R. GRACE	-	United States	Sugar estates Fishmeal Chemicals Paper	1969 1973 ... ...	CITIBANK: held 11% of the long-term debt of the company and had two representatives on the board. <sup>a/</sup> Meanwhile, GRACE has had a long history of membership on CITIBANK's board of directors. <sup>b/</sup> Morgan Guaranty: May have been an important lender. <sup>c/</sup>
2. Cerro de Pasco	-	United States	Mining Cattle raising	1973 1969	Morgan Guaranty: Cerro reportedly under the control of Chase Manhattan; Newmont Mining Corp. and American Metal Climax. The former is under the influence of the Morgan group and the Rockefeller group. <sup>d/</sup> CITIBANK: Possibly important lender. <sup>e/</sup>
3. International Petroleum Company	Standard Oil of New Jersey	United States	Petroleum extraction and refining	1968	Chase Manhattan Bank: The Chase group had suspected control of the parent through historical relationship and ownership of voting stock. <sup>f/</sup> Morgan Guaranty: May have been important lender to the parent. <sup>g/</sup>
4. Marcona Mining Company	Utah Construction and Mining Corp.	United States	Mining	1975	... ..
5. Peruvian Telephone Company	ITT	United States	Telephone Company	1969	Lazard Freres and Co: Representatives on the executive committee of the firm. <sup>h/</sup> Kuhn Loeb and Co.:
6. H.J. Heinz; Cargill; Ralston Purina; W.R. GRACE (see No 1) Gold Kist; Ferrostal; Taiyo Fishing, Et Al		United States (65.0%) England (6.6%) France (5.7%) Japan (4.7%) Swiss (3.9%) Other (14.9%)	Fishing industry	1973	Bank of America: The former may have been an important lender to Heinz and the latter an important lender to Ralston Purina. <sup>i/</sup>

Table A3.1 (continued)

Local foreign firm	Foreign parent	Owners' nationality	Nature of operations in Peru	Initial date of takeover	Bank ties (where known or suspected)
7. Empresas Eléctricas Asociadas and Energía Eléctrica Andina, S.A.	...	Switzerland	Electric power	1971	...
8. Cementos Lima	...	Switzerland	Cement	1971	Holder Bank Financiera Glarus S.A.: Shareholder through Sindicato de Inversiones y Administración S.A. <u>k/</u>
9. Banco Continental	Chase Manhattan Bank	United States	Banking	1970	...
10. Banco de Crédito	Banque Française et Italienne pour L'Amérique del Sud	Italian-French	Banking	1970-71 <sup>l/</sup>	Banca Commerciale Italiana: Parent is owned by these banks. <sup>m/</sup> Banque de L'Indochine et de Suez:
11. Banco de Lima	Credit Lyonnais	French	Banking	1970-71 <sup>n/</sup>	...
12. General Motors	...	United States	Automobiles	1969 <sup>o/</sup>	Morgan Guaranty: Each bank had two representatives on the board in 1969. <sup>p/</sup> Manufacturers Hanover: May have been an important lender. <sup>q/</sup>
13. ANACONDA	...	United States	Mining	1969 <sup>r/</sup>	Chase Manhattan: Chase held 12% and Citibank 11% of company's long term debt. Each had a representative on the board. <sup>s/</sup>
14. Kaiser Aluminum	...	United States	Mining	1969 <sup>t/</sup>	Bank of America: May have been an important lender. <sup>u/</sup>
15. Banco Internacional	Chemical Bank; W.R.GRACE, <u>et al</u>		Banking	1970 <sup>v/</sup>	...

Table A3.1 (conclusion)

Note: Data in Kotz study refer to the period 1967-1969. Data in Cohen study refer to primary and secondary lenders (both international and domestic) to TNCs over the period 1973-1976. Data should be used with great caution and are meant to be only suggestive of possible links. Also, information is relevant only to the extent that the links were in effect at time that crucial action was taken on the firm by the Government of Peru.

- a/ Kotz, p. 168.
- b/ NACLA (March 1976), pp. 8-10.
- c/ Cohen, attachment 5.
- d/ Malpica, p. 180.
- e/ See footnote C
- f/ Kotz, p. 188.
- g/ See footnote C
- h/ Kotz, p. 163.
- i/ Distribution of value of foreign shares, See Ministry of Fishing - OSP, p. 134.
- j/ See footnote C
- k/ Information obtained from field research.
- l/ Ownership reduced from 62% to 20%.
- m/ Banker Research Unit (1977)
- n/ Participation reduced to less than 20%.
- o/ Production license revoked.
- p/ Kotz, p. 179.
- q/ See footnote C
- r/ Lost mining concession.
- s/ Kotz, p. 176.
- t/ Lost mining concession.
- u/ See footnote C
- v/ Bought by government.



Table A 4.2

PERU: AVERAGE INTEREST RATES ON CREDIT AUTHORIZED BY OFFICIAL INSTITUTIONS, 1965-1976

(Percentages)

	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976
A. Multilateral finance	5.54	3.20	3.47	3.47	2.25	4.98	2.59	3.00	6.36	6.94	4.58	7.08
1. Development finance												
1.1 IBRD	5.50	6.00	-	-	-	7.25	-	-	7.25	7.25	-	8.56
1.2 IDB	6.00	2.65	3.47	3.47	2.25	3.43	2.59	3.00	3.97	6.68	2.00	5.05
1.3 Andean Development Corp.	-	-	-	-	-	-	-	-	-	7.67	7.94	-
2. Compensatory finance												
2.1 IFF	-	-	2.00	2.00	2.00	2.00	2.00	2.00	2.00	2.00	2.00	5.30
2.2 Other	-	-	-	-	-	-	-	-	-	-	-	-
B. Bilateral finance	2.88	3.35	4.37	5.82	5.14	7.29	6.71	4.31	4.69	6.22	5.09	3.15
1. United States	2.65	3.09	3.63	2.12	-	6.00	6.88	2.95	5.71	7.29	10.28	7.33
1.1 Eximbank	-	6.00	6.00	-	-	6.00	-	-	-	-	-	8.40
1.2 AID	1.80	2.12	2.12	2.12	-	-	2.75	2.75	-	2.75	-	2.75
1.3 Commodity credit corp.	-	-	-	-	-	-	6.13	6.13	6.13	10.40	10.20	9.00
1.4 Other	5.00	5.00	-	-	-	-	8.00	-	-	7.07	10.00	8.00
2. Western Europe												
2.1 France	-	-	-	5.00	-	8.78	-	-	3.50	-	3.85	-
2.2 United Kingdom	-	6.50	-	8.00	-	-	-	-	-	6.00	3.00	2.94
2.3 Germany	3.00	-	-	6.17	-	-	-	-	2.00	-	4.58	2.00
2.4 Netherlands	-	-	6.50	-	-	-	6.50	6.50	4.47	6.50	2.50	6.31
2.5 Spain	-	-	-	7.50	-	8.00	-	7.00	-	7.50	-	-
2.6 Other	-	-	8.50	8.00	-	9.00	-	2.00	-	8.50	1.61	5.16
3. Japan	-	-	-	-	-	-	-	5.50	3.50	6.35	-	-
4. Centrally planned economies												
4.1 Union of Soviet Socialist Republics	-	-	-	-	-	-	-	-	2.00	2.00	2.00	2.02
4.2 Hungary	-	-	-	-	-	-	6.00	2.83	6.00	-	3.67	6.00
4.3 Other	-	-	-	-	-	-	7.34	8.75	-	-	2.00	0.04
5. Canada	-	-	-	-	5.14	6.82	6.38	7.25	6.85	7.63	6.97	8.37
6. Other	-	-	-	-	-	6.06	6.62	6.39	-	6.83	7.81	-
<u>Total</u>	<u>4.69</u>	<u>3.23</u>	<u>4.09</u>	<u>5.03</u>	<u>3.17</u>	<u>5.95</u>	<u>5.62</u>	<u>4.24</u>	<u>5.20</u>	<u>6.28</u>	<u>5.02</u>	<u>4.32</u>

Source: CEPAL on the basis of official data.

Table A 4.3

PERU: AVERAGE GRACE PERIOD ON CREDIT AUTHORIZED BY OFFICIAL INSTITUTIONS, 1965-1976

( years )

	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976
A. Multilateral finance	4.79	3.66	3.23	3.75	4.00	7.79	4.50	4.50	7.37	5.35	5.65	4.83
1. Development finance												
1.1 IBRD	5.12	5.00	-	-	-	10.00	-	-	7.69	5.00	-	3.86
1.2 IDB	2.00	3.40	3.23	3.75	4.00	6.28	4.50	4.50	6.52	5.63	7.50	6.17
1.3 Andean Development Corp.	-	-	-	-	-	-	-	-	-	2.98	3.24	-
2. Compensatory finance												
2.1 IMF	-	-	-	-	-	-	-	-	-	-	-	-
2.2 Other	-	-	-	-	-	-	-	-	-	-	-	-
B. Bilateral finance	7.44	7.30	6.26	3.84	1.34	2.31	1.98	3.78	3.92	4.09	1.97	2.05
1. United States	7.31	7.55	6.87	10.00	-	3.50	2.50	3.83	0.93	3.93	1.42	3.72
1.1 Eximbank	-	1.33	2.00	-	-	3.50	-	-	-	-	-	3.64
1.2 AID	10.00	10.00	10.00	10.00	-	-	10.00	10.00	-	10.00	-	10.00
1.3 Commodity Credit Corp.	-	-	-	-	-	-	1.00	1.00	1.00	1.00	1.00	1.00
1.4 Other	-	-	-	-	-	-	3.00	-	-	0.91	2.00	2.00
2. Western Europe												
2.1 France	-	-	-	2.50	-	2.00	-	-	1.00	-	2.76	-
2.2 United Kingdom	-	4.00	-	4.00	-	-	-	7.00	-	5.50	3.75	4.55
2.3 Germany	7.50	-	-	3.00	-	-	-	-	10.50	-	5.73	10.00
2.4 Netherlands	-	-	4.00	-	-	-	3.50	3.59	5.24	4.50	8.00	5.96
2.5 Spain	-	-	-	2.00	-	2.00	-	2.00	-	5.50	-	-
2.6 Other	-	-	3.00	2.00	3.00	2.00	-	5.00	-	5.50	9.06	5.30
3. Japan	-	-	-	-	-	-	-	5.00	7.00	4.50	-	-
4. Centrally planned economies												
4.1 Union of Soviet Socialist Republics	-	-	-	-	-	-	-	-	1.50	1.50	1.49	1.32
4.2 Hungary	-	-	-	-	-	-	2.00	0.95	0.50	-	0.66	-
4.3 Other	-	-	-	-	-	-	2.00	1.00	-	-	0.50	5.90
5. Canada	-	-	-	-	0.85	1.42	1.00	3.00	2.10	3.78	3.09	1.57
6. Other	-	-	-	-	-	3.39	0.67	0.87	-	2.76	2.18	-
<u>Total</u>	<u>5.63</u>	<u>4.48</u>	<u>5.33</u>	<u>3.81</u>	<u>2.57</u>	<u>5.50</u>	<u>2.65</u>	<u>3.82</u>	<u>4.98</u>	<u>4.20</u>	<u>2.46</u>	<u>2.88</u>

Source: CEPAL on the basis of official data.



Table A 4.4

PERU: AVERAGE AMORTIZATION PERIOD ON CREDIT AUTHORIZED BY OFFICIAL INSTITUTIONS <sup>a/</sup>

(years)

	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976
A. Multilateral finance	15.73	22.40	19.94	17.45	26.00	20.75	18.82	15.50	14.86	17.56	15.43	17.01
1. Development finance												
1.1 IBRD	16.41	20.00	-	-	-	20.00	-	-	13.48	20.00	-	18.29
1.2 IDB	10.00	22.88	19.94	17.45	26.00	21.26	18.82	15.50	18.57	16.24	22.50	15.25
1.3 Andean Development Corp.	-	-	-	-	-	-	-	-	-	5.98	6.22	-
2. Compensatory finance												
2.1 IMF	-	-	4.00	4.00	4.00	4.00	4.00	4.00	-	-	-	4.00
2.2 Other	-	-	-	-	-	-	-	-	-	-	-	-
B. Bilateral finance	17.92	22.77	18.49	9.21	8.37	5.22	9.84	11.59	9.91	9.26	7.64	10.85
1. United States	25.29	25.46	21.41	30.00	-	3.50	13.81	10.82	2.03	12.00	3.47	8.86
1.1 Eximbank	-	6.17	8.00	-	-	3.50	-	-	-	-	-	3.09
1.2 AID	30.00	30.00	30.00	30.00	-	-	30.00	30.00	-	30.00	-	30.00
1.3 Commodity credit corp.	-	-	-	-	-	-	2.00	2.00	2.00	2.00	2.00	2.00
1.4 Other	5.00	5.00	-	-	-	-	22.00	-	2.50	6.99	5.50	5.50
2. Western Europe												
2.1 France	-	-	-	3.50	-	3.97	-	-	13.00	-	15.30	-
2.2 United Kingdom	-	14.00	-	14.00	-	-	-	25.00	-	9.50	20.50	20.09
2.3 Germany	15.00	-	-	6.04	-	-	-	-	19.50	-	15.06	20.00
2.4 Netherlands	-	-	12.00	-	-	-	12.00	13.61	14.91	15.50	22.00	15.87
2.5 Spain	-	-	-	4.00	-	5.00	-	1.50	-	9.50	-	-
2.6 Other	-	-	1.00	4.00	14.50	4.00	-	24.50	-	9.50	19.22	8.45
3. Japan	-	-	-	-	-	-	-	13.52	18.00	9.50	-	-
4. Centrally planned economies												
4.1 Union of Soviet Socialist Republics	-	-	-	-	-	-	-	-	10.00	10.00	9.92	11.30
4.2 Hungary	-	-	-	-	-	-	6.50	10.26	6.50	-	7.75	3.50
4.3 Other	-	-	-	-	-	-	8.00	3.00	-	-	11.67	9.04
5. Canada	-	-	-	-	6.54	3.83	2.00	9.00	6.11	6.63	10.46	2.61
6. Other	-	-	-	-	-	8.90	4.65	1.70	-	7.28	1.87	-
<u>Total</u>	<u>16.43</u>	<u>22.49</u>	<u>18.93</u>	<u>11.97</u>	<u>16.53</u>	<u>14.25</u>	<u>12.20</u>	<u>11.81</u>	<u>11.43</u>	<u>10.01</u>	<u>8.68</u>	<u>12.67</u>

Source: CEPAL on the basis of official data.



Table A 4.6  
PERU: AVERAGE INTEREST COSTS OF AUTHORIZED SUPPLIER CREDITS, 1965-1976  
(Percentages)

	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976
<u>Supplier credits</u>												
1. United States	7.24	5.92	9.06	6.80	-	6.00	-	7.78	7.22	6.14	9.00	-
2. Western Europe												
2.1 Germany	7.17	-	7.24	6.82	6.53	6.67	-	6.92	8.00	7.66	8.50	8.70
2.2 United Kingdom	6.00	-	6.00	5.91	5.28	6.97	4.74	7.53	5.00	7.74	8.50	8.48
2.3 Spain	-	5.49	6.00	-	8.00	7.00	7.00	8.00	6.50	9.85	9.85	-
2.4 France	6.19	8.50	6.30	-	6.27	6.85	7.53	7.50	7.50	9.19	-	8.83
2.5 Finland	-	6.00	8.32	-	-	-	-	-	-	-	8.00	-
2.6 Sweden	-	-	-	-	-	-	-	-	7.96	-	-	8.07
2.7 Italy	-	6.54	6.53	-	6.52	9.25	-	7.00	3.59	1.98	9.25	7.00
2.8 Other	7.10	7.51	8.90	-	8.43	5.46	7.75	7.40	7.68	8.70	10.05	9.22
3. Japan	7.00	8.20	-	6.50	-	-	-	7.15	-	-	-	7.50
4. Centrally planned economies												
4.1 Yugoslavia	-	-	-	-	-	-	6.50	7.00	7.50	7.36	-	-
4.2 Union of Soviet Socialist Republics	-	-	-	-	-	-	-	-	3.00	3.00	4.49	4.50
4.3 Other	-	-	-	-	-	-	-	7.02	-	-	11.00	-
5. Canada	-	-	6.50	-	7.90	7.90	-	7.90	-	-	-	-
6. Mexico	-	-	-	-	-	-	-	-	-	-	-	8.68
7. Other	-	9.00	8.00	-	-	7.00	7.00	7.08	7.00	-	4.06	8.64
<u>Total</u>	<u>6.85</u>	<u>6.26</u>	<u>6.89</u>	<u>6.67</u>	<u>7.03</u>	<u>6.94</u>	<u>6.51</u>	<u>7.27</u>	<u>4.82</u>	<u>7.62</u>	<u>6.11</u>	<u>6.94</u>

Source: CEPAL on the basis of official data.

Table A 4.7  
 PERU: AVERAGE GRACE PERIOD ON AUTHORIZED SUPPLIER CREDITS  
 ( years )

	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976
<u>Supplier credits</u>												
1. United States	0.99	1.22	1.00	2.62	-	3.50	1.00	1.99	5.19	0.37	1.73	-
2. Western Europe												
2.1 Germany	0.77	-	1.32	0.98	0.99	0.09	-	1.23	0.72	1.42	0.39	0.10
2.2 United Kingdom	0.50	-	1.00	1.67	0.95	-	-	0.94	2.00	1.76	0.50	1.62
2.3 Spain	-	1.26	2.00	-	0.50	0.50	0.50	0.50	0.50	0.50	0.50	-
2.4 France	0.30	0.50	2.12	-	0.66	2.00	0.54	1.00	1.37	1.34	-	0.37
2.5 Finland	-	-	0.91	-	-	-	-	-	-	-	3.00	-
2.6 Sweden	-	-	-	-	-	-	-	-	0.50	-	-	2.43
2.7 Italy	-	4.33	3.00	-	1.46	2.00	-	1.47	1.67	1.79	-	0.83
2.8 Other	-	0.58	-	-	0.43	0.54	2.00	0.76	1.78	1.37	1.04	1.00
3. Japan	2.00	1.94	-	2.00	0.50	-	-	2.79	0.50	-	-	1.00
4. Centrally planned economies												
4.1 Yugoslavia	-	-	-	-	-	-	5.00	1.00	2.00	4.56	-	-
4.2 Union of Soviet Socialist Republics	-	-	-	-	-	-	-	-	1.00	1.00	-	0.50
4.3 Others	-	-	-	-	-	-	-	2.48	-	-	2.50	-
5. Canada	-	-	0.50	-	1.00	1.00	-	1.00	-	-	-	-
6. Mexico	-	-	-	-	-	-	-	-	-	-	-	2.17
7. Other	-	1.00	0.50	-	-	0.50	3.00	0.89	2.50	-	1.98	0.92
<u>Total</u>	<u>1.01</u>	<u>2.87</u>	<u>1.97</u>	<u>2.22</u>	<u>0.99</u>	<u>0.52</u>	<u>3.69</u>	<u>2.08</u>	<u>1.58</u>	<u>2.64</u>	<u>1.41</u>	<u>1.67</u>

Source: CEPAL on the basis of official data.

Table A 4.8

PERU: AVERAGE AMORTIZATION PERIOD ON AUTHORIZED SUPPLIER CREDITS

( YEARS )

	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976
<u>Supplier credits</u>												
1. United States	2.78	5.21	5.35	6.53	-	3.50	2.00	4.02	3.02	1.24	4.85	-
2. Western Europe												
2.1 Germany	7.77	-	4.11	4.53	3.61	5.66	-	3.82	6.50	3.76	1.14	4.58
2.2 United Kingdom	3.50	-	4.00	4.50	4.90	2.93	3.70	4.00	4.50	4.24	4.50	4.50
2.3 Spain	-	9.87	3.00	-	4.50	4.00	4.50	4.50	2.50	4.50	4.50	-
2.4 France	6.22	4.50	6.24	-	3.59	4.65	4.46	5.00	5.73	5.61	-	5.31
2.5 Finland	-	12.00	10.22	-	-	-	-	-	-	-	8.50	-
2.6 Sweden	-	-	-	-	-	-	-	-	6.50	-	-	7.30
2.7 Italy	-	10.79	9.84	-	8.76	8.00	-	5.65	11.77	2.81	5.00	3.73
2.8 Other	7.00	6.58	4.76	-	1.58	3.56	7.00	2.15	7.22	5.99	6.72	4.36
3. Japan	6.00	5.91	-	8.00	2.50	-	-	9.04	0.50	-	-	1.50
4. Centrally planned economies												
4.1 Yugoslavia	-	-	-	-	-	-	9.50	3.50	2.50	10.75	-	-
4.2 Union of Soviet Socialist Republics	-	-	-	-	-	-	-	-	8.76	6.53	4.52	4.50
4.3 Other	-	-	-	-	-	-	-	9.41	-	-	0.50	-
5. Canada	-	-	4.50	-	10.00	8.00	-	1.00	-	-	-	-
6. Mexico	-	-	-	-	-	-	-	-	-	-	-	6.05
7. Other	-	1.00	5.00	-	-	4.50	8.00	3.32	8.00	-	5.50	7.44
<u>Total</u>	<u>6.26</u>	<u>10.00</u>	<u>12.16</u>	<u>6.24</u>	<u>7.74</u>	<u>5.67</u>	<u>8.19</u>	<u>6.37</u>	<u>9.58</u>	<u>7.42</u>	<u>5.45</u>	<u>5.38</u>

Source: CEPAL on the basis of official data.

Table A 5.1

PERU: COMMERCIAL BANK LENDING ACCORDING TO AMOUNTS AUTHORIZED, 1965-1970<sup>a/</sup>

(Millions of dollars)

0-5.9	6-14.9	15-24.9	25-34.9	35-44.9	45-54.9
Guaranty and Credit	Nat. Detroit Corp.	Bank of N. Scotia	Bank of America	Chase Manhattan	Citibank
Schroders	Charter N.Y. Corp.			Continental Ill.	Bankers Trust
Phil. National	1 <sup>st</sup> National Boston				Manufacturers Hanover
Western Bankcorp.	Crocker National				
B. Commerciale Italiana	Franklin National				
Morgan Guaranty					
Wellington Overseas					
Westdeutsche Landesbank					
Girozentrale					
Banque L'Union Europeenne					
Panamerican Credit					
Midland and Int. Bank					
Bank of Tokyo					
Royal Bank of Canada					
Toronto Dominion Lloyds					
Bank					

Source: CEPAL, on the basis of official data.

<sup>a/</sup> Includes credits guaranteed by export credit agencies.

PERU: COMMERCIAL BANK LENDING ACCORDING TO AMOUNT AUTHORIZED, 1971-1976<sup>a/</sup>

(Millions of dollars)

< 16	≥ 16 and < 41	≥ 41 and < 68	≥ 68 and < 95	≥ 95 and < 123	≥ 123 < 150
Schroders Ltd.	Banca Commerciale Italiana	Bank of Nova Scotia	Chase Manhattan	Bank of America	Citicorp
Nat. Detroit Corp.	Bank of Tokyo	Bankers Trust		Manufacturers Hanover	
Phil. National Bank	Lloyds Bank	Continental Illinois		Wells Fargo	
Western Bancorporation	Franklin National Bank	Morgan Guaranty			
Westdeutsche Landesbank	National and Commercial Banking Group Ltd.	Crocker National			
Girozentrale		Royal Bank of Canada			
Charter N.Y. Corp.	Banca Tristate Copp.	Toronto Dominion Bank			
First Nat. Boston	Banca Nazionale de Lavarò	Dresdner			
Banque L'Union		Banco do Brasil			
Europeenne	Credit Lyonnais				
Midland and Int. Bank Ltd.	Banque Francais du Comm. Exterieur				
Swiss Bank Corp.	Canadian Imperial Bank of Commerce				
Swiss Credit Corp.	Fuji Bank Ltd.				
Swiss Volksbank	Amro Bank				
Marine Midland Bank	First Pennsylvania Corp.				
First Bank System Inc.	Deutsche Bank				
Midland Bank Group	Bank of Montreal				
Associated Japanese Bank Ltd.	Commerzbank A.G.				
Tokai Bank	Chemical Bank				
Banque Continental du Luxembourg	First Chicago Corp.				
Banque Europeenne de Tokyo	Security Pacific Corp.				
Banque Internationale a Luxembourg	Union Bank of Switzerland				
Bayerische Hypotheken Interunion Banque	Long Term Credit Bank of Japan				
Banque Nationale de Paris	American Express				
Societe Generale					
Banque Commerciale Pour L'Europe du Nord					
Banque Indochine Et De Suez					
Industrial National Corp.					
Japan Int. Bank Ltd.					
Libra Bank Ltd.					
CIT Financial Corp.					
Atlantic Int. Bank Ltd.					
Euroamerican Int. Bank					
FIDELCOR					
Italian International Bank					
Mitsubishi Trust Ltd.					
Sanwa Bank					
Anthony Gibbs and Sons					
Banco de Santander					
Mitsui Bank Ltd.					

Dai-Ichi Kangyo Bank	Comco International Bank
Seafirst Corp.	First National State Bank Corporation
Shanugi Corp.	Harris Bancorporation
Algemene Bank Nederland	LTCB Asia Ltd.
Balfour and Williamson	Western American Bank Ltd.
Commerce Union Bank	Banque de la Societe Financiere
Girard Company	Europeenne
Kyowa Bank	Asian and Euroamerican Bank Ltd.
Republic of Texas Corp.	Banque Arabe Et Internationale
European Brazilian Bank Ltd.	D'Investissement
Hokkaido Takushoku Bank	Banco Nazionale Dell'Agricoltura
International Commercial Bank Ltd.	International Mexican Bank Ltd.
Nippon Credit Bank	Trade Invest Bank and Trust Co.
United International Bank	Trade Development Bank Holding
Yasuda Trust and Banking Co.	Barclays Bank
Taiyo Kobe Bank	Banco Atlantico S.A.
Centraal Corp.	Banco Di Roma
Banco Ambrosiano	Banco Hispanoamericana
Commercial Bank of Kuwait	Banco Urquijo
Credit Du Nord	Banco Melli
Hartford National Corp.	Banque De Bruxelles Lambert
Industrial Bank of Japan	Berliner Handels-und Frankfurter
Kredit Bank N.V.	Bank
La Salle National Bank	Citizen and Southern National Bank
Mitsubishi Bank Ltd.	Iran Overseas Investment Bank
Mitsui Trust and Banking Co.	Nordeutsche Landesbank Girozentrale
Orion Bank Ltd.	Banco Nacional de Panama
Rothschild Int.	Skandinaviska Enskilpa Banken
Saitama Bank	Banco de Bogotá
Sumitomo Bank	Banque Europeene de Credit S.A.
Union Planters National Bank	Eurolatin American Bank Ltd.
Daiwa Bank	Banco Popular Español
Grindlay's Bank	First National Bank of St. Louis
Credito Italiano	UBAF Bank Ltd.
Nomura Securites Co.	Bank Lew A.G.
Compagnie Financiere de Paris	Privat Bank and Verwaltungsgesellschaft
Et Pays Bas	Bank Fur Gemeinwirtschaft A.G.
European American Bancorporation	Bankhaus Hermann Lampe
Northern States Bancorporation	Hambros Bank
Banco Mexicano	Industrial Multinational Investment Corp.
National Westminster Bank	Nippon European Bank
D.G. Bank	Osterreichische Landerbank A.G.
London and Continental Banks Ltd.	Hokuriku Bank
Morgan Guaranty and Partners	Rainer Corporation
Bank of Yokohama	Liberal Bank
Banque Canadienne Nationale	
Banque Worms	
Dow Banking Corp.	
Toyo Trust and Banking	
Allgemeine Deutsche Credit	
Anstalt	
Cleveland Trust	

Source: CEPAL, on the basis of official data.

a/ Includes credits with export credit guarantees.



Table A 5.3

PERU: BOOKING OF LOANS ACCORDING TO COUNTRY OF ORIGIN OF THE BANKS, 1971-1976

Cooking	United States	Japan	Canada	United Kingdom	Germany	France	Italy	Switzerland	Consortium	Other
Headquarters	32.9	25.1	74.7	93.7	23.0	98.4	14.1	30.0	84.8	73.5
London	13.1	37.6	13.3	-	4.3	-	4.4	63.4	1.3	6.1
Bahamas	37.3	0.2	2.3	1.5	-	-	5.5	-	1.0	0.3
Panama	5.2	-	-	-	0.7	-	11.0	-	-	5.2
Cayman Isles	4.1	-	-	-	-	-	-	-	-	3.0
Paris	-	-	0.4	-	-	-	24.3	-	-	1.5
New York	-	3.3	1.7	0.7	-	-	15.4	-	-	1.8
Luxembourg	2.1	-	-	-	64.7	-	-	6.6	-	2.5
Switzerland	-	0.4	-	0.7	-	-	12.1	-	-	-
Other	0.2	3.5	-	-	-	-	11.0	-	1.3	1.8
Unspecified	5.1	29.9	7.6	3.3	7.3	1.6	2.2	-	11.6	4.3
<u>Total</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>

Source: CEPAL, on the basis of official data.

Table A 5.4  
PERU: BOOKING OF LOANS ACCORDING TO THE ASSET SIZE OF THE BANKS, 1971-1976

Booking	Asset range (millions of dollars) <sup>a/</sup>						
	65 789-	32 894-	16 447-	8 223-	4 111-	2 055-	< 1 634
	32 895	16 448	8 224	4 112	2 056	1 634	
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
Headquarters	46.8	35.4	46.6	61.2	73.4	78.3	84.3
London	2.6	17.8	19.4	18.0	-	6.1	3.5
Bahamas	24.5	21.4	16.4	4.2	6.7	-	5.2
Panama	5.8	4.0	0.5	1.2	-	-	5.2
Cayman Isles	6.4	0.6	3.7	0.6	-	-	-
Paris	-	1.2	-	0.6	-	-	-
New York	-	2.1	-	-	-	0.9	-
Luxembourg	6.1	6.1	7.9	5.3	-	-	-
Switzerland	-	0.7	-	0.6	-	-	-
Other	0.5	1.6	-	-	-	0.9	-
Unspecified	7.3	9.1	5.6	8.4	19.9	13.8	1.7
<u>Total</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>

Source: CEPAL, on the basis of official data.

<sup>a/</sup> Assets based on data for 1975 from The Banker, June 1976.

Table A6.1

Steps for organization of a syndicated credit

1. Mandate issued to lead manager.
2. Invitations sent to other banks to join management group.
3. Draft loan agreement and syndication memorandum submitted to borrower.
4. Revisions to syndication memorandum to be agreed<sup>to</sup> by borrower.
5. Responses required from banks to join management group.
6. Formal fully-underwritten offer, telex sent to the borrower.
7. Borrower approves final proof of syndication memorandum.
8. Borrower gives comments on loan agreement.
9. Borrower advises lead manager of its acceptance of the underwritten offer.
10. Telexes sent to pre-selected group of banks to be invited to participate.
11. Marked-up copy of draft loan agreement submitted to the management group.
12. Revised draft loan agreement sent to banks invited to participate.
13. Final allocation of participations made.
15. Last date for comments on loan agreement from participating banks.
16. All proposed revisions to loan agreement advised to borrower.
17. Final draft loan agreement sent to participants and to borrower.
18. Earliest date for signing loan agreement.

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Source: Financial Times "Syndicated Loans" World Banking Survey, May 21, 1979.

Table A 6.2

PERU: LEAD BANKS ACCORDING TO THEIR IMPORTANCE AS MOBILIZERS OF CREDIT, 1971-1976<sup>a/</sup>

Amount mobilized by lead bank as percent of total value of all syndicates <sup>b/</sup>	Percent participation of lead bank in its own syndicates (average)
<u>Major lead bank</u>	
1. <u>27 - 34</u>	
Citicorp	14.4
Wells Fargo	10.0
2. <u>20 - 26.9</u>	
Manufacturers Hanover	10.7
<u>Intermediate lead banks</u>	
3. <u>13 - 19.9</u>	
Bank of America	10.2
Toronto Dominion Bank	5.1
4. <u>7 - 12.9</u>	
Chase Manhattan Bank	18.6
Bank of Nova Scotia	13.2
Bankers Trust	10.1
Continental Illinois	6.0
Philadelphia National Corporation	3.3
Morgan Guaranty Trust Co.	10.0
Bank of Tokyo	15.5
Royal Bank of Canada	3.3
Lloyds Bank	10.2
Dresdner Bank	10.4
Bank of Montreal	3.3
Chemical Bank	3.3
First Chicago Corp.	6.6
Banco Nacional de Panamá	3.3
<u>Minor lead banks</u>	
5. <u>7</u>	
Banca Commerciale Italiana	50.0
Crocker National Bank	15.1
Swiss Bank Corp.	28.2
Union Bank of Switzerland	13.3
Marine Midland Bank	8.3
National Commercial Banking Group	17.3
Banca Nazionale de Lavarco	7.1
Long Term Credit Bank of Japan	12.0
Tokai Bank	1.9
Credit Lyonnais	12.5
Banque de L'Indochine Et de Suez	25.0
Libra Bank	6.5
Fuji Bank	8.7
Mitsui Bank	8.3
Algemene Bank Nederland	50.0
American Express	20.0
Mitsubishi Bank	7.5
Deutsche Bank	41.6
Grindlay's Bank	8.3
Compagnie Financiere de Paris Et des Pays-Bas	50.0
European American Bank	10.0
Banque Canadienne Nationale	8.3
Western American Bank	16.6
Iran Overseas Investment Bank	2.5
Banque Europeene de Credit	8.3
Eurolatin American Bank	5.4
Banco Popular Español	4.1

Source: CEPAL, on the basis of official data.

a/ Lead banks are managers (or agent) and co-managers.

b/ The amount mobilized by a bank is the total value of the syndicates for which it was a lead bank. Since a syndicate can have several lead banks, the sum of the percentages of all banks exceeds 100.

Table A 7.1

PERU: RESULTS OF t TEST ON ANNUAL AVERAGE LIBOR SPREAD OF LOANS OF SELECTED BANKS VS. ANNUAL AVERAGE LIBOR SPREAD ON LOANS OF ALL BANKS IN THE STUDY<sup>a/</sup>

(Paired observations)

Bank	Country	$t$	$\bar{\Delta}$	$\sigma_{\Delta}$	$\phi = N-1$
<u>1972-1976</u>					
1. Chase Manhattan	United States	.0762	0.0062	0.1817	4
2. CITICORP	United States	1.1031	0.0428	0.0870	
3. Bank of Nova Scotia	Canada	0.7840	0.0110	0.3140	
4. Bankers' Trust	United States	1.3130	0.0789	0.1340	
5. Continental Illinois	United States	-0.5500	-0.0372	0.1510	
6. Manufacturers Hanover	United States	2.4000*	0.0732	0.0681	
7. Banca Commerciale Italiana	Italy	1.5350	0.1010	0.1471	
8. Morgan Guaranty Trust	United States	0.4212	0.0242	0.1285	
9. Bank of Tokyo	Japan	-0.1485	-0.0142	0.2139	
10. Royal Bank of Canada	Canada	-0.1784	-0.0108	0.1353	
11. Toronto Dominion Bank	Canada	0.6700	0.0212	0.0703	
12. Lloyds Bank Ltd.	United Kingdom	-0.6740	-0.0720	0.2388	
13. Wells Fargo	United States	1.1466	0.0334	0.0650	
14. Fugji Bank Ltd.	Japan	-0.4479	-0.0150	0.0749	
15. Sanwa Bank	Japan	-0.8999	-0.0688	0.1710	
16. Banco de Santander	Spain	0.0332	0.0014	0.0942	
17. Dai-Ichi Kangyo Bank	Japan	0.4837	0.0692	0.3199	
<u>1972-1975</u>					
1. Chase Manhattan	United States	-0.1249	-0.1280	0.2042	3
2. CITICORP	United States	0.7645	0.0380	0.0994	
3. Bank of Nova Scotia	Canada	1.0717	0.1733	0.3233	
4. Bankers' Trust	United States	1.0069	0.0780	0.1549	
5. Continental Illinois	United States	-0.4180	-0.0365	0.1746	
6. Manufacturers Hanover	United States	1.8109	0.0710	0.0784	
7. Banca Commerciale Italiana	Italy	1.2484	0.1058	0.1694	
8. Morgan Guaranty Trust	United States	0.1358	0.0098	0.1436	
9. Crocker National Bank	United States	-0.7720	-0.0735	0.1904	
10. Bank of Tokyo	Japan	-0.3201	-0.0383	0.2390	
11. Royal Bank of Canada	Canada	-0.1665	-0.0130	0.1562	
12. Toronto Dominion Bank	Canada	0.1688	0.0060	0.0711	
13. Lloyds Bank Ltd.	United Kingdom	-0.8588	-0.1103	0.2568	
14. Banque Commerciale pour L'Europe du Nord	Soviet Union	2.6364	0.0258	0.0195	
15. Wells Fargo	United States	0.6217	0.0213	0.0684	
16. Libras Bank Ltd.	United Kingdom	-0.3684	-0.0203	0.1100	
17. Canadian Imperial Bank of Commerce	Canada	-0.7655	-0.0653	0.1705	
18. FIDELCORP	United States	-0.8394	-0.0528	0.1257	
19. Fugji Bank Ltd.	Japan	-1.3161	-0.0393	0.0596	
20. Sanwa Bank Ltd.	Japan	-1.2403	-0.1065	0.1717	
21. Banco de Santander	Spain	-0.3926	-0.0186	0.0955	
22. Dai-Ichi Kangyo Bank	Japan	0.3574	0.0660	0.3693	

Sources: CEPAL, on the basis of official data.

Notes:  $t$  = Student's  $t$  statistic.

$\bar{\Delta}$  = Mean of the differences between paired values,  $x$  and  $y$ , where  $x$  is the annual average spread on the loans of each bank and  $y$  is the annual average spread on loans of all banks in the study.

$\sigma_{\Delta}$  = Standard deviation of the differences between the paired values,  $x$  and  $y$ , at  $N-1$  degrees of freedom.

$\phi$  = Degrees of freedom.

a/ Annual averages are the mean spreads weighted by the value of the loans authorized. The average spreads for each bank were paired with the global annual averages for all banks. Exercise was carried out only on credits that had no guarantee of an export credit agency.

\* Significant at 90%.

Table A7.2

PERU: RESULTS OF t TEST ON ANNUAL AVERAGE LIBOR SPREAD OF LOANS OF BANKS  
GROUPED ACCORDING TO COUNTRY OF ORIGIN VS ANNUAL AVERAGE LIBOR  
SPREAD ON ALL LOANS OF ALL BANKS IN THE STUDY<sup>a/</sup>

(Paired observations)

Country of banks	$t$	$\bar{\Delta}$	$\sigma_{\Delta}$	$\phi = N - 1$
	<u>1972-1976</u>			4
United States	1.2280	0.0332	0.0605	
Japan	-0.5467	-0.2680	0.1096	
Canada	0.2706	0.0080	0.0661	
United Kingdom	-0.1413	-0.0080	0.1266	
Germany	-0.4453	-0.0360	0.1808	
France	0.1503	0.0160	0.2381	
Italy	1.2255	0.0480	0.0876	
Switzerland <sup>b/</sup>	-	-	-	
Other	-0.5058	-0.0140	0.6189	
Consortium	-0.2818	-0.0120	0.0952	
	<u>1972-1975</u>			3
United States	1.2780	0.0340	0.0594	
Japan	-0.9852	-0.0525	0.1066	
Canada	0.8006	0.0250	0.0625	
United Kingdom	-0.4009	-0.0275	0.1372	
Germany	-0.6672	-0.0650	0.1949	
France	0.9099	0.0125	0.2746	
Italy	0.8081	0.0400	0.0990	
Switzerland <sup>b/</sup>	-	-	-	
Other	-0.8817	-0.0275	0.6238	
Consortium	-0.3703	-0.0200	0.1080	

Source: CEPAL, on the basis of official data.

Note:  $t$  = Student's t statistic.

$\bar{\Delta}$  = Mean of the differences between paired values, x and y, where x is the annual average spread on the loans for banks in each country group and y is annual average spread for all banks in the study.

$\sigma_{\Delta}$  = Standard deviation of the differences between the paired values at N-1 degrees of freedom.

$\phi$  = Degrees of freedom.

<sup>a/</sup> Annual averages are mean spreads weighted by the value of the loans authorized. The average spreads for each country group were paired with the global annual averages for all banks. Exercise was carried out on loans that had no guarantee of an export credit agency.

<sup>b/</sup> Banks from this country did not provide a sufficient number of degrees of freedom.

\* Significant at 90%.

Table A7.3

PERU: RESULTS OF t TEST ON ANNUAL AVERAGE LIBOR SPREAD OF LOANS OF BANKS  
GROUPED ACCORDING TO ASSET SIZE VS. ANNUAL AVERAGE LIBOR  
SPREAD OF ALL LOANS ON ALL BANKS IN THE STUDY<sup>a/</sup>

(Paired observations)

Asset range (millions of dollars)	Equivalent international rankings <sup>b/</sup>	$t$	$\bar{\Delta}$	$\sigma_{\Delta}$	$\phi = N-1$
		<u>1972-1976</u>			4
1) 65.789 - 32.895	1 - 10	0.5194	0.022	0.9471	
2) 32.894 - 16.448	11 - 46	-0.9810	-0.0160	0.0365	
3) 16.447 - 8.224	47 - 91	0.7027	0.0200	0.0636	
4) 8.223 - 4.112	92 - 147	1.0392	0.0520	0.1119	
5) 4.111 - 2.056	148 - 263	0.7049	0.0220	0.0698	
6) 2.055 - 1.634 <sup>c/</sup>	264 - 300	-	-	-	
7) < 1.634	> 300	-0.5209	-0.0180	0.0773	
		<u>1972-1975</u>			3
1) 65.789 - 32.895	1 - 10	0.2781	0.0150	0.1079	
2) 32.894 - 16.448	11 - 46	-0.9798	-0.0200	0.0408	
3) 16.447 - 8.224	47 - 91	2.5627 <sup>*</sup>	0.0450	0.0319	
4) 8.223 - 4.112	92 - 147	1.3943	0.0775	0.1112	
5) 4.111 - 2.056	148 - 263	0.2689	0.0100	0.0744	
6) 2.055 - 1.634 <sup>c/</sup>	264 - 300	-	-	-	
7) < 1.634	> 300	-0.7171	-0.0300	0.0837	

Source: CEPAL, on the basis of official data.

Note:  $t$  = Student's t statistic.

$\bar{\Delta}$  = Mean of the differences between paired values, x and y, where x is the annual average libor spread for banks in each asset range and y is the annual average maturity for all banks in the study.

$\sigma_{\Delta}$  = Standard deviation of the differences between the paired values at N-1 degrees of freedom.

$\phi$  = Degrees of freedom.

a/ The annual averages are mean spreads weighted by the value of the loans authorized. The average spreads for each asset group were paired with the global annual average for all banks. The exercise was carried out only on loans that had no guarantee of an export credit agency.

b/ The rankings are on a scale from 1-300 for the corresponding asset range. The rankings are based on balance sheet date for 1975 as presented in The Banker, June 1976.

c/ Insufficient degrees of freedom to perform test.

\* Significant at 90%.

Table A7.4

PERU: RESULTS OF t TEST ON ANNUAL AVERAGE MATURITY OF LOANS OF SELECTED BANKS  
VS. ANNUAL AVERAGE MATURITY ON LOANS OF ALL BANKS IN THE STUDY<sup>a/</sup>

(Paired observations)

Bank	Country	$t$	$\bar{\Delta}$	$\sigma_{\Delta}$	$\phi = N-1$
<u>1972-1976</u>					
1) Chase Manhattan	United States	-1.0710	-1.0572	2.2083	4
2) Bank of America	United States	-1.1210	-1.0502	2.0948	
3) Citicorp	United States	0.4435	0.0126	0.6373	
4) Bank of Nova Scotia	Canada	-0.4875	-0.2160	0.9908	
5) Bankers Trust	United States	-2.5390*	-0.6460	0.5690	
6) Continental Illinois	United States	0.4492	0.0976	0.4858	
7) Manufacturers Hanover	United States	0.4451	0.1198	0.6018	
8) Banca Commerciale Italiana	Italy	-0.0354	-0.0088	0.5543	
9) Morgan Guaranty Trust	United States	0.2915	0.1098	0.8423	
10) Bank of Tokyo	Japan	-0.5059	-0.2226	0.9838	
11) Royal Bank of Canada	Canada	1.3051	0.2752	0.4715	
12) Toronto Dominion Bank	Canada	-0.9585	-0.4718	1.1006	
13) Lloyds' Bank Ltd.	United Kingdom	1.8690	0.4508	0.5393	
14) Long Term Credit Bank	Japan	-0.4430	-0.5570	2.8130	
15) Wells Fargo	United States	2.1450*	0.5176	0.5392	
16) Canadian Imperial Bank	United States	0.2747	0.1882	1.5319	
17) Fugji Bank Ltd.	Japan	1.2265	0.4780	0.8715	
18) Sanwa Bank	Japan	0.5042	0.2886	1.2800	
19) Banco de Santander	Spain	0.2481	0.1524	1.5735	
20) Dai-Ichi Kangyo Bank	Japan	3.6820*	0.8298	0.5040	
<u>1972-1975</u>					
3					
1) Chase Manhattan Bank	United States	-1.1228	-1.3618	2.4256	
2) Bank of America	United States	-0.9456	-1.1385	2.4081	
3) Citicorp	United States	0.4630	0.1685	0.7278	
4) Bank of Nova Scotia	Canada	-0.0202	-0.0103	1.1033	
5) Bankers Trust	United States	-4.2351*	-0.8478	0.4003	
6) Continental Illinois	United States	-0.6047	-0.1620	0.5358	
7) Manufacturers Hanover	United States	0.3154	0.1095	0.6944	
8) Banca Commerciale Italiana	Italy	-0.1622	-0.5130	0.6319	
9) Morgan Guaranty Trust	United States	0.1996	0.9700	0.9720	
10) Crocker National	United States	-0.9534	-0.5438	1.1407	
11) Bank of Tokyo	Japan	-0.5746	-0.3185	1.1087	
12) Royal Bank of Canada	Canada	0.7722	0.1940	0.5025	
13) Toronto Dominion Bank	Canada	-0.2843	-0.1300	0.9145	
14) Lloyds' Bank Ltd.	United Kingdom	1.7614	0.5240	0.5949	
15) Long Term Credit Bank	Japan	-0.4579	-0.7365	3.2168	
16) Banque Commerciale Pour L'Europe Du Nord	Soviet Union	3.7356*	0.4028	0.2156	
17) Wells Fargo	United States	2.0976	0.6068	0.5785	
18) Libra Bank Ltd.	United Kingdom	2.0770	0.5410	0.5209	
19) CIT Financial Corp.	United States	-0.4557	-0.6740	2.9584	
20) Canadian Imperial Bank of Commerce	Canada	-0.2486	-0.1845	1.4843	
21) FIDELCORP	United States	-0.0743	-0.0530	1.4259	
22) Fugji Bank Ltd.	Japan	1.1311	0.5573	0.9853	
23) Sanwa Bank	Japan	0.4344	0.3205	1.4757	
24) Banco de Santander	Spain	0.1895	0.1503	1.5860	
25) Dai-Ichi Kangyo	Japan	5.1094*	0.9970	0.3903	

Source: CEPAL, on the basis of official data.

Note:  $t$  = t statistic.

$\bar{\Delta}$  = Mean of the differences between the paired values, x and y, where x is the annual average maturity on loans of an individual bank any y is the global annual average maturity on loans of all banks in the study.

$\sigma_{\Delta}$  = Standard deviation of the differences between the paired values x and y at N-1 degrees of freedom.

$\phi$  = Degrees of freedom.

<sup>a/</sup> Annual averages are the mean maturities weighted by the value of loans carrying a specific maturity. The averages for each bank were paired with the global annual average for all banks. Exercise was carried out only on loans that had no guarantee of an export credit agency.

\* Significant at 90%.



Table A7.5

PERU: RESULTS OF t TEST ON ANNUAL AVERAGE MATURITY OF LOANS OF BANKS GROUPED ACCORDING COUNTRY OF ORIGIN VS. ANNUAL AVERAGE MATURITY OF ALL LOANS OF ALL BANKS IN THE STUDY<sup>a/</sup>

(Paired observations)

Country of banks	$t$	$\bar{\Delta}$	$\sigma_{\Delta}$	$\phi = N-1$
		<u>1972-1976</u>		4
United States	-1.3475	-0.054	0.0896	
Japan	0.8821	0.300	0.7605	
Canada	-0.3009	-0.004	0.2974	
United Kingdom	0.0119	0.002	0.3760	
Germany	0.8431	0.242	0.6418	
France	-0.5015	-0.220	0.9810	
Italy	-0.4625	-0.142	0.6866	
Switzerland <sup>b/</sup>	-	-	-	
Other	5.1588*	0.392	0.1699	
Consortium	0.0215	0.006	0.6244	
		<u>1972-1975</u>		3
United States	-0.8926	-0.0450	0.1008	
Japan	0.7671	0.3350	0.8735	
Canada	0.1808	0.0300	0.3319	
United Kingdom	-0.1777	-0.0375	0.4220	
Germany	0.7102	0.2625	0.7393	
France	-0.6412	-0.3475	1.0839	
Italy	-0.5661	-0.2175	0.7684	
Switzerland <sup>b/</sup>	-	-	-	
Other	7.1003*	0.4500	0.1268	
Consortium	-0.0910	-0.0325	0.7141	

Source: CEPAL, on the basis of official data.

Note:  $t$  = t statistic.

$\bar{\Delta}$  = Mean of the differences between paired values, x and y, where x is the annual average maturity for banks in each country group and y is the annual average maturity for all banks.

$\sigma_{\Delta}$  = Standard deviation of the differences between the paired values at N-1 degrees of freedom

$\phi$  = Degrees of freedom.

<sup>a/</sup> The annual averages are mean maturities weighted by the value of the loan carrying the specific maturity. The averages for each country group were paired with the global annual averages for all banks. Exercise was carried out only on loans that had no guarantee of an export credit agency.

<sup>b/</sup> Banks from this country did not provide a sufficient number of degrees of freedom.

\* Significant at 90%.

Table A7.6

PERU: RESULTS OF t TEST ON ANNUAL AVERAGE MATURITY OF LOANS OF BANKS GROUPED ACCORDING TO ASSET SIZE VS. ANNUAL AVERAGE MATURITY ON ALL LOANS OF ALL BANKS IN THE STUDY<sup>a/</sup>

(Paired observations)

Asset range (millions of dollars)	Equivalent international ranking b/	$t$	$\bar{\Delta}$	$\sigma_{\Delta}$	$\phi = N-1$
<u>1972-1976</u>					
1) 65 789 - 32 895	1 - 10	0.1624	0.0280	0.3856	4
2) 32 894 - 16 448	11 - 46	-0.5293	-0.0340	0.1436	
3) 16 447 - 8 224	47 - 91	-0.4804	-0.0420	0.1955	
4) 8 223 - 4 112	92 - 147	-1.6440	-0.2320	0.3156	
5) 4 111 - 2 056	148 - 263	0.6730	0.1260	0.4187	
6) 2 055 - 1 634	264 - 300 <sup>c/</sup>	-	-	-	
7) < 1 634	> 300	0.7657	0.1520	0.4439	
<u>1972-1975</u>					
1) 65 789 - 32 895	1 - 10	0.3242	0.0700	0.4318	3
2) 32 894 - 16 448	11 - 46	-1.5173	-0.0825	0.1087	
3) 16 447 - 8 224	47 - 91	0.4016	0.0275	0.1370	
4) 8 223 - 4 112	92 - 147	-1.6344	-0.2800	0.3426	
5) 4 111 - 2 056	148 - 263 <sup>c/</sup>	0.4866	0.1175	0.4829	
6) 2 055 - 1 634	264 - 300	-	-	-	
7) < 1 634	> 300	0.5854	0.1500	0.5125	

Sources: CEPAL, on the basis of official data.

Notes:

$t$  = t statistic.

$\bar{\Delta}$  = Mean of the differences between paired values, x and y, where x is the annual average maturity for banks in each asset range and y is annual average maturity on loans of all banks in the study.

$\sigma_{\Delta}$  = Standard deviation of the differences between the paired values at N-1 degrees of freedom.

$\phi$  = Degrees of freedom.

a/ The annual averages are mean maturities weighted by the value of the loan carrying the specific maturity.

The averages for each asset group were paired with the global annual average of all banks. The exercise was carried out only on loans that had no guarantee of an export credit agency.

b/ The rankings are on a scale from 1-300 for the corresponding asset range. The rankings are based on balance sheet data for 1975 as presented in The Banker, June 1976.

c/ Insufficient degrees of freedom.

\* Significant at 90%.

Table A7.7

PERU: RESULTS OF T TEST ON ANNUAL AVERAGE COST OF FLAT FEES ON ALL LOANS OF SELECTED BANKS  
VS. ANNUAL AVERAGE COST OF FLAT FEES ON ALL LOANS OF ALL BANKS IN THE STUDY<sup>a/</sup>

(Paired observations)

Name of bank	Country	$t$	$\bar{\Delta}$	$\sigma_{\Delta}$	$\phi = N-1$
<u>1972-1976</u>					
1) Bank of America	United States	-4.0474*	-0.2074	0.1146	4
2) Citicorp	United States	-0.3152	-0.0214	0.1518	
3) Bank of Nova Scotia	Canada	-0.9600	-0.1384	0.3224	
4) Bankers Trust	United States	-0.4278	-0.0380	0.1986	
5) Continental Illinois	United States	-1.6443	-0.0968	0.1316	
6) Manufacturers Hanover	United States	0.9256	0.0802	0.1937	
7) Banca Commerciale Italiana	Italy	1.8961	0.1222	0.1441	
8) Morgan Guaranty Trust	United States	0.1297	0.0114	0.1966	
9) Bank of Tokyo	Japan	0.1057	0.0072	0.1523	
10) Royal Bank of Canada	Canada	-0.7183	-0.0594	0.1849	
11) Toronto Dominion Bank	Canada	4.9664*	0.1684	0.0758	
12) Lloyds Bank Ltd.	United Kingdom	0.3353	0.0324	0.2161	
13) Long Term Credit Bank	Japan	0.7563	0.0664	0.1963	
14) Wells Fargo	United States	1.3974	0.1254	0.2007	
15) Canadian Imperial Bank	Canada	0.0277	0.0056	0.4527	
16) Fugji Bank Ltd.	Japan	3.8586*	0.1566	0.0975	
17) Sanwa Bank Ltd	Japan	1.8808	0.1396	0.1660	
18) Banco de Santander	Spain	4.7630*	0.2546	0.1196	
19) Dai-Ichi Kangyo Bank	Japan	2.9825*	0.1424	0.1068	
<u>1972-1975</u>					
1) Bank of America	United States	-3.3055*	-0.2156	0.1305	3
2) Citicorp	United States	-0.8890	-0.0623	0.1401	
3) Bank of Nova Scotia	Canada	-0.0961	-0.0076	0.1560	
4) Bankers Trust	United States	-1.5555	-0.1085	0.1395	
5) Continental Illinois	United States	-1.7110	-0.1198	0.1400	
6) Manufacturers Hanover	United States	0.3983	0.0393	0.1971	
7) Banca Commerciale Italiana	Italy	1.7652	0.0643	0.0728	
8) Morgan Guaranty Trust	United States	-0.5492	-0.0468	0.1705	
9) Crocker National Bank	United States	-1.7451	-0.1645	0.1885	
10) Bank of Tokyo	Japan	-1.0161	-0.0495	0.0974	
11) Royal Bank of Canada	Canada	0.1344	0.0083	0.1228	
12) Toronto Dominion Bank	Canada	3.9672*	0.1520	0.0766	
13) Lloyds Bank Ltd	United Kingdom	-0.6939	-0.0480	0.1383	
14) Long Term Credit Bank	United States	0.2460	0.0245	0.1992	
15) Banque Commerciale Pour L'Europe Du Nord	Soviet Union	1.9912	0.2338	0.2348	
16) Wells Fargo	United States	0.8756	0.0958	0.2187	
17) Libra Bank	United Kingdom	1.5344	0.0970	0.1264	
18) CIT Financial Corporation	United States	-0.7672	-0.0953	0.2483	
19) Canadian Imperial Bank of Commerce	Canada	2.5005*	0.1985	0.1588	
20) FIDELCOR	United States	0.9417	0.1033	0.2193	
21) Fugji Bank Ltd	Japan	2.9800*	0.1373	0.0921	
22) Sanwa Bank	Japan	1.2769	0.1160	0.1817	
23) Banco de Santander	Spain	3.7603*	0.2298	0.1222	
24) Dai-Ichi Kangyo Bank	Japan	2.2054	0.1195	0.1082	

Sources: CEPAL, on the basis of official data.

Note:  $t = *$  statistic.

$\bar{\Delta}$  = Mean of the differences between paired values, x and y, where x is the annual average cost of flat fees on all loans of a bank and y is the global annual average cost of flat fees on all loans of all banks.

$\sigma_{\Delta}$  = Standard deviation of the differences between the paired values at N-1 degrees of freedom.

$\phi$  = Degrees of freedom.

a/ Annual averages are the mean cost of flat fees on all loans weighted by the value of the loans. The annual averages for each bank were paired with the annual average of all banks. Exercise was carried out only on loans without a guarantee of an export credit agency. Note that in syndicated credits fees were distributed equally among all banks.

\* Significant at 90%.

Table A7.8

PERU: RESULTS OF T TEST ON ANNUAL AVERAGE COST OF FLAT FEES OF ALL LOANS OF BANKS GROUPED ACCORDING TO COUNTRY OF ORIGIN VS. ANNUAL AVERAGE COST OF FLAT FEES ON ALL LOANS OF ALL BANKS IN THE STUDY<sup>a/</sup>

(Paired observations)

Country of banks	$t$	$\bar{\Delta}$	$\sigma_{\Delta}$	$\phi = N-1$
		<u>1972-1976</u>		4
United States	-0.5502	-0.0184	0.0748	
Japan	2.1937*	0.0940	0.0958	
Canada	-0.4713	-0.0460	0.2183	
United Kingdom	0.8883	0.0692	0.1742	
Germany	0.1698	0.0172	0.2265	
France	0.7004	0.1658	0.5293	
Italy	1.8090	0.0118	0.1461	
Switzerland <sup>b/</sup>	-	-	-	
Other	3.1501*	0.1812	0.1286	
Consortium	5.0929*	0.1410	0.0619	
		<u>1972-1975</u>		3
United States	-2.1633	-0.0473	0.0437	
Japan	1.8487	0.0590	0.0638	
Canada	2.1979	0.0500	0.0455	
United Kingdom	0.1089	0.0065	0.1194	
Germany	-0.7609	-0.0620	0.1630	
France	0.6214	0.1890	0.6083	
Italy	1.6283	0.0593	0.0728	
Switzerland <sup>b/</sup>	-	-	-	
Other	2.3430	0.1715	0.1464	
Consortium	3.9381*	0.1408	0.0715	

Source: CEPAL, on the basis of official data.

Note:  $t$  =  $t$  statistic.

$\Delta$  = Mean of the differences between paired values,  $x$  and  $y$ , where  $x$  is the annual average cost of flat fees on all loans of banks in each country group and  $y$  is the annual average cost of flat fees on all loans of all banks.

$\sigma_{\Delta}$  = Standard deviation of the differences between the paired values at  $N-1$  degrees of freedom.

$\phi$  = Degrees of freedom.

<sup>a/</sup> Annual averages are the mean cost of flat fees on all loans weighted by the value of the loans. The annual averages for each group of banks were paired with the annual average cost of fees on all loans of all banks. Exercise was carried out only on loans without a guarantee of an export credit agency. Note that in the case of syndicated credits, fees were distributed equally among all banks.

<sup>b/</sup> Banks from this country did not provide a sufficient number of degrees of freedom.

\* Significant at 90%.

Table A7.9

PERU: RESULTS OF t TEST ON ANNUAL AVERAGE COST OF FLAT FEES OF LOANS OF BANKS GROUPED ACCORDING TO ASSET SIZE VS. ANNUAL AVERAGE COST OF FLAT FEES ON LOANS OF ALL BANKS IN THE STUDY<sup>a/</sup>

(Paired observations)

Asset range (millions of dollars)	Equivalent international rankings <sup>b/</sup>	$t$	$\bar{\Delta}$	$\sigma_{\Delta}$	$\phi = N-1$
<u>1972-1976</u>					4
1) 65 789 - 32 895	1 - 10	-0.2261	-0.0110	0.1088	
2) 32 894 - 16 448	11 - 46	-0.3095	-0.0038	0.0275	
3) 16 447 - 8,224	47 - 91	-0.9671	-0.0412	0.0990	
4) 8 223 - 4 112	92 - 147	-0.8146	-0.0412	0.1131	
5) 4 111 - 2 056	148 - 263	2.6878 *	0.1160	0.0965	
6) 2 055 - 1 634 <sup>c/</sup>	264 - 300	-	-	-	
7) < 1 634	> 300	5.6116 *	0.1380	0.0548	
<u>1972-1975</u>					3
1) 65 789 - 32 895	1 - 10	-0.8482	-0.0415	0.0978	
2) 32 894 - 16 448	11 - 46	-0.7032	-0.0098	0.0277	
3) 16 447 - 8 224	47 - 91	-0.2648	-0.0103	0.0774	
4) 8 223 - 4 112	92 - 147	0.2993	0.0065	0.0434	
5) 4 111 - 2 056 <sup>c/</sup>	148 - 263	-1.9360	0.0978	0.1010	
6) 2 055 - 1 634	264 - 300	-	-	-	
7) < 1 634	> 300	4.8363 *	0.1230	0.0509	

Source: CEPAL, on the basis of official data.

- Notes:  $t$  = t statistic.  
 $\bar{\Delta}$  = Mean of the differences between paired values, x and y, where x is the annual average cost of fees on all loans of banks in each asset range and y is the annual average cost of flat fees on all loans of all banks.  
 $\sigma_{\Delta}$  = Standard deviation of the differences between the paired values at N-1 degrees of freedom.  
 $\phi$  = Degrees of freedom.

- a/ The annual averages are the mean cost of flat fees weighted by the value of the loan. The averages for all banks. The exercise was carried out only on loans that had no guarantee of an export credit agency. Note that in the case of syndicated credits fees were distributed equally among all banks.  
b/ The rankings are on a scale from 1-300 for the corresponding asset range. The rankings are based on balance sheet data for 1975 as presented in The Banker, June 1976.  
c/ Insufficient degrees of freedom.

\* Significant at 90%.

Table A7.10

PERU: BREAKDOWN OF LOANS ACCORDING TO TYPE AND COUNTRY ORIGIN OF LENDING BANKS, 1971-1976<sup>a/</sup>

(Percent)

Country	Import and goods	Other imports	Refinance	Free disposition	Projects	Nationalization	Other <sup>b/</sup>	Total loans
United States	2.4	0.2	48.4	29.9	8.7	9.3	1.1	100.0
Japan	0.6	-	43.5	39.2	16.0	-	0.7	100.0
Canada	2.1	-	53.1	28.0	15.9	-	0.9	100.0
United Kingdom	8.3	-	49.7	18.4	23.6	-	-	100.0
Germany	-	-	57.0	5.7	37.3	-	-	100.0
France	-	-	51.9	27.9	20.2	-	-	100.0
Italy	-	-	58.8	29.6	11.6	-	-	100.0
Switzerland	-	-	16.3	17.5	7.6	58.6	-	100.0
Consortium	1.3	-	64.4	19.7	14.6	-	-	100.0
Other	1.2	-	40.2	25.1	33.5	-	-	100.0
<u>Memorandum items</u>								
Unweighted average	1.6	-	48.3	24.1	18.9	6.8	0.3	100.0
Standard deviation	2.4	-	12.6	8.7	9.5	17.5	0.4	

Source: CEPAL, on the basis of official data.

<sup>a/</sup> Excludes loans with guarantees of export credit agencies.

<sup>b/</sup> Loans which could not be classified into any other category.

Table A7.11

PERU: BREAKDOWN OF LOANS ACCORDING TO TYPE AND THE ASSET SIZE OF LENDING BANKS, 1971-1976<sup>a/</sup>

(Percent)

Asset range (millions of dollars)	World rank range (1-300)	Import of k goods	Other imports	Refinance	Free dispo- sition	Projects	National- ization	Other	Total loans
1) 65 789 - 32 895	1 - 10	2.1	0.5	56.9	25.8	12.4	2.3	-	100.0
2) 32 894 - 16 448	11 - 46	2.8	-	43.5	30.0	15.2	7.9	0.7	100.0
3) 16 447 - 8 224	47 - 91	1.9	-	55.8	26.5	9.4	5.3	1.1	100.0
4) 8 223 - 4 112	92 - 147	-	-	40.0	21.4	20.4	16.7	1.6	100.0
5) 4 111 - 2 056	148 - 263	-	-	44.6	24.2	25.1	3.8	2.3	100.0
6) 2 055 - 1 634	264 - 300	-	-	62.5	26.8	10.7	-	-	100.0
7) < 1 634	> 300	1.0	-	53.4	29.3	16.3	-	-	100.0
8) Unknown <sup>b/</sup>	...	-	-	38.2	38.6	18.5	4.7	-	100.0
<u>Memorandum items</u>									
Unweighted average		1.0	-	49.4	27.8	16.0	5.1	0.7	100.0
Standard deviation		1.1	-	8.3	4.8	4.9	5.1	0.8	

Source: CEPAL, on the basis of official data.

<sup>a/</sup> Excludes loans with guarantees of export credit agencies.

<sup>b/</sup> Banks where no data were available on asset size.

Table A7.12

PERU: BREAKDOWN OF LOANS ACCORDING TO ECONOMIC SECTOR AND THE COUNTRY  
OF ORIGIN OF LENDING BANKS, 1971-1976<sup>a/</sup>

(Percent)

Sectors	United States	Japan	Canada	United Kingdom	Germany	France	Italy	Switzerland	Commonwealth	Other	Memo items	
											Unweighted average	standard deviation
Primary	13.2	5.8	15.6	29.9	9.7	38.6	10.9	-	3.2	5.1	13.2	11.6
Secondary and tertiary	12.8	24.0	12.0	32.5	29.9	30.7	15.4	11.1	19.8	47.9	(23.6)	(11.2)
(Secondary)	(8.3)	(22.7)	(7.1)	(32.5)	(29.9)	(27.4)	(15.4)	(11.1)	(11.2)	(36.8)	(20.2)	(10.4)
(Tertiary)	(4.5)	(1.3)	(4.9)	-	-	(3.3)	(-)	(-)	(8.6)	(11.1)	(3.4)	(3.8)
Unclassified <sup>b/</sup>	74.0	70.2	72.4	37.6	60.4	30.7	73.6	88.9	77.0	47.0	63.2	17.9
<u>Total loans</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	

Source: CEPAL, on the basis of official data.

a/ Excludes loans with guarantees of export credit agencies; also, only accounts for loans where there was ex ante agreement between borrower and lender on the destination of the credit.

b/ Loans that went to a number of undesignated sectors. These are basically general refinance credits.



Table A7.13

PERU: BREAKDOWN OF LOANS ACCORDING TO ECONOMIC SECTORS AND THE SIZE  
OF LENDING BANKS, 1971-1976<sup>a/</sup>  
(Percent)

Sectors	Asset range of banks (millions of dollars) <sup>b/</sup>							Memo items		
	65 789-	32 894-	16 447-	8 223-	4 111-	2 055-	< 1 634	Un-	Un-	Standard
	32 895	16 448	8 224	4 112	2 056	1 634	known	weighted		
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	average	
Primary	15.4	11.5	8.1	31.4	13.6	42.0	5.4	19.6	18.4	11.6
Secondary and tertiary	21.1	17.9	19.6	21.5	33.8	-	32.3	30.3	22.1	10.1
Secondary)	(14.3)	(17.0)	(19.3)	(18.3)	(23.2)	(-)	(25.8)	(20.3)	(17.3)	(7.3)
Tertiary)	(6.8)	(0.9)	(0.3)	(3.2)	(10.6)	(-)	(6.5)	(10.0)	(4.8)	(4.0)
Unclassified <sup>c/</sup>	63.5	70.6	72.6	47.1	52.6	58.0	62.3	50.1	59.6	8.7
<u>Total loans</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	

Source: CEPAL, on the basis of official data.

a/ Excludes loans with guarantees of export credit agencies; also, only accounts for loans where <sup>there</sup> was an ex ante agreement between borrower and lender on the destination of the credit.

b/ Assets based on data for 1975 as found in The Banker, June 1976.

c/ Loans that went to a number of undesignated sectors. These are basically general refinance credits.

Table A7.14

PERU: BANKS EXTENDING CREDIT WITH GUARANTEES OF HOME COUNTRY  
EXPORT CREDIT AGENCIES, 1971-1976

(Percent)

Banks	Guaranteed credits of the bank as a percent of all guaranteed credits	Guaranteed credits of the bank as a percent of all credits of the bank
Schroders Ltd.	5.6	88.8
Manufacturers' Hanover	5.1	11.0
Philadelphia National Bank	2.5	27.8
Western Bancorporation	0.3	2.9
Banca Commerciale Italiana	0.1	1.1
Crocker National Bank	0.6	3.0
Lloyds Bank Ltd.	1.3	6.8
Swiss Bank Corporation	1.0	13.4
National and Commercial Banking Group	15.9	93.9
Credit Lyonnais	6.4	51.0
Banque Francaise Du Commerce Exterieur	9.1	81.7
Banque de L' Indochine et de Suez	4.0	72.1
Algemene Bank Nederland	4.5	100.0
Amro Bank	10.8	100.0
Balfour and Williamson	0.5	25.2
Banco do Brasil	18.8	71.6
Compagnie Financiere de Paris et des Pays-Bas	5.2	75.4
Banco Mexicano	3.7	100.0
Banque Worms	1.8	63.7
Barclays Bank	2.9	43.6

Source: CEPAL, on the basis of official data.

Table A 8.1

PERU: A SELECTED LIST OF PROJECTS WITH PARTICIPATION OF FOREIGN COMMERCIAL BANKS, 1972-1976

Name of project	Date of loans	Suppliers	Lending institutions	Amount <u>a/</u> (millions of US dollars)	Interest rate	Total maturity (years)
1) Oxygen plant	1974	Linde A.G.	Deutsche Bank	2.3	1.3 + libor	7.0
	1976	Linde A.G.	Deutsche Bank	0.5	1.3 + libor	7.0
2) Treatment plant for steel bars and plates	1972	Fives cail	French Treasury	0.6	3.5	20.0
		Babcock	Credit Lyonnais	1.8*	6.5	10.0
	1976	DEMAG	Banque Francaise De Commerce Ext.			
			Banque De Paris et Pays Bas	DEMAG	0.4	8.5
3) Anode plant	1975	DEMAG	Lloyds Bank	1.2	1.5 + libor	7.0
4) Copper refinery at Ilo	1972	Mitsui	Mitsui	23.1	6.75	13.0
	1973	Furukawa Electric	Furukawa Electric	2.6	1.75 + libor	8.0
5) Alkali plant	1975	Oronzio de Nora	Oronzio de Nora	2.5	8.0	5.0
	1976	Westinghouse	Crocker National Bank	0.3*	8.25	5.0
		Marbrook, Div. of the Foram Corp.		1.0*	8.0	5.0
		Dunham Bus. Int. Dorr Oliver Inc. Zurn Industries Inc.				
6) Telephone switchboard systems	1974	Philips Telecommunications Industries	Amro Bank	13.4*	8.0	13.0
	1974	Philips Telecommunications Industries	N.I.O. <u>b/</u>	6.3	6.5	20.0
	1974	Bell Telephone	Bell Telephone	22.3	...	...

Table A 8.1 (continuación 1)

Name of project	Date of loans	Suppliers	Lending institutions	Amount a/ (millions of US dollars)	Interest rate	Total maturity (years)
7) Amplification and rehabilitation of railroads	1975	Pandral (United Kingdom)	Lloyds Bank	2.8*	7.0	5.0
		Martencita (Brazil)	Bank of London & Montreal	0.8	1.5 + libor	5.0
	1973	M.L.W. Worthington Ltd. Sidney Steel Corp.	Banco do Brasil	0.3*	7.0	5.0
			Bank of Montreal	3.7	1.25 + prime	7.0
		Export Development Corp. of Canada	13.5	7.25	13.0	
...	Mecano Export-Import	Protocol Peru-Romania	8.4	...	...	
8) Transandean oil pipeline and north feeder line	1976	Const. Protexa	Const. Protexa	27.0	2% + libor	5.5
	1976	Const. Protexa	Const. Protexa	6.0	2% + prime	5.5
	1976	Const. Protexa	Financiera Aceptaciones	60.0*	8.5	10.5
	...	Machine Export	Protocol Peru-Russia	6.1	...	...
	...	Bechtel Inc.	Banco Interamericano de Desarrollo	0.5	...	...
	...	Bechtel Inc.	Various	3.1	...	...
	...	Bechtel Inc.	Banco Interamericano de Desarrollo	0.6	...	...
	1974	-	Japan-Peru Oil Co. c/	230.0	6.5	14
	...	-	Japan-Peru Oil Co. c/	63.8	...	...
	1974	Techint	Technit	40.1	7.5	10
	1977	Techint	Technit	3.5	9.5	180 days
	1974	Rustin Gas Turbines	Manufacturers Hanover Finance Ltd.	11.0*	8.0	11.5
	1975	-	Syndicate headed by Wells Fargo Bank	50.0d/	1.75 + libor	7.0
	1975	-	Syndicate headed by Wells Fargo Bank	50.0d/	1.75 + libor	7.0
	1975	George Wimpey Ltd.	Schroders Ltd.	11.9*	8.0	7.0
	...	George Wimpey Ltd.	Schroders Ltd.	(0.6)*	...	...
	...	Page Communications	Page Communications	2.0	...	...
	...	Bechtel Inc.	Crocker National Bank	15.0	1.75 + libor	6.5
	1977	Various	Corporation Andina de Fomento	20.0	10.0	8.0
	1977	Consortium Williams/Sedco/Hoer	Citicorp	14.6	...	...
	1977	F.H. Gotteld	Deutsche Bank	0.5	2% + libor	1.0
	1975	Joint Venture Hoesch-Falzgitter	Syndicate headed by Dresdner Bank	24.4e/	2% + libor	5.0
1976	...	DAVAL S.A.	2.0	0.6% + libor	2.0	
1974	..	Japan-Peru Oil Corp-Japan Petroleum Development Corp.	100.0	6.0%	14.0	

Table A 8.1 (continuación 2)

Name of project	Date of loans	Suppliers	Lending institutions	Amount a/ (millions of US dollars)	Interest rate	Total maturity (years)
9) Expansion of cement plant Norte Pacasmayo S.A.	1976	Fuller <u>et al</u>	United States Eximbank	8.1	8.0%	11.5
	1976	Fuller <u>et al</u>	Philadelphia National Bank	5.4*f/	1% + prime	7.0
	1976	Fuller <u>et al</u>	Philadelphia National Bank	2.7f/	1% + prime	4.0
	1976	Fuller <u>et al</u>	Philadelphia National Bank	1.3	2% + libor	6.5
	1976	Fuller <u>et al</u>	Banque Worms	1.2	2% + libor	7.0
	1976	Fuller <u>et al</u>	Banque Worms and Banque Francaise de Commerce Ext.	5.0*	7.5	11.0
	1976	Siemens	Siemens	0.4	9.5	10.5
	1976	Siemens	Kreditanstalt	4.0	9.5	10.5
	1977	Haver and Boecker	Haver and Boecker	0.5	8.0	10.5
	10) Diesel motor plant (Motores Andino)	1976	Perkins Motors	Schroders	0.5	2.0% + libor
1977		Perkins Motors	Schroders	2.7*	7.5%	5.0
11) Copper mine: Cerro Verde, stage I	1972	British Smelter Construction Ltd.	Williams and Glyn's Bank	21.7*	6.0%	14.8
	1972	Various	Syndicate headed by Williams and Glyn's Bank	12.7	2.25 + libor	5.0
	1972	Wright Engineers Ltd.	Export Development Corp. of Canada	21.4	7.25%	14.0
	1973	Various United States Suppliers	Continental Ill. Bank	7.0	1.0 + prime	7.0
	1976	Various	Continental Ill. Bank	9.5	2.0 + libor	5.5
	12) Refinery La Pampilla	1972	Technip	Credit Lyonnais Banque de Paris et de Pay Bas Banque Francaise du Commerce Ext.	22.9*	6.75
1975		Technip	Credit Lyonnais	2.9*	7.2	5.0
1977		Technip	Credit Lyonnais	0.7*	7.25	4.0
...		Technip	Credit Lyonnais	(FF 3.6)	...	...
13) Hydroelectric plant Mantaro		1975	Engineering Consultants Electrowatt	Swiss Credit Bank	3.3	9.0%
	1973	GIE-Impregilo	GIE Impregilo	219.6	...	...
	1973	GIE-Impregilo	GIE Impregilo	48.5	6.5%	17.5

Table A 8.1 (concluded)

Name of project	Date of loans	Suppliers	Lending institutions	Amount <sup>a/</sup> (millions of US dollars)	Interest rate	Total maturity (years)	
14) Paper plant	1974	Bufete Protecona	Banco Nacional de Comercio Exterior	1.6*	8.0%	6.0	
	1975	Bufete Rust	Citibank	0.6	1.125+ libor	5.0	
	1975	Valmet Oy	Valmet Oy	13.6	8.0%	2.5	
	1975	Valmet Oy	Valmet Oy	19.3	8.0%	9.0	
	1975	Valmet Oy	Citibank	1.7	1.75 + libor	7.0	
	1975	Valmet Oy	Valmet Oy	0.1	...	...	
	...	Valmet Oy	Protocol Peru-Finland	(MF 5.0)	...	...	
	1977	Valmet Oy	Valmet Oy	1.0	8.0%	8 months	
	1977	Valmet Oy	Valmet Oy	1.0	8.0% <sup>g/</sup>	9.5	
	1976	Elof Hansson	Elof Hansson	2.5	8.5%	5.0	
	1976	Elof Hansson	Elof Hansson	15.7	8.0%	11.0	
	1976	Commonwealth Construction Company	Export Development Corp. of Canada	1.1	8.75%	5.5	
	1976	Commonwealth Construction Company	Royal Bank of Canada	0.5	1.75 + prime	5.5	
	1976	Distral S.A.	Distral S.A.	0.4	2.0 + libor	8.0	
	1977	Distral S.A.	Distral S.A.	2.1	8.25%	8.0	
	1976	Degremont S.A.	Credit Lyonnais	0.2	2% + libor	5.0	
	1977	Degremont S.A.	Degremont S.A.	0.9	8.75%	6.5	
	1977	Elof Hansson	Elof Hansson	0.8*	8.5%	4.0	
	1977	Elof Hansson	Elof Hansson	4.9*	8.0%	9.5	
	1977	Commonwealth Construction Company	Export Development Corp. of Canada	1.3	8.75	4.25	
			Alban and Felt Co.				
			SNA International	Royal Bank of Canada	0.3	2.0 + prime	4.25
			Same as above	Bank of Montreal	0.1	2.0 + prime	4.25
			"	Royal Bank of Canada	0.5	2.0 + prime	2.5
			"	Bank of Montreal	0.1	2.0 + prime	2.5
	1977	Cofpa-Martell	Cofpa	0.3	9.0%	3.0	
	1977	Catala	Credit Lyonnais	0.1	2.25 + libor	2.0	
	1977	Geschmay-Wagner	Deutsche Bank A.G.	0.4	5.0% + discount rate of bank	5.0	
	1977	Elof Hansson	Elof Hansson	0.3*	9.0%	3.5	
	1977	Elof Hansson	Elof Hansson	2.0*	8.5%	9.0	
1977	Bufete Industrial	Banco Mexicano S.A.	0.5*	8.0%	3.17		

Source: Data provided to CEPAL by COFIDE and CEPAL on the basis of official data.

<sup>a/</sup> Non-United States currencies were converted to dollars using the average exchange rate for the year corresponding to the date of authorization.

<sup>b/</sup> De Nederlandse Investeringsbank noor Ontwikkelingslanden N.V.

<sup>c/</sup> Called JAPECO and owned as follows: 25% Marubeni Corp; 25% Mitsui Group; and 50% Japanese Petroleum Development Corp, which is a Japanese State Enterprise.

<sup>d/</sup> The Government of Iran deposited the equivalent amounts in the accounts of the lending banks as part of an agreement with Peruvian authorities to finance the pipeline.

<sup>e/</sup> Both the suppliers and bankers operated under the aegis of a "shell" Peruvian Corporation called ALAMBRESA. This group financed another 27 million dollars of purchases which are not indicated in the table, i.e., the total financed through ALAMBRESA was 119 million D-marks.

<sup>f/</sup> Part of a joint loan with Eximbank.

<sup>g/</sup> 67 000 dollars was free of interest.

\* Guaranteed by home country export credit agency.

Table A8.2

Peruvian Government Stabilization Program, June 1975

MEASURES ADOPTED IN ORDER TO OBTAIN BALANCE OF PAYMENTS EQUILIBRIUM

Various measures have been implemented in order to restore equilibrium in the external sector, including the following:

a) An increase in the exchange rate from S/ 45 to S/ 65 per dollar.

The equilibrium exchange rate parity for June was estimated at S/ 58.96 per dollar. However, in order to further improve the competitiveness of the external sector in the short run and compensate the rise in costs as a result of the measures which have been adopted, parity was fixed at S/ 65 per dollar by the Board of Directors of the Central Reserve Bank, in consultation with the Government.

b) Non Traditional Export Promotion .

The tax rebate mechanism (CERTEX), previously fixed at a basic rate of 40% of the export value, was reduced only by 10%, to a basic rate of 30%, so as to increase the competitiveness of manufactured goods in the international market.

Industries are expected to respond rapidly to the export incentives adopted, generating additional foreign exchange due to the idle productive capacity resulting from the reduction of internal aggregate demand expected as a result of the stabilization program.

c) Export Promotion of the small and medium mining sector .

The mining acceptance bond, a low interest credit mechanism, though reduced from 20% to 10% of the FOB export value, has been maintained in order to accelerate the reactivation of small and medium sized mining enterprises, which have been producing approximately 20% of Peru's copper and 35% of its silver, lead and zinc.

Table A8.2  
(Continued)

d) Increase in the effective capital goods import tariff.

This measure, adopted in order to correct excessive use of capital intensive production processes, will tend to promote labor intensive industries, reduce imports and achieve a more rational utilization of existing productive capacity.

e) Reorganization of the import control system.

A system of annual import programs and annual foreign exchange budgets has been established in order to forecast the goods which will have to be imported and the foreign exchange necessary for purchasing them. This will make the import control system more coherent, rational and expeditive, assuring an adequate supply of goods to the country while serving as a mechanism for restricting the use of foreign exchange in short supply, when necessary.

f) Priority for foreign exchange generating projects.

Special priority has been given to those projects generating foreign exchange through exports or import substitution so as to gain and maintain balance of payments equilibrium in the future.



Table A8.2  
(Continued)

MEASURES ADOPTED IN ORDER TO SOLVE THE GOVERNMENT'S  
FINANCIAL GAP

The following measures have been implemented with the purpose of increasing fiscal revenues:

a) 15% tax on exports of traditional products .

This tax, computed on the basis of the FOB price, was created in order to tap windfall profits generated by the devaluation. It is estimated that this tax will increase fiscal revenues by \$/ 7.8 billion during the second semester of this year.

b) Sales tax on gasoline .

This should generate \$/ 5.5 billion during the rest of this year. Other petroleum derivatives have not been affected.

c) Increase of the sales tax on goods and services .

All regulations relating to this tax have been integrated. The rate on luxury products has been increased from 27% to 40%, while the rate affecting most other products has risen from 17% to 20%. Taxes on foodstuffs and medicines have not been altered.

These increases are expected to provide \$/ 2.0 billion in new revenues during the second half of 1976.

d) Increase in effective tariffs for the imports of capital goods.

The rise in effective tariff rates, applied differentially according to the priority of the industry and the type of activity involved, will yield an additional revenue of \$/ 500 million by December of this year. This measure does not affect imports of goods already shipped.

Table A8.2  
(Continued)

e) The license plate tax has been tripled.

In addition, a tax of 50% in excess of this has been established for vehicles assembled abroad since 1970. This is expected to generate another S/ 700 million during the following semester.

f) Increase from 67% to 72.5% in the sales tax on cigarettes.

This measure, along with the authorized price rise of this product should increase fiscal revenues in 1976 by S/ 500 million.

g) Increase in mail and toll rates.

This is expected to yield around S/ 500 million this year.

Additional measures have been adopted, implementing an austerity policy for the whole of the public sector by reducing current and investment expenditures. Amongst these, the following are included:

a) Reduction in current expenditures.

The hiring of new personnel, as well as increases in salaries, for the public sector have been suspended until December 1976. In addition, purchases of goods and services have been severely restricted.

b) Reduction in investment expenditures.

Investment expenditures of the Central Government have been reduced by S/ 4.5 billion for the present 1975-76 fiscal budget. These budget cuts respond to the priority level of the corresponding investment projects, favouring those destined to support the balance of payments.

Table A8-2  
(Continued)

MEASURES RELATING TO STATE ENTERPRISES

a) Policy making in State Enterprises.

Measures have been implemented in order to rationalize and improve the efficiency of state enterprises by allowing them to function on a basis similar to that of private enterprises: managerial decision making, adequate working capital, a sound investment policy and debt structure, and a profit level at least equivalent to the cost of money in the capital market.

b) Reduction in Current Expenditures.

As a means of rationalizing current expenditures, a strict austerity policy has been adopted for state enterprises. Hiring may not exceed 2% over the June 30 level, and wages have been frozen for the rest of the year. Increases in other operation cost have been linked to, and may not exceed, increases in the cost of living index.

c) Reduction in Investment Expenditure.

Investment expenditures have been severely diminished by a total of S/ 9,666 million, affecting especially those projects not considered critical for balance of payments support by 1980.

d) Price Policy.

State enterprises have been authorized to adjust the prices or tariffs of the products or services they sell, in order to cover their costs and generate internal funds to act as a counterpart to the external financing of their investment programs or supply funds to the central government. These rises are expected to increase income by approximately S/ 11.5 billion, during the second semester of this year.

Table A8.2  
(Continued)

MEASURES ADOPTED IN ORDER TO INCREASE INTERNAL SAVINGS

These include the following:

- a) An average increase of 3% in the interest rate as from July 1.

This is designed to promote personal savings and protect them against internal price rises in the medium run. The mechanism modifying interest rates has been made more flexible in order to allow a more rapid response to future price developments.

- b) Business enterprises will only be allowed to distribute 10% of their paid capital from 1976 profits to shareholders.

In this way, greater revenues generated by price increases will result in a higher level of internal saving and reduce the demand for working capital from the banking system.

Non-distributed profits, which will increase enterprise's reserves, are allowed to be distributed after 1977.

- c) Reinvestment incentives.

Agricultural, industrial, fishing and mining enterprises have been allowed to invest profits during 1976-77, tax free, as part of their working capital. Previously this could only be done to increase fixed assets. This measure is designed to increase the enterprises' working capital.

- d) An expansion in the Central Government's current account savings.

This will result from increases in tax revenues and reductions in current expenditures.

Table A8.2  
(Continued)

MEASURES RELATING TO PRICES AND WAGES

a) Prices.

The stabilization program has been designed to reduce the demand for non-essential goods, especially those with a high imported component. This can be clearly seen by the higher prices of gasoline, cigarettes and other products resulting from the measures previously described.

In order to assure a normal operation on the part of business enterprises, these have been authorized to adjust the prices of their goods and services, including those imported, during the next 90 days, after which they will again be subject to controls.

Prices are expected to rise about 25% during the second semester as a result of the stabilization program.

b) Wages.

Wages have been increased by an average of 10% in order to reduce the impact of rising prices on purchasing power. This increase, however, has been applied on a progressive basis, so that lower income groups receive a higher rate. The minimum wage has also been increased for the same reason.

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Source: Central Bank, Aide Memoire on the Economic Stabilization Program of Peru, Lima, July 1976.

Annex 3

PROFILES ON SELECTED BANKS LENDING TO PERU

The study has made observations on certain banks throughout the various chapters of the study. This annex will attempt consolidate in a brief way the findings on some of the banks. Much of the terminology reflects that used in the body of the text. It should be made explicit that some aspects of the profile are subjective evaluations based on observed behavior with Peru and do not in any way pretend to be of an empirical nature.

1. Citicorp, U.S.A. Has had a branch in Lima since 1920. A major lender in the sixties and seventies as well as a major lead bank in syndication. While there is no indication that it undercut market terms with regard to the price of loans, it clearly was a sophisticated bank willing to take greater risks than many other big money center institutions. In the seventies, Citicorp had a relative commitment in Peru that was of an intermediate level vis-a-vis all other banks; however, it was considerably higher than most other big money center banks that had been lending to the government. Moreover, Citicorp actively participated in traditionally less preferred areas of finance such as refinance, free disposition and infrastructure. It made little use of export credit guarantees. And importantly, it provided finance for the transandean oil pipeline, a project of very high national priority. When negotiations began in 1976 for refinance relief without the presence of the IMF in 1976, Citicorp took a positive position and headed the Steering Committee of coordinating banks. When the banks' plans to monitor the economy failed in 1977, Citicorp refused to head any further Steering Committees and its position in negotiations hardened somewhat. However, it continued to be relatively flexible in on-going negotiations and was classified as having had a "soft" negotiating position among the major commercial lenders. In sum,

while not excessively aggressive, Citicorp has been a very important creditor with a generally flexible attitude (within a commercial context) in extending credits and resolving problems involving Peru. Citicorp was a creditor to the Cuacone project.

2. Wells Fargo, U.S.A. Not significantly present as a lender in the sixties, but probably the key commercial actor of the seventies. In this latter period, it came from nowhere to become a major lender and a major lead bank in syndication. Also, relative to its size, the institution had the highest commitment to Peru of any regular commercial bank. The bank achieved its status so quickly because of inside contacts and an aggressive lending posture up through 1974. A very high executive at the bank is a Peruvian national who had formerly worked at the Central Bank of Peru. The commercial bank's knowledge of the public sector and the Peruvian market gave Wells Fargo special leverage in the country. This was complemented by an aggressive lending strategy that saw the bank repeatedly undercut the prevailing market terms for Peruvian loans, thus making the bank instrumental in Peru's gaining acceptance in international markets and in the cheapening of credit for the government. The bank also managed to become a major lead bank in Peru (and internationally) by cleverly establishing working relationships with a wide number of small and intermediate-sized banks throughout the world that, incidentally, like Wells Fargo, were mostly newcomers to the international scene. The bank also appeared to have no preference about what it financed and made no significant use of export credit guarantees. Wells Fargo led two large syndicates to finance the oil pipeline. The institution's posture became more conservative after 1975, following general market behavior in the post-oil crisis period. The bank helped to finance the foreign private Cuacone copper project.

3. Manufacturers Hanover, U. S. A. Traditionally "Peru's banker". In the sixties this bank was probably the key lending institution, because of the volume of loans, its high relative commitment, and the fact that it was the major organizer of several large multi-institutional credits that helped the country through its fiscal and balance of payments crises. (It also was a major creditor to the private sector.) In the seventies, the bank appears to have taken a slightly more conservative view of the country, as there was some slippage in its relative commitment. However, it continued to be a major force in commercial finance via its maintenance of a position as a major creditor and its intermediate importance as a lead bank. While it did not show an aggressive posture with regard to the pricing of loans, it actively extended the traditionally less preferred refinance and free disposition credits. It participated in the finance of the oil pipeline and took little recourse to export credit guarantees. Manufacturers also indirectly helped Peru reach a settlement with the U. S. over various investment disputes, as a high ranking executive of the bank was the key negotiator in the settlement. During the post-1975 economic crisis this bank was very flexible (within a commercial context) and maintained an excellent image with both the public and private sectors; it has commonly been characterized as being a "reasonable" banking institution. When Citicorp withdrew as head of the bankers' Steering Committee in 1977, it was this bank which took its place. Manufacturers was a commercial lender to the foreign private Cuajone copper project.

4. Chemical Bank, U. S. A. Not a significant creditor in the sixties; however, in the seventies it became a lender of intermediate importance to the government. Nevertheless, Chemical probably had one of the most restrictive attitudes towards the military government. In the late 60's it bought into a local bank. However, the timing of the purchase was inappropriate as there



was much public concern about foreign participation in the financial sector; moreover, Chemical made no attempt to consult authorities prior to its acquisition. Its equity participation therefore was a source of irritation and was a prime mover in the civilian government's decision to Peruvianize local banks. This was followed by outright nationalization of the subsidiary by the military government. The bank made no secret of its displeasure with this action and with measures taken on other TNCs. While almost all major international banks had reentered the Peruvian public-sector market by 1973, Chemical was conspicuous by its absence. It entered only in 1974, and then very symbolically as a participant in a syndicated credit that was part of the formal settlement of the investment dispute with the U.S. government. Lending was more vigorous thereafter. Ironically, Chemical decided to enter the public sector market almost precisely at a time when the economic situation of the government was beginning to unravel. This bank helped to finance the foreign private Cuaajone copper project.

5. Morgan Guaranty Trust, U.S.A. A lender of minor importance in the sixties. In the seventies it was a lender of intermediate importance. Only of minor importance as a lead bank in syndication for the government. Never appeared to be very enthusiastic about Peru, reflected in a low level of relative commitment rather than in the nature of its lending or terms. This traditionally conservative bank took the symbolic role of heading the syndicated credit that was part of the settlement of the investment dispute with the U.S. During the economic crisis of the second half of the seventies this bank was considered a hardliner, resisting refinance without the presence of the IMF and continuously being in favor of measures to pressure the government into submitting to Fund discipline. Morgan was a creditor to the Cuaajone project developed by the U.S.-owned Southern Peru Copper Corp.

6. Bankers Trust, U.S.A. A major lender to Peru in the 1960s with a high relative commitment. In the seventies it showed a more cautious attitude; while the nature of its lending showed no strong preferences, it slipped to an

intermediate level of importance as a lender and there was a very marked fall in its relative commitment as well. It also revealed average maturities that were significantly shorter than those offered by the market. As a lead bank it was of minor importance. During the economic crisis in the second half of the seventies this bank took a hardline against the government's efforts to evade the IMF, or assuage the effects of its scrutiny. Bankers Trust participated in the finance of the Cuajone copper project.

7. Continental Illinois, U.S.A. A major lender to the government in the 1960's with a relatively high level of relative commitment. In the seventies there apparently was a much more cautious attitude; while showing no special preferences in the nature of its lending or terms, it fell to an intermediate level of importance as a lender and its relative commitment underwent sharp decline. During the economic crisis of the seventies this bank took a conservative position and was one of the hardliners which were adamant about the necessity of having the government submit to the IMF. Participated in the finance of the oil pipeline.

8. Bank of America, U.S.A. Has had a branch bank in Lima since 1966. It was a major creditor in both the sixties and the seventies. However, its level of relative commitment, while remaining basically unchanged in absolute terms over the period, was only at an intermediate level relative to other banks in the former period and was at a low level in the latter period. While the bank showed no special enthusiasm for government loans in the seventies, it did attempt to maintain its market position through the meeting of terms and conditions offered by the competition.

9. Chase Manhattan Bank, U.S.A. In the mid-sixties it bought into a Peruvian bank which was later nationalized by the military government. Compensation, however, was very prompt and quite lucrative for the bank. In both the 1960s and 1970s this institution was a major lender to the government. Compared to other banks

its relative commitment was of an intermediate and low level in the sixties and seventies, respectively. As a lead bank for the government it was of minor importance; however, it also led a large 200 million dollar credit for the Cuajone copper mine in the private sector. During the economic crisis after 1975 Chase fell into the group of hardliner banks. It also repeatedly interfered in the government's treatment of the Southern Peru Copper Corp, e.g. it reportedly threatened to tie the success of the 1978-1979 refinance negotiations with major private creditors to adequate settlement of a dispute over the handling of the foreign exchange resources of the Cuajone copper mine.

10. Crocker National Bank, U.S.A. A bank of intermediate importance as a lender in the sixties and seventies, of minor importance as a lead bank. Its relative commitments were at an intermediate level with respect to other banks in both periods. Appeared to be a rather aggressive lender in the early 1970's, both through price cutting and the nature of its lending. Participated in the finance of the oil pipeline. After 1975, notwithstanding what was a general change in the market environment, the bank's attitude turned rather conservative. It did not participate in the general refinance relief arranged by U.S. creditors in 1976, suggesting that it may have had one of the more hardline positions against the government's efforts to avoid the IMF. In the early 70's the bank had the uncommon practice of explicitly setting the legal jurisdiction of loans in Peru.

11. Bancal Tristate Corporation, U.S.A. Not a significant lender in the sixties, but of intermediate importance in the seventies. Had one of the highest relative commitments of any regular bank in this latter period, indicating a rather aggressive lending strategy towards Peru. However, after 1975 the bank appears to have turned rather conservative; like Crocker National it did not participate in the general refinance credit arranged by U.S. banks in 1976 that was designed to bail out the country's external accounts in the absence of the IMF.

12. American Express International, U.S.A. Not a significant lender in the sixties, but of intermediate importance in the seventies. Of minor importance as a lead bank. Had one of the highest relative commitments of any regular bank. Its style of lending was relatively aggressive. Participated basically in loans of refinance, free disposition and infrastructural projects.
13. First Chicago Corp. U.S.A. Not a significant lender in the sixties, but of intermediate importance as a lender in the seventies. Of minor importance as a lead bank. Had a low level of relative commitment. Appears to have maintained a restricted attitude on the military government as reflected in the fact that it held loans back until the government reached a formal settlement with the U.S. in 1974.
14. Bank of Nova Scotia, Canada. A lender of intermediate importance in both the sixties and seventies with a high intermediate position in terms of relative commitment. In the sixties it provided considerable short and medium term assistance to the financially-strapped civilian government. Not an aggressive lender in the 1970's, but it preserved its relatively high profile as a lender to the government. In the post-1975 economic crisis this bank was the representative of Canadian institutions in the Steering Committee and was considered to be one of the "soft" banks in the long series of negotiation with commercial creditors. Scotia Bank participated in the finance of the Cuajone project.
15. Dresdner Bank, Germany. Was not a significant lender in the sixties, but became of intermediate importance in the seventies. As a lead bank it was of intermediate importance. The bank's lending in the early seventies was rather aggressive and after Wells Fargo it probably was next in importance in terms of bringing general market acceptability and more favorable credit conditions to Peru. The bank led a major syndicated credit for the oil pipeline. In the post-1975 economic crisis the bank represented European institutions in the

private creditors' Steering Committee. A relatively strong advocate of the Peruvian position in negotiations during the economic crisis, this bank even extended the government a short term credit to help it pass international reserve targets of an IMF stand-by accord.

16. Bank of Tokyo, Japan. Has had a branch in Lima since 1965. Was a minor lender to the government in the sixties and was of intermediate importance in the seventies. Its relative commitment was low compared to other banks for both periods. As a lead bank it was of intermediate importance. This institution was a fairly aggressive lender in the early 1970s; not only did it get involved in price cutting, but it also had a relatively high proclivity for fixed interest rate loans and with great frequency extended the traditionally less attractive free disposition loans. The Bank of Tokyo was the Japanese representative in the private creditors' Steering Committee. Also a creditor for the private-foreign Cuajone project.

17. Credit Lyonnais, France. Has long had a subsidiary in Lima. Its participation was reduced to less than 20% after the military government's banking reform laws. Was not a significant lender in the sixties, but was classified as of intermediate importance in the seventies. Its relative commitment was low. As a lead bank it played a minor role in Peru. The bank's lending strategy was rather cautious and a high percentage of the credit extended had guarantees of the French export credit agency. However, in negotiations pursued during the post-1975 economic crisis, this institution was considered to be in the group of "soft" banks.

18. Lloyds Bank, U.K. Has had a branch in Lima since 1936. Was not a significant lender to the government in the sixties, but became a lender of intermediate importance in the seventies. Its relative commitment to Peru was low in both periods. As a lead bank it played a minor role. The bank appears to have pursued a slightly cautious lending strategy, with significant lending

for projects and capital goods imports. Helped to finance the oil pipeline. Lead bank for a 23.5 million dollar syndicated credit for Quajone.

19. Banca Commerciale Italiana, Italy. Has long held indirectly a subsidiary in Lima. Under the military government participation was reduced to below 20%. In the sixties it was a lender of minor importance, while in the seventies the institution was of intermediate importance. The bank was a lead bank of minor importance. Its relative commitment was low in both periods. Involved itself in price cutting in the early seventies, and the nature of its lending was somewhat bold with a high frequency of refinance loans and credits of free disposition. Participated in the finance of the oil pipeline.

20. Schroders Ltd. U.K; National and Commercial Banking Group, U.K; Banque Francaise du Commerce Extérieur, France; Banque de l'Indochine et de Suez, France; Algemene Bank Nederland, Holland; Amro Bank, Holland; Compagnie Financiere de Paris et des Pays-Bas, France; and Banque Worms, France. All would be considered to have had a conservative lending strategy in the seventies due to the fact that a very high percentage of loans was covered by home country export credit guarantees.

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