

PO - CH/NL/0348



PART B

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Begins : 12/8/88 .
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PO -CH /NL/0348

PART B

Chancellor's (Lawson) Papers:

NIGERIAN AID AND THE
INTERNATIONAL MONETARY
FUND

DD 's : 25 Year



17/11/95

PO -CH /NL/0348
PART B

BF 23/8

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160262
MDLIAN 9370

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FM LAGOS

TO PRIORITY FCO

TELNO 868

OF 121148Z AUGUST 88

INFO PRIORITY TREASURY, ECGD, BANK OF ENGLAND, DTI, ODA

INFO PRIORITY UKDEL IMF/IBRD WASHINGTON

INFO ROUTINE ABIDJAN (FOR UK DIRECTOR AFDB), KADUNA

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✓

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MY TELNO 856: NIGERIA/IMF

belmont

SUMMARY

1. CENTRAL BANK GOVERNOR IN LONDON. NEXT STEPS. NO DIVERGENCE OF VIEW BETWEEN WORLD BANK AND IMF. FOREIGN EXCHANGE MARKET THE MAIN PROBLEM AREA BETWEEN THEM AND NIGERIA.

DETAIL

2. HUSAIN HAS CALLED TO BRIEF ME ON THE OUTCOME OF THE IMF'S MISSION. HE WAS ABLE TO GIVE SOME ADDITIONAL INFORMATION TO WHAT JIMENEZ HAD TOLD MORRICE ON 6 AUGUST (MY TUR). AHMED, GOVERNOR OF THE CENTRAL BANK, WHO TRAVELLED TO LONDON ON 10 AUGUST, WILL LEAD THE NIGERIAN TEAM AT THE LONDON CLUB IN TALKS IN WEEK BEGINNING 15 AUGUST. HE WILL EXPLAIN TO THE BANKS HOW NIGERIA WILL CONTINUE TO HONOUR HER COMMITMENTS. MINISTER OF STATE (ALHAJI ABUBAKAR ALHAJI - AAA) MAY ALSO PARTICIPATE BUT AHMED WOULD REMAIN IN THE LEAD. WE HAVE ALSO LEARNED THAT OKONGWU, MINISTER OF FINANCE, IS IN LONDON, BUT HE IS RECOVERING FROM AN ILLNESS AND WE ASSUME IS UNLIKELY TO ATTEND THE LONDON CLUB MEETINGS.

3. THEREAFTER, NEXT STEP WOULD BE COMPLETION BY 31 AUGUST OF THE NEGOTIATIONS BETWEEN THE WORLD BANK AND THE NIGERIANS ON THE FORMER'S TRADE POLICY LOAN. AHMED AND AAA WOULD BE IN WASHINGTON FROM 5-7 SEPTEMBER TO GIVE THE NIGERIAN REACTIONS TO THE IMF'S PROPOSALS. THIS WOULD GIVE TIME FOR DATA EVALUATION TO BE COMPLETED AND FOR DETAILS OF THE AGREEMENT TO BE PRESENTED IN NIGERIA. WHICHEVER WAY THE WASHINGTON TALKS WENT, JAY COX, VICE-PRESIDENT (AFRICA) OF IBRD, WOULD COME TO LAGOS AROUND 12 SEPTEMBER EITHER TO PUT FINAL SEAL ON THE AGREEMENT OR TO SORT OUT ANY LAST MINUTE PROBLEMS.

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4. HUSAIN SAID THEY HOPED THAT THE WORLD BANK'S ARRANGEMENTS FOR NIGERIA WOULD BE PRESENTED TO THE IBRD BOARD IN OCTOBER AND THE IMF/NIGERIA AGREEMENT TO THE IMF BOARD LATER IN OCTOBER. IBRD WOULD BE FREE TO RELEASE ITS TRADE POLICY LOAN AS SOON AS NIGERIANS SIGNED AN AGREED LETTER OF INTENT. ANY PROPOSALS FOR FURTHER RESCHEDULING OF DEBTS ALREADY RESCHEDULED WOULD GO TO THE PARIS CLUB AT ABOUT THE SAME TIME OR SLIGHTLY LATER. IMF/IBRD FINAL PROPOSALS FOR CLOSING THE EVENTUAL FINANCING GAP FOR NIGERIA WOULD INEVITABLY DEPEND ON PRIOR DECISIONS ABOUT NEW MONEY COMMITTED BY THE LONDON AND PARIS CLUBS.

5. HUSAIN LARGELY CONFIRMED WHAT JIMENEZ HAD SAID ABOUT BUDGETARY EXPENDITURE. THE IMF TEAM HAD BEEN SATISFIED THAT THE NIGERIANS WERE DOING ALL THAT COULD BE EXPECTED OF THEM TO BRING THE BUDGET DEFICIT DOWN TO MANAGEABLE PROPORTIONS.

6. HUSAIN AGREED THAT A MAJOR PROBLEM REMAINED OVER THE FOREIGN EXCHANGE MARKET (FEM). ONE POSSIBILITY WAS TO PHASE OUT THE FEM RATE AND RELY ONLY ON THE INTER-BANK RATE, WHICH WOULD NEED TO BE SUITABLY ADJUSTED. HOWEVER, THERE WERE STILL THE QUESTIONS OF WHICH RATE AND HOW MUCH FUNDING WOULD BE POLITICALLY ACCEPTABLE. THE IMF PROPOSAL OF US DOLLARS 80 MILLION PER FORTNIGHT HAD BEEN REJECTED, AS TOO LITTLE FOR NIGERIA'S MINIMUM REQUIREMENTS. BUT THE NIGERIANS SEEMED TO ACKNOWLEDGE THE NEED FOR A REDUCTION, TO BE ACHIEVED EITHER BY LETTING NAIRA RATE FLOAT FURTHER DOWN OR BY OTHER MEANS.

7. HUSAIN WAS UNCLEAR AS TO PRECISELY WHAT THE NIGERIAN WOULD NOW ASK FOR IN TERMS OF DEBT RESCHEDULING. 1988 AND 1989 MATURITIES WOULD HAVE TO BE RESCHEDULED BUT SO MIGHT THE INTEREST DUE ON DEBT ALREADY RESCHEDULED UP TO DECEMBER 1987.

8. I DESCRIBED TO HUSAIN THE IRRITATION AND DISAPPOINTMENT FELT IN LONDON OVER THE FAILURE TO PAY MORATORIUM DEBT INTEREST DUE ON 30 JUNE 1987. HE SUGGESTED THAT WE SHOULD PRESS THE GOVERNOR OVER THIS WHILE HE IS IN LONDON AND ALSO OVER OTHER TROUBLESOME DEBTS SUCH AS THOSE TO BRITISH AIRWAYS AND BRITISH AEROSPACE, SINCE THE RELEASE OF FOREIGN EXCHANGE FOR THESE PAYMENTS WILL REQUIRE HIS PERSONAL APPROVAL. I AM

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TELEGRAPHING SEPARATELY ABOUT THIS.

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ADDITIONAL 1

MR WICKS NO 10 DOWNING ST

NNNN

FROM: MR P MOUNTFIELD
DATE: 14 SEPTEMBER 1988

CHANCELLOR OF THE EXCHEQUER

cc: Chief Secretary
Economic Secretary
Sir P Middleton
Sir G Littler
Mr Lankester
Mr Evans
Mr Walsh
Mr Bottrill
Mr P Davis
Mr Gieve
Mrs Thomson

*Thanks.
OK.*

Ch. Agree with M.M.'s recommendation?

*JC
16/9*

NIGERIA: IMF, PARIS CLUB, ETC

The pace of negotiations on the next round is hotting-up. There is a preliminary meeting with the Chairman of the Paris Club on Monday, which I shall attend. This note seeks your instructions on the line to take then.

Background: Nigerian economy

2. After the disastrous budget introduced in January, things predictably got worse during the year. Credit expansion accelerated. The public sector deficit rose; foreign exchange reserves were almost exhausted; debt service payments became sporadic; the exchange rate was allowed to appreciate to an unrealistic level; and at the same time, public resistance to modest energy price increases was used as an excuse to postpone further adjustment.

3. From the early summer, there were signs that the "sound men" had reasserted control. Okongwu became largely discredited, and

many of his functions were transferred to his former Permanent Secretary, Alhaji ("AAA"), who was made Minister of Budget and Planning. The Central Bank Governor (Ahmed) re-emerged as a man with the confidence of the President. Falae, the Secretary of the Military Government, backed the reformers. New negotiations began with the commercial banks, and subsequently with the IMF and the IBRD. Some corrective action has already been taken; more is planned for the new budget at the end of the year. Meanwhile, the fall in the oil price has further undermined the present policy, and made adjustment even more essential.

IMF programme

4. We have no hard details yet. We are doubtful whether the degree of adjustment will match the limited finance likely to be available or provide for contingencies such as a continuation of the present low oil price. But the Fund assure us that agreement on a Letter of Intent is close. The actions already taken on the budgetary side are seen as helpful. The Fund seems to have postponed its insistence on immediate increases in petroleum product prices. They seem prepared, also, to agree to the abandonment of the foreign exchange auction system (which has fluctuated wildly, and is easily manipulated) in favour of an administered system which will - in theory - track the secondary market rate more closely. A fresh Fund mission goes to Lagos at the beginning of October; judgement reserved until we see their report. But the assumption is that an agreement with the Fund will be reached during October. We shall press now for the Fund's assumptions on adjustment and financing to be both realistic and consistent. We do not want to be faced with an inadequate programme, but we can postpone a final decision on whether to support it at the Board until we have seen the final version. There will of course be a great deal of political pressure from FCO and No.10 to support it.

Commercial banks

5. Agreement was virtually reached with the banks in July on a fresh rescheduling package, which postpones payment of all the medium and long-term debt; gives a breathing space for the payment of short-term debt (which has already been rolled over once, and in some cases twice); but provides no new money. The banks, however, are insisting on being paid last year's interest arrears on letters of credit and will continue to receive interest without providing any new money. They will therefore be reducing their exposure in Nigeria. Final agreement has been postponed. Ahmed tells us this is because he feels he has a duty to the government creditors, not to leave them at the end of the queue (and therefore, as financiers of last resort); this is mainly presentational, because he has little chance of squeezing more new money out of the banks. Indeed Barclays tell us that the banks are prepared to walk away rather than concede new money.

Paris Club

6. So the Paris Club may provide the residual finance after all. The balance of payments projections we have so far seen from the IMF suggest that, even if the banks do all that has been promised so far, and making allowances for IBRD and ADB lending, as well as bilateral lending from Japan, there is still a very wide financing gap. Taking 1988 and 1989 together (a sensible assumption, since we are now so late in the year) it seems likely that the Paris Club will have to reschedule all new principal falling due; current interest; and at least part, and probably all, of the "moratorium interest" due on previously-rescheduled debt under earlier agreements. The total sums to be consolidated may be of the order of \$4 billion; the UK share is about £700 million. The UK has been paid one instalment of moratorium interest; the second due in June, has not been received although it is said that the necessary instructions have just been issued. The working assumption is that Nigeria will bring its payments to other creditors upto that date as well, and reschedule the rest.

7. The object of next week's informal meeting (which we helped to set up) is to let the Nigerians explore with the French chairman (with help from the IMF and ourselves) the need for debt relief, and the amount which, realistically, they can expect to receive. I have talked round the other main creditors. The Americans will do "whatever the figures seem to justify". The Germans and French, like us very large creditors, recognise the need for significant relief, including some part of the moratorium interest. All agree that it would be unwise to offer "Toronto terms" to Nigeria. Although it will probably qualify, in due course, on per-capita income terms, it is a very big debtor, with long-term prospects (including LNG as well as oil) far better than those of the really poor countries. Anyway, to press for Toronto terms at this stage would imperil the chances of an agreement on your initiative, and might wreck the chances of a deal for Nigeria as well. The people in the IMF who deal with debt questions are also anxious not to imperil the chances of an agreement, and urge us to avoid anything "too exotic" at this stage. Toronto terms would not, in practice, help Nigerian cash-flow in 1988 or 1989 anyway, so long as all the moratorium interest falling due in those years has to be rescheduled (which gives them 100 per cent relief, and not just 33 per cent). We anticipate quite a lot of trouble with the smaller creditors, particularly those who have had great difficulty in establishing debt lists, or who have experienced delays in payments under previous agreements. We also think it will be wise to confine the consolidation period to 1988 and 1989 (the period likely to be covered by an IMF programme) despite the fact that the agreement with the banks runs for a longer period. We do not know what length of rescheduling will be requested, but it is likely to exceed 15 years. The Banks have agreed to reschedule letters of credit over 14 years. The Paris Club will probably stick at 10.

Recommendation

8. If you agree, I should like to confirm this line at the meeting in Paris on Monday, and join forces with the French and the IMF in lowering Nigerian expectations to a realistic level. I shall obviously avoid committing the UK on the question of the IMF programme at this stage; but I would like to indicate (explicitly with your support) that provided the programme contains adequate adjustment measures and financing, we shall back it at the Board, and will also strongly support a debt relief programme on the lines indicated above i.e. including moratorium interest if absolutely necessary.

[Amendment
telephoned by
Mr. Mountfield]

R1

P MOUNTFIELD



FROM: J M G TAYLOR
DATE: 19 September 1988

Php

MR MOUNTFIELD

cc Chief Secretary
Economic Secretary
Sir P Middleton
Sir G Littler
Mr Lankester
Mr Evans
Mr Walsh
Mr Bottrill
Mr P Davis
Mr Gieve
Mrs Thomson

NIGERIA: IMF, PARIS CLUB, ETC

The Chancellor was grateful for your minute of 14 September. He is content with the line you propose to take.

JMG

J M G TAYLOR

From P Mounthuid
Date 10 October 88

Chief Secretary

Ch,

To be aware.

cc Chancellor —
Mr Lankester
Mr Boltrill

10/10 ✓

pm

NIGERIA : EXPORT CREDIT COVER

We have been warned that the Chairman of Bwaters, Adrian White, may lobby Ministers at Brighton about a major irrigation project in Nigeria (in President Babangida's home state). His main target will be Lord Young, but he may also approach you.

The scheme depends on ECGD cover. This is at present held up because of Nigeria's continuing debt problems. (There are significant arrears due to ECGD; and these are likely to be caught up in a major rescheduling later this year). Unfortunately there is a high degree of political commitment, because of the President's personal ~~com~~ involvement, this was the one project singled out for half-promises of support when the Prime Minister visited Nigeria earlier this year.

Line to take: Recognise importance of project. But Nigeria in serious difficulty - made very much worse by latest fall in oil price. Can't service existing debt; shouldn't be encouraged to borrow more, except for projects which pay for themselves in foreign exchange. Currently waiting for report from IMF. Will reconsider thereafter. No promises; and wrong to arouse expectations. But will take your points seriously.

Apologies for late-night ms

RM



P. Wanless
FROM: P T WANLESS
DATE: 13 October 1988

MR MOUNTFIELD

cc: Chancellor - 2
Mr Lankester
Mr Bottrill

NIGERIA: EXPORT CREDIT COVER

Thank you for your note of 10 October. The Chief Secretary found this most helpful.

P. Wanless

PETER WANLESS
Assistant Private Secretary

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FM FCO

TO IMMEDIATE UKDEL IMF/IBRD WASHINGTON
TELNO 186
OF 170026Z OCTOBER 88
INFO IMMEDIATE LAGOS, PARIS

PARIS FOR MOUNTFIELD.

IMF MISSION TO NIGERIA

SUMMARY

1. NIGERIAN POLICY MEASURES FALL SHORT OF IMF MANAGEMENT'S REQUEST BUT MISSION CHIEF IS RETURNING TO WASHINGTON WITH A DRAFT LETTER OF INTENT FOR CONSIDERATION BY CAMDESSUS. EXTERNAL FINANCING GAP REMAINS LARGE AND TREATMENT OF ARREARS TO PARIS CLUB CREDITORS COULD CREATE A PROBLEM.

DETAIL

2. JIMENEZ, LEADER OF THE IMF MISSION TO LAGOS, CALLED TO SEE LANKESTER (TREASURY) ON HIS WAY BACK TO WASHINGTON. HE REPORTED THAT ALTHOUGH THE NIGERIANS HAD TAKEN A NUMBER OF USEFUL POLICY MEASURES, THEY WERE NOT ENOUGH TO SATISFY THE BRIEF THAT HE HAD RECEIVED FROM IMF MANAGEMENT LONG HYPHEN ALTHOUGH THEY WERE PROBABLY THE MOST THAT THE NIGERIANS WERE PREPARED TO UNDERTAKE.

3. THE FUND WAS SEEKING A MAJOR IMPROVEMENT IN BOTH BUDGETARY AND CREDIT POLICIES. THE NIGERIAN AUTHORITIES WERE NOW ACHIEVING BETTER CONTROL OF PUBLIC EXPENDITURE AFTER SUBSTANTIAL OVER-RUNS IN THE FIRST HALF OF THE YEAR. CAPITAL WARRANTS HAD BEEN FROZEN, AND AAA BACKED BY THE PRESIDENT WAS RESISTING FIRMLY ANY EXTRA BUDGETARY EXPENDITURES.

4. THE GOVERNMENT WAS AIMING TO KEEP EXPENDITURE IN CASH TERMS IN 1989 CLOSE TO THE LIKELY 1988 OUTTURN. CAPITAL SPENDING REQUESTS OF NAIRA 49 BILLION WERE BEING TRIMMED TO NAIRA 7 BILLION LONG HYPHEN ALTHOUGH THIS WOULD STILL BE HIGHER THAN THE NAIRA 6.5 BILLION THIS YEAR. THE AUTHORITIES AIMED TO REDUCE SUBSIDIES TO PARASTATALS BY INCREASING PRICES. TELEPHONE CHARGES HAD ALREADY BEEN RAISED. ELECTRICITY PRICES WERE PLANNED TO RISE LATER IN THE YEAR. NIGERIAN AIRLINES WAS ALSO BEING RESTRUCTURED.

5. ON THE REVENUE SIDE, THE NIGERIANS WERE CONTEMPLATING SOME ADDITIONAL REVENUE MEASURES LONG HYPHEN QUOTE BUT NOT ENOUGH TO SATISFY IMF MANAGEMENT UNQUOTE. JIMENEZ DID NOT ELABORATE ON THE PRECISE MEASURES THE FUND WERE SEEKING.

6. THE RAPID EXPANSION OF CREDIT WAS A PARTICULAR CONCERN TO TO THE FUND. THE NEW CASH RATIOS INTRODUCED BY THE CENTRAL BANK HAD BEGUN TO BITEOUT CREDIT GROWTH PARTICULARLY TO THE GOVERNMENT WAS STILL RAPID. THE MONEY SUPPLY WAS LIKELY TO INCREASE BY AROUND 30 PER CENT IN 1988 LONG HYPHEN ACCOMPANIED BY INFLATION AT A SIMILAR RATE. IT WAS PROVING DIFFICULT TO PERSUADE THE NIGERIANS TO TAKE THE NECESSARY ACTION ON INTEREST RATES.
7. THE NIGERIANS, HOWEVER, DID APPEAR TO BE READY TO CONTEMPLATE TAKING MEASURES ON THE EXCHANGE RATE.
8. THE REAL ECONOMY WAS SHOWING SOME IMPROVEMENT COMPARED TO 1987 WITH A HIGHER LEVEL OF CAPACITY UTILISATION IN INDUSTRY AND IMPROVED AGRICULTURAL OUTPUT PARTLY AS A RESULT OF BETTER WEATHER.
9. THE CURRENT BALANCE OF PAYMENTS, HOWEVER, STILL SEEMED LIKELY TO SHOW A DEFICIT OF DOLLAR 1.8 BILLION IN 1988 AND DOLLAR 2.4 BILLION IN 1989 COMPARED TO DOLLAR 1.1 BILLION IN 1987 (BASED ON FIGURES JIMENEZ LEFT WITH THE BANK OF ENGLAND. PLEASE PROTECT). THE WORSENING IN THE CURRENT DEFICIT REFLECTED LARGELY THE RESULT OF LOWER OIL PRICES WHICH WERE NOT BEING OFFSET WHOLLY BY HIGHER OUTPUT. JIMENEZ UNDERSTOOD OIL PRODUCTION WAS RUNNING AT ABOUT 1.4 MBD. HE WAS ASSUMING THE OIL PRICE WOULD RECOVER CLOSE TO DOLLAR 15 A BARREL IN 1989. IMPORTS WERE LIKELY TO BE SLIGHTLY LOWER IN VALUE TERMS IN 1988 THAN LAST YEAR WHICH IMPLIED A SIGNIFICANT VOLUME REDUCTION.
10. JIMENEZ SAID THE BALANCE OF PAYMENTS OUTTURN WAS OF COURSE HIGHLY SENSITIVE TO OIL PRICES. NEVERTHELESS, HE BELIEVED THAT CURRENT DEFICITS OF THIS MAGNITUDE COULD BE FINANCED LONG HYPHEN ALBEIT WITH A MAJOR EFFORT BY CREDITORS. THE NIGERIANS WERE NOT LIKELY TO WANT TO DRAW ON FUND MONEY LONG HYPHEN ALTHOUGH IF THEY DID A SUBSTANTIAL SUM OF ABOUT DOLLAR 300 MILLION COULD BE AVAILABLE UP FRONT AS PART OF A DOLLAR 600 MILLION SBA. SOME DOLLAR 900 MILLION OF GROSS NEW BALANCE OF PAYMENTS LOANS FROM THE IBRD, THE AFRICAN DEVELOPMENT BANK AND THE JAPANESE WOULD BE AVAILABLE IN 1989. THE BULK OF THE REST OF THE FINANCING, HOWEVER, WOULD NEED TO COME FROM PARIS CLUB CREDITORS WHO THE FUND ASSUMED WOULD BE PREPARED TO RESCHEDULE 100 PER CENT OF ORIGINAL MATURITIES, AMORTISATION ON PREVIOUSLY RESCHEDULED DEBT AND MORATORIUM INTEREST. THE FUND WAS LOOKING FOR A SMALL REBUILDING OF NIGERIA'S RESERVES IN 1989.
11. JIMENEZ WAS CONCERNED THAT THE UNEVEN RECEIPT OF INTEREST PAYMENTS BY DIFFERENT PARIS CLUB CREDITORS IN 1988 MIGHT

HINDER A RESCHEDULING. HE ASKED US TO SOUND OTHER CREDITORS AS TO WHETHER THEY WERE PREPARED TO ACCEPT 1 JANUARY 1988 FOR THE START OF THE CONSOLIDATION PERIOD. IF THEY INSISTED ON A 1 JULY 1988 START DATE, THEN THE NIGERIANS WOULD NEED TO FIND AN EXTRA DOLLAR 300 MILLION TO CLEAR ARREARS AND BRING ALL CREDITORS UP TO THE SAME LEVEL. IF THE NIGERIANS WERE PREPARED TO DRAW IMF MONEY THIS COULD FILL THE GAP.

12. JIMENEZ SAID NIGERIA NEEDED A LONG PERIOD OF ADJUSTMENT. AAA, FALAE AND THE SMALL TEAM AROUND THE PRESIDENT WERE TRYING TO TAKE SENSIBLE DOMESTIC ECONOMIC MEASURES AND KEEP NIGERIA IN TOUCH WITH ITS INTERNATIONAL CREDITORS. IF THEY FAILED, OTHER PEOPLE COULD TAKE OVER. OTHER MINISTERS WERE NOT COMMITTED TO ECONOMIC REFORM.

13. THE NEXT STEP WILL BE FOR JIMENEZ TO REPORT TO IMF MANAGEMENT. THE ACTIONS ON THE BUDGET, INTEREST RATES AND THE EXCHANGE RATE FELL SHORT OF WHAT WAS REQUIRED. IF FUND MANAGEMENT NEVERTHELESS AGREED TO ACCEPT THE LETTER OF INTENT AS THE BASIS FOR A PROGRAMME HE BELIEVED THAT PRIOR ACTIONS WOULD BE NEEDED ON THE PUBLIC EXPENDITURE TARGETS FOR 1989, REVENUE MEASURES AND THE EXCHANGE RATE SYSTEM.

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TELNO 1062

OF 200915Z OCTOBER 88

INFO PRIORITY TREASURY, BANK OF ENGLAND, DTI, ECGD, WASHINGTON

A large, stylized handwritten signature in black ink is located in the upper right quadrant. To its left, a red checkmark is drawn, with a red arrow pointing from the checkmark towards the signature.

NIGERIAN ECONOMY

1. DURING A CALL ON OKONGWU, MINISTER OF FINANCE, ON 18 OCTOBER, HE SAID THAT HE HAD SEEN THE IMF TEAM, NOW IN LAGOS, AND WAS CONFIDENT THAT THEY COULD REACH AGREEMENT DURING THE CURRENT VISIT. HE SAID THE TEAM HAD BEEN CRITICAL HOWEVER OF THE UNEVEN WAY IN WHICH NIGERIA HAD BEEN PAYING ITS MORATORIUM INTEREST WHICH HAD DISRUPTED THE SOLIDARITY OF SUPPORT PARTICULARLY IN THE PARIS CLUB, AND SAID HE HAD BEEN URGED TO EVEN UP THE PAYMENTS, PAYING PARTICULAR HEED TO THOSE COUNTRIES WHICH AS YET HAD RECEIVED NONE. I STRESSED THE NEED FOR COMPLETING OUR MORATORIUM INTEREST PAYMENTS DUE ON 30 JUNE AND POINTED OUT HOW MUCH WAS HANGING ON THE MEETING OF THIS COMMITMENT. OKONGWU SAID THE FULL PAYMENTS HAD BEEN AUTHORISED BY THE MINISTRY OF FINANCE AND IT WAS NOW A QUESTION OF THE CENTRAL BANK FINDING THE FUNDS.

2. OKONGWU ALSO MADE A PITCH FOR THE CREATION OF A CONSULTATIVE GROUP FOR NIGERIA WITH THE UK TAKING THE LEAD. I RESPONDED THAT ALTHOUGH WE HAD GIVEN SOME THOUGHT TO THE SUGGESTION WE HAD DOUBTS ABOUT WHETHER IT WAS THE RIGHT ANSWER AT THIS TIME.

3. I HAVE ARRANGED TO MEET JIMENEZ, LEADER OF THE IMF TEAM, ON FRIDAY 21 OCTOBER, FOR AN ACCOUNT OF THEIR VISIT.

HEAP

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FM LAGOS

TO IMMEDIATE DESKBY 251730Z FCO

TELNO 1076

OF 251600Z OCTOBER 1988

AND TO IMMEDIATE DESKBY 251730Z TREASURY (FOR LANKESTER, DUS)

AND TO IMMEDIATE DESKBY 251730Z BANK OF ENGLAND (FOR MAYES)

INFO PRIORITY ECGD, DTI, ODA, PARIS (FOR MOUNTFIELD),

INFO PRIORITY UKDEL IMF/IBRD WASHINGTON, ABDIJAN (FOR UK

EXECUTIVE DIRECTOR AFDB).

MY TELNO 1068: IMF MISSION TO NIGERIA

SUMMARY

1. NEGOTIATIONS CONTINUE BETWEEN IMF AND NIGERIAN GOVERNMENT. NO MAJOR BREAKTHROUGH, BUT STARK REALITIES BECOMING INCREASINGLY EVIDENT. PROGRESS IN PART MAY BE DEPENDENT UPON WILLINGNESS OF CREDITORS TO KEEP NIGERIA AFLOAT.

DETAIL

2. I SAW JIMENEZ, LEADER OF THE IMF MISSION TO NIGERIA, THIS MORNING (25 OCTOBER) FOR AN ASSESSMENT OF HIS VISIT. JIMENEZ PLANS TO LEAVE TONIGHT, AND TO CALL ON TREASURY (LANKESTER) AND BANK OF ENGLAND TOMORROW MORNING 26 OCTOBER. HE MADE THE FOLLOWING POINTS:

(A) THERE TENDED, ON THE ONE HAND, TO BE INSUFFICIENT APPRECIATION IN CREDITOR COUNTRIES OF HOW MUCH THE NIGERIANS HAD DONE TO GET TO GRIPS WITH THEIR ECONOMIC DIFFICULTIES AND THE POLITICAL AND SOCIAL RISKS INVOLVED IN DOING SIGNIFICANTLY MORE, AND ON THE OTHER HAND A FAILURE ON THE PART OF THE NIGERIANS THEMSELVES TO RECOGNISE JUST HOW SERIOUS THEIR SITUATION WAS. THIS LED TO EXAGGERATED EXPECTATIONS OF HOW FAST THINGS COULD BE IMPROVED.

(B) THE SIZE OF THE DEBT BURDEN AND THE WEAKNESS OF THE OIL PRICE OVERSHADOWED ALL OTHER FACTORS. THE FALL IN OIL PRICE HAD CAUSED THE IMF TO REVISE THEIR ASSUMPTIONS ABOUT FUTURE REVENUE SINCE THE PARIS CLUB BRIEFING ON 20 SEPTEMBER. THE OVERALL SIZE OF NIGERIA'S DEPT WAS BEING REVISED SIGNIFICANTLY UPWARDS IN THE LIGHT OF FURTHER DEBT RECONCILIATION AND OTHER NEW INFORMATION INCLUDING LETTERS OF CREDIT ARREARS. JIMENEZ

ESTIMATED THAT TOTAL ARREARS AT THE END OF 1988 WOULD AMOUNT TO US DOLLARS 5.5 BILLION, WITHOUT THE SAME AMOUNT FALLING DUE FOR PAYMENT IN 1989. YET HE DID NOT SEE HOW THE NIGERIANS COULD POSSIBLY AFFORD TO PAY IN 1989 MORE THAN ABOUT US DOLLARS 2.5 BILLION. HENCE THE NEED FOR DRASTIC RESCHEDULING AND PROBABLY OTHER MEASURES.

(C) THE NIGERIANS WERE GIVING PRIORITY TO PAYING THE MULTI-LATERAL AGENCIES AND PROMISSORY NOTE HOLDERS. THE LONDON CLUB SETTLEMENT, ALTHOUGH BENEFICIAL IN THE LONG RUN, DID ENTAIL SUBSTANTIAL PAYMENTS FOR THE REST OF THIS YEAR AND NEXT. THEREFORE A CONSIDERABLE PRESSURE FELL ON THE PARIS CLUB.

(D) THE DISPARITY IN MORATORIUM INTEREST PAYMENT TO PARIS CLUB MEMBERS WAS A MAJOR DIFFICULTY. BECAUSE SOME, LIKE OURSELVES, HAD BEEN PAID MONIES DUE ON 30 JUNE THIS YEAR, THE CUT-OFF DATE FOR PAYMENTS MIGHT HAVE TO BE 1 JULY. THE NIGERIANS HAD PAID SOME OF THE MAIN CREDITORS, SUCH AS OURSELVES, AHEAD OF THE OTHERS, IN THE HOPE THAT THESE PAYMENTS WOULD HAVE RELEASED NEW CREDITS. NOW THEY WOULD HAVE TO EVEN UP THE PAYMENTS. JIMENEZ CONFIRMED IN RESONSE TO MY QUESTION THAT THIS MEANT THAT OUR PROSPECTS FOR OUR GETTING EARLY PAYMENT OF THE OUTSTANDING 30 JUNE MORATORIUM INTEREST WERE POOR.

(E) A FURTHER DIFFICULTY WAS THE NEED TO RESTRICT THE NAIRA DEFICIT. EVEN AFTER CAREFUL SCRUTINY, BIDS BY FEDERAL MINISTRIES FOR CAPITAL EXPENDITURE IN 1989 TOTALLED N49 BILLION. THE IMF CALCULATED THAT ONLY ABOUT N6.5 BILLION WOULD BE AVAILABLE. THIS AMPLY ILLUSTRATED THE SIZE OF THE PROBLEM.

(F) ALHAJI ABUBAKER ALHAJI (AAA), THE MINISTER OF STATE FOR BUDGET AND PLANNING, HAD BEEN LEADING THE NIGERIAN TEAM (WITH FINANCE MINISTER, OKONGWU, EFFECTIVELY SIDELINED), AND HAD ADDED MUCH REALISM AND FORCEFULNESS TO THE NIGERIAN POSITION. THE IMF THOUGHT HE WAS THE BEST ALLY THEY WERE LIKELY TO HAVE IN SUCH A POSITION. JIMENEZ SAID THAT HE FEARED THAT IF DEMANDS PUT UPON AAA BY THE CREDITORS WERE TOO UNREALISTIC, THEN LESS INFORMED AND MORE SENIOR MEMBERS OF THE GOVERNMENT MIGHT PUSH HIM OUT. THERE WAS INDEED A SIMILAR DANGER FOR THE FUTURE OF THE BABANGIDA ADMINISTRATION AS A WHOLE, THESE WERE POITICAL MATTERS OUTSIDE THE SCOPE OF THE IMF THAT THE CREDITORS WOULD HAVE TO CONSIDER.

(G) INDEED, THE PROBLEMS WERE MORE POLITICAL THAN ECONOMIC, GIVEN THE SIZE OF THE CUTS IN EXPENDITURE THAT WOULD BE REQUIRED TO CLOSE

THE FINANCING GAP. JIMENEZ WAS DUE TO MEET BOTH AAA AND THE CENTRAL BANK AFTER OUR MEETING, WHEN HE EXPECTED THEM TO PRESENT COUNTER-PROPOSALS TO THOSE PROPOSED BY THE IMF TEAM FOR ACHIEVING THIS. HE COULD NOT YET PREDICT THE OUTCOME. HOWEVER, AAA WAS WELL AWARE OF THE IMPORTANCE OF REACHING SOME SORT OF ACCORD WITH THE IMF. JIMENEZ FELT THAT THERE WAS PERHAPS A FIFTY-FIFTY CHANCE OF ACHIEVING AN AGREEMENT WHICH ALL CONCERNED COULD LIVE WITH, BUT THIS DEPENDED VERY MUCH ON A POLITICAL CONSENSUS AMONG THE CREDITORS THAT IT WAS BETTER TO PAY A PRICE TO KEEP THE NIGERIAN SHIP AFLOAT THAN FORCE MEASURES THAT WOULD CAUSE IT TO SINK. IT MIGHT TAKE LONGER THAN PREVIOUSLY ANTICIPATED TO PUT AN AGREEMENT TOGETHER, BUT MUCH DEPENDED ON WHAT PROPOSALS THE NIGERIANS CAME UP WITH AT THE FINAL MEETING.

(H) JIMENEZ SAID THAT THE EXCHANGE RATE WAS A FURTHER WORRY. THE NIGERIANS, SENSIBLY, WERE THINKING OF ABOLISHING THE FORTNIGHTLY AUCTION AND HAVING A SINGLE INTER-BANK MARKET TO WHICH THE CENTRAL BANK COULD CONTRIBUTE WHATEVER FUNDS IT COULD AFFORD. HOWEVER, JIMENEZ SAID THAT THIS WOULD UNDOUBTEDLY PUT A LOT OF FURTHER PRESSURE ON THE EXCHANGE RATE. HE DOUBTED THAT THE NIGERIANS REALISED HOW MUCH FURTHER DEVALUATION WOULD BE LIKELY TO RESULT, BUT THAT TOO WOULD GIVE THEM SEVER POLITICAL AND SOCIAL PROBLEMS.

(I) IN RESPONSE TO MY QUESTION, JIMENEZ SAID THAT HE FELT SURE THE NIGERIANS WOULD FIND IT POLITICALLY IMPOSSIBLE TO ACCEPT IMF STANDBY MONEY (A VIEW WHICH I SHARE). HE COMMENTED THAT IN ANY EVENT THAT FACILITY WAS NO LONGER PARTICULARLY RELEVANT, SINCE IT WOULD ENTAIL REPAYMENTS IN THREE OR FOUR YEARS TIME WHICH THE NIGERIANS WOULD NOT BE ABLE TO AFFORD. ASKED ABOUT THE IMF'S ENHANCED STRUCTURAL ADJUSTMENT FACILITY, JIMENEZ SAID THAT ALTHOUGH THE NIGERIANS MIGHT HAVE BEEN PREPARED TO ACCEPT THIS, THEY WERE NOT ELIGIBLE.

(J) ON NON-OIL EXPORTS, JIMENEZ SAID IT WAS HARD TO GET HOLD OF ADEQUATE DATA (A FACTOR OF DEREGULATION), BUT HE DID NOT SEE HOW THESE WOULD GROW SUFFICIENTLY (ONLY 6% IN 1987) TO MAKE A SIGNIFICANT IMPACT ON NIGERIA'S FOREIGN EXCHANGE REVENUES IN THE NEXT FEW YEARS.

(K) JIMENEZ SAID THAT THE NIGERIANS WERE ANXIOUS TO OBTAIN CREDITS FOR THE MAJOR HYDROCARBON PROJECTS WHICH WOULD EARN ADDITIONAL FOREIGN EXCHANGE IE THE OSO CONDENSATES PROJECT, THE LNG PROJECT AND THE PETROCHEMICAL PHASE II.

COMMENT

3. JIMENEZ SEEMED ALMOST OVERWHELMED BY THE NEWLY REVEALED SIZE OF THE PROBLEMS, AND SEEMED TO DOUBT WHETHER THESE COULD BE SOLVED WITHOUT SOME FUNDAMENTAL RETHINKING, MORE ON THE PART OF THE CREDITOR COUNTRIES THAN BY NIGERIA. HE DID NOT RAISE, NOR DID I, THE FORMULATION OF A CONSULTATIVE GROUP. NOR DID HE ASCRIBE ANY SPECIAL ROLE TO BRITAIN (UNLIKE THE US AMBASSADOR, WHO IN A WIDE RANGING DISCUSSION ON THE NIGERIAN ECONOMY A FEW DAYS AGO SAID THAT MORE AND MORE WAS IT THE THINKING IN WASHINGTON THAT BRITAIN SHOULD TAKE THE LEAD IN A FUNDAMENTAL REAPPRAISAL OF NIGERIA'S ECONOMIC NEEDS). JIMENEZ DID NOT DRAW TOO MANY CONCLUSIONS, PERHAPS LARGELY BECAUSE HE DID NOT THEN KNOW THE NATURE OF THE FINAL NIGERIAN PROPOSALS, AND ALSO BECAUSE OF THE IMPOSSIBILITY - PARTICULARLY NOW, OF PREDICTING WHERE THE OIL PRICE IS HEADING. ALSO BECAUSE HE KEPT EMPHASISING THAT THE ANSWERS TO THE PROBLEMS WERE MOVING FROM THE ECONOMIC TO THE POLITICAL SPHERE. HIS MOOD MAY HAVE BEEN SUMMED UP WHEN I ASKED WHAT WOULD HAPPEN NEXT AFTER HE HAD REPORTED BACK TO WASHINGTON, TO WHICH HE SAID, HALF AMUSED, THAT HE WOULD PROBABLY HAVE TO LOOK FOR ANOTHER JOB.

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TO PRIORITY FCO

TELNO 1093

OF 311240Z OCTOBER 1988

AND TO PRIORITY TREASURY, BANK OF ENGLAND, ECGD
INFO PRIORITY DTI, ODA, PARIS (FOR MOUNTFIELD),
INFO PRIORITY UKDEL IMF/IBRD WASHINGTON, ABIDJAN (FOR UK EXECUTIVE
DIRECTOR AFBD).

YOUR TELNO 186: NIGERIAN ECONOMY AND IMF

SUMMARY

1. MINISTER OF STATE FOR BUDGET REACTS TO IMF MISSION AND THE ECONOMIC SITUATION, AND CONFIRMS THE SERIOUSNESS OF THE SITUATION. HE ASKS THAT BRITAIN TAKE THE LEAD IN SECURING PARIS CLUB AGREEMENT AND IN MOBILISING ECONOMIC SUPPORT FOR NIGERIA.

DETAIL

2. I CALLED ON ALHAJI ABUBAKAR ALHAJI (AAA), MINISTER OF STATE FOR BUDGET AND PLANNING, ON 27 OCTOBER PRIMARILY TO GET HIS ASSESSMENT OF THE IMF MISSION, AND TO GET HIS VIEWS ON THE LIKELY NEXT STEP. AAA, WHO SEEMED VERY TIRED AND A LITTLE DEPRESSED, SAID THAT THE NEGOTIATIONS WITH THE IMF HAD BEEN VERY DIFFICULT INDEED, BUT THEY HAD BEEN ABLE TO AGREE A LETTER OF INTENT WHICH HE HOPED WOULD MAKE IT POSSIBLE TO GO TO THE IMF BOARD IN NOVEMBER. HE SAID THAT WORK ON THE US DOLLARS 500 MILLION WORLD BANK FINANCIAL POLICY DEVELOPMENT LOAN HAD ALSO BEEN COMPLETED, AND A SUBMISSION SHOULD BE MADE TO THE WORLD BANK BOARD IN DECEMBER.

3. AAA CONFIRMED THAT THE IMF TEAM HAD BEEN CONCERNED THAT MORATORIUM INTEREST PAYMENTS HAD BEEN MADE TO SOME PARIS CLUB MEMBERS AND NOT TO OTHERS, AND HAD URGED THAT THESE BE EVENED UP. AAA SAID THIS COULD NOT BE DONE: IT WOULD REQUIRE US DOLLARS 450 MILLION WHICH THEY COULD NOT AFFORD TO BRING ALL PAYMENTS UP TO 30 JUNE. HE SAID HE HAD EXPLAINED TO THE IMF THAT THE UK, US AND GERMANY HAD BEEN PAID INTEREST DUE ON 30 JUNE BECAUSE THEY HAD BEEN THE FIRST TO RECONCILE THEIR DEBTS, BUT THEY HAD STILL BEEN TOLD THAT THEY MUST PAY EVERYONE EVENLY, TO GET PARIS CLUB AGREEMENT TO RESCHEDULING. JIMENEZ (IMF) HAD AGREED TO TRY TO PERSUADE THE CREDITORS TO FOREGO THE ARREARS AND ADOPT AN

EARLIER CUT-OFF DATE. FAILING THAT, THE FIRST PRIORITY WOULD HAVE TO BE TO PAY INTEREST TO THOSE WHO SO FAR RECEIVED LITTLE OR NONE.

4. AAA SAID THAT THE QUESTION OF THE FORMATION OF A CONSULTATIVE GROUP HAD BEEN DISCUSSED WITH THE IMF AND THE WORLD BANK, BUT THIS COULD ONLY BE TAKEN FORWARD AFTER A PARIS CLUB AGREEMENT. THE IMF HAD BEEN DIFFICULT OVER THE OPERATION OF THE FOREIGN EXCHANGE AUCTIONS, BUT THE NIGERIAN GOVERNMENT INTENDED TO ADOPT A SINGLE INTERBANK MARKET, AND ABANDON THE FORTNIGHTLY EXCHANGE AUCTIONS: THE DETAILS WERE STILL BEING WORKED OUT. THE 1989 BUDGET USUALLY PRESENTED IN THE LAST WEEK OF DECEMBER) WOULD BE BASED ON AN EXCHANGE RATE OF N5 TO THE DOLLAR (N 4 TO THE DOLLAR IN 1988), BUT HOW FAR THE NAIRA COULD BE DEVALUED BEYOND THIS WOULD DEPEND LARGELY ON ECONOMIC AND POLITICAL FACTORS. DEVALUATION WAS STILL SEEN BY NIGERIANS AS EVIDENCE OF ECONOMIC MISMANAGEMENT AND THE GOVERNMENT HAD ALREADY TAKEN STICK FOR THE LARGE DEVALUATION UP TO NOW. I ASKED WHAT ASSUMPTIONS THE BUDGET WOULD MAKE ABOUT OIL PRICES. HE SAID HE WAS MAKING PLANS ON THE BASIS OF THREE LEVELS, 12 DOLLARS, 14 DOLLARS AND 16 DOLLARS.

5. AAA ENDED WITH A PLEA THAT BRITAIN SHOULD TAKE THE LEAD IN PERSUADING CREDITORS TO ACCPET THE REALITIES OF NIGERIA'S POSITION, PARTICULARLY OVER THE IMPRACTICALITY OF PAYING ALL MORATORIUM INTEREST UP TO 30 JUNE, AND HELP ACHIEVE AGREEMENT TO PARIS CLUB RESCHEDULING. PRESIDENT BABANGIDA WAS VERY MUCH AWARE THAT NIGERIA DEPENDED UPON THE UK FOR THIS. AAA SAID THAT IT WAS NOT JUST NIGERIANS WHO THOUGHT THIS: 'EVERYBODY, INCLUDING THE AMERICANS,' HAD TOLD HIM THAT IT WAS QUITE ESSENTIAL THAT BRITAIN SHOULD TAKE THE LEAD. I SAID THAT WE HAD ALREADY GIVEN A LOT OF SUPPORT, BUT THAT WE, AND ECGD PARTICULARLY, DID HAVE A GENUINE DIFFICULTY WITH THE DELAYS IN REACHING AGREEMENT WITH THE IMF AND THE FAILURE TO MEET THE 30 JUNE PAYMENTS IN FULL. NEVERTHELESS WE WERE OF COURSE CONTINUOUSLY UPDATING OUR APPRAISAL, AND I WOULD REPORT WHAT HE HAD SAID.

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FROM: J M G TAYLOR

DATE: 3 November 1988

JMG

MR MOUNTFIELD

cc Mr Bottrill
Mrs Thompson

NIGERIAN ECONOMY AND IMF

... The Chancellor has seen Lagos Tel no 1100 (attached). He would be grateful for a quick note on the points raised.

JMG

J M G TAYLOR

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TO PRIORITY FCO

TELNO 1100

OF 011530Z NOVEMBER 1988

AND TO ROUTINE TREASURY, BANK OF ENGLAND, ECGD, DTI, ODA

AND TO ROUTINE UKDEL IMF/IBRD WASHINGTON

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A quick note, post.

MIPT AND MY TELNO 1093: NIGERIAN ECONOMY AND IMF

SUMMARY

1. THE NIGERIAN GOVERNMENT, AND IT SEEMS OTHERS, APPEAR TO BE LOOKING FOR A LEAD FROM BRITAIN IN MOBILISING INTERNATIONAL SUPPORT FOR THE NIGERIAN ECONOMY. THERE ARE REASONS FOR GIVING THESE APPEALS SERIOUS CONSIDERATION.

DETAIL

2. I SOUGHT THE VIEWS OF ABUBAKAR ALHAJI (AAA) (MINISTER OF STATE FOR BUDGET), AHMED (GOVERNOR OF CENTRAL BANK) AND HUSAIN (LOCAL WORLD BANK REPRESENTATIVE) ON THE ECONOMIC SITUATION AFTER THE IMF VISIT, SINCE I FELT THESE MIGHT BE USEFUL IN DETERMINING OUR OWN ATTITUDES AS THE ATTEMPTS TO REACH A SETTLEMENT WITH THE IMF COME TO A CRUNCH, AND PRIOR TO THE NEXT PARIS CLUB MEETING. MY TURS PRESENT THEIR VIEWS WITHOUT COMMENT: THE FOLLOWING MIGHT ALSO BE TAKEN INTO ACCOUNT.

3. WE EARNED CONSIDERABLE CREDIT FROM THE NIGERIANS FOR TAKING THE LEAD IN HELPING THEM IN 1986. INDEED I WOULD SUGGEST THAT MOST OF THE IMPROVEMENT IN RELATIONS IN THE PAST TWO YEARS FLOWED FROM HMG'S HELP IN THEN PERSUADING PARIS CLUB MEMBERS AND LEADING BANKS TO RESCHEDULE DEBTS AS A BASIS FOR A STRUCTURAL ADJUSTMENT PROGRAMME, AND FROM THE BANK OF ENGLAND'S #250 MILLION BRIDGING LOAN. THE NIGERIAN PERFORMANCE HAS IMPROVED CONSIDERABLY SINCE THEN, EVEN IF NOT AS QUICKLY AND NOT AS EVENLY AS WE WOULD HAVE WISHED. THE NIGERIANS ARE MAKING SIGNIFICANT CUTS IN EXPENDITURE. THEY ARE PURSUING POLICIES DESIGNED TO INCREASE EXPORT EARNINGS. THEY ARE BITING SOME HARD BULLETS EG PUTTING UP TELEPHONE CHARGES BY SOME 700% AND INTERNATIONAL AIRFARES BY 100%. MAJOR ELECTRICITY PRICE INCREASES AND OTHER SIMILAR MEASURE ARE SAID TO BE IN THE PIPELINE. THE PROGRAMME OF PRIVATISATION IS EVLOVING (ALTHOUGH MOST PARTS OF THE PUBLIC

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SECTOR ARE IN SUCH A MESS THAT THE NIGERIANS SURELY OVER-ESTIMATE THEIR SALEABILITY).

4. YET THE NIGERIANS AGAIN FACE A MAJOR FOREIGN EXCHANGE FINANCING GAP AND ARE AGAIN IN URGENT NEED OF GENEROUS RESCHEDULING, AND THE INJECTION OF NEW EXTERNAL FUNDS.

5. THERE APPEARS TO BE A WIDELY-HELD VIEW, NOT JUST THAT OF THE NIGERIAN GOVERNMENT, THAT BRITAIN'S POSITION IS MORE CRITICAL THAN THAT OF ANY OTHER CREDITOR. AS SEEN FROM HERE, THERE WOULD SEEM GOOD GROUNDS FOR OUR TAKING ON THAT ROLE.

6. IF WE WERE ABLE TO TAKE THE LEAD, OR SIMPLY DEMONSTRATE OUR SUPPORT, THEN THAT WOULD REFLECT OUR LARGER STAKE IN THIS COUNTRY THAN THE OTHER CREDITORS INCLUDING NOT LEAST OUR LARGER EXPORTS. THERE ARE CLEARLY A VARIETY OF WAYS IN WHICH WE COULD DEMONSTRATE THAT SUPPORT: SUPPORT FOR RESCHEDULING AT THE PARIS CLUB, THE RESUMPTION OF SOME ECGD MEDIUM TERM COVER, (ESPECIALLY THE BIWATER PROJECT) PARTICIPATION IN HYDROCARBON PROJECTS SUCH AS OSO AND LNG, OR TO INDICATE OUR WILLINGNESS TO PARTICIPATE IN A CONSULTATIVE GROUP ALBEIT UNDER WORLD BANK LEADERSHIP AND PERHAPS WITH THE SUBJECT MATTER SPREAD TO FOCUS ON DEVELOPMENT AS MUCH AS DEPTS, AND THEREBY REMOVING THE IMPLICATION OF THE PROMISE OF CAPITAL AID.

7. IF WE DID FEEL ABLE TO TAKE ANY SUCH STEPS I SEE NO REASON WHY WE SHOULD NOT LOOK FOR MORE THAN JUST CONTINUING GOODWILL IN RETURN. WE COULD SAY TO THE NIGERIANS AT THE HIGHEST LEVEL THAT WE WOULD EXPECT IN RETURN A MORE POSITIVE ATTITUDE ON THEIR PART TOWARDS OUR INTERESTS WHETHER THAT WERE THE AWARD OF CONTRACTS OR VOTES ON THE FALKLANDS AT THE UN. (AND OF COURSE THAT THEY WOULD CONTINUE TO FOLLOW IMF APPROVED POLICIES). HOW FAR WE COULD PURSUE THAT LINE WOULD DEPEND ON THE LEVEL AND FLEXIBILITY OF THE HELP WE FELT ABLE TO GIVE, BUT THE NIGERIANS UNDERSTAND VERY WELL, AND THEMSELVES LIVE BY, THE PHILOSOPHY THAT FAVOURS COME AT A PRICE. MOREOVER IT IS A PHILOSOPHY THAT THE NIGERIANS SEE THE FRENCH PURSUING WITH NO LITTLE SUCCESS IN ALL THE COUNTRIES AROUND THEM.

8. WE MUST SURELY ALSO TAKE INTO ACCOUNT IS THE STABILITY OF THE BABANGIDA REGIME IF THEY DO NOT GET SOME OUTSIDE HELP. THIS OF COURSE IS DIFFICULT TO ASSESS AND WE HAVE TO BE WARY OF CRYING WOLF TOO SOON. HOWEVER, WAGE LEVELS IN NIGERIA HAVE INCREASED VERY LITTLE IN THE LAST YEAR OR TWO WHILE THE PRICE OF MANY

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BASIC ITEMS, INCLUDING FOODSTUFFS, HAS RISEN ENORMOUSLY. INFLATION, IS NOW IN THE 20 - 30% RANGE AND RISING. THIS GOVERNMENT HAS BEEN ABLE TO PUSH THROUGH UNPOPULAR MEASURES THAT A POPULARLY ELECTED GOVERNMENT WOULD HAVE FOUND MORE DIFFICULT. BUT THERE IS A LIMIT AND CERTAINLY THE GOVERNMENT HERE, NOT ONLY THE MILITARY BUT ALSO THOSE LIKE THE GOVERNOR OF THE CENTRAL BANK, BELIEVE THAT THE LIMIT IS CLOSE. IF THE PRESENT REGIME IS NOT ONLY MORE PRO WEST THAN ANY LIKELY ALTERNATIVE, BUT ALSO MORE LIKELY TO EASE THE COUNTRY OUT OF ITS PRESENT ECONOMIC MORASS THEN WE PERHAPS SHOULD GIVE SERIOUS THOUGHT TO THEIR APPEALS FOR A BRITISH LEAD.

9. FINALLY, WE ARE BEGINNING TO PEER INTO THE DARK TUNNEL OF A POSSIBLE NEED FOR SUBSTANTIAL AID FOR NIGERIA IN THE NOT TOO DISTANT FUTURE. THIS NEED COULD PERHAPS BE HEADED OFF BY LESSER HELP AT THIS STAGE.

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FM UKDEL IMF/IBRD WASHINGTON
TO DESKBY 100800Z FCO
TELNO 237
OF 092300Z NOVEMBER 88

IMF: FINANCING PARALLEL WITH FUND ARRANGEMENTS

SUMMARY

1. FOLLOWING US PRESSURE, FUND BOARD DISCUSSION OF JAPAN'S PARALLEL FINANCING PROPOSALS POSTPONED.

DETAIL

2. OVER THE PAST COUPLE OF DAYS WE, AND OTHER OFFICES HERE, HAVE BEEN SUBJECT TO HEAVY LOBBYING FROM THE STAFF (WHITTOME) AND THE JAPANESE (YAMAZAKI), AS WELL AS ON THE OTHER SIDE THE US (TEMPLEMAN) ABOUT THE LINE WE WOULD TAKE IN THE DISCUSSION SCHEDULED TODAY ON JAPAN'S PROPOSALS FOR PARALLEL FINANCING WITH FUND ARRANGEMENTS. WE RESPONDED CAUTIOUSLY ALONG THE LINES OF YOUR TELNO 192. THIS SEEMED TO BE BROADLY THE POSITION OF MOST OF THE EUROPEANS, WITH WHOM WE CONSULTED, ALTHOUGH THE FRENCH TONE WAS PERHAPS SLIGHTLY MORE POSITIVE TOWARDS THE JAPANESE, AND THE GERMANS MODIFIED THEIR POSITION IN THE DIRECTION OF THE JAPANESE AFTER BEING LOBBIED.

3. WE HEARD THIS MORNING FROM THE US THAT THEY HAD PERSUADED THE JAPANESE TO ASK FOR A POSTPONEMENT OF THE DISCUSSION. ACCORDINGLY, AT THE START OF THE MEETING, CAMDESSUS (MD) ANNOUNCED THAT HE WAS ACCEDING TO A JAPANESE REQUEST FOR A POSTPONEMENT. BEFORE HE COULD MOVE ON TO THE NEXT BUSINESS, HOWEVER, GROSCHE (GERMANY) EXPRESSED DISQUIET, AND ASKED FOR ELABORATION FROM YAMAZAKI. YAMAZAKI, CLEARLY VERY SHAKEN AND UNHAPPY, MADE A SHORT STATEMENT THAT JAPAN HAD TRIED TO COOPERATE FULLY WITH THE INTERNATIONAL COMMUNITY AND WOULD CONTINUE TO DO SO. HOWEVER, FOR 'PRESENTATIONAL REASONS' THEY NOW THOUGHT IT WOULD BE BETTER IF THERE WERE A POSTPONEMENT OF THE DISCUSSION UNTIL SOME OF THE QUESTIONS RAISED HAD BEEN SORTED OUT. FILARDO (VENEZUELA), ENOCH, ZECCHINI (ITALY) AND FOGELHOLM (NORDICS) ALSO EXPRESSED UNEASE AT THE POSTPONEMENT, NOTING THAT, WHILST THEY COULD GO ALONG WITH YAMAZAKI'S REQUEST, THEY HAD PREPARED THEIR RESPONSES TO THE JAPANESE PROPOSALS AND STILL HOPED THEY WOULD BE ABLE TO PRESENT THEM AT AN EARLY DATE. FOGELHOLM ASKED HOW THE DELAY WOULD HELP, GIVEN THAT MOST OF THE CONCERNS HE HAD INTENDED TO RAISE RELATED TO STAFF

INVOLVEMENT IN THE PREPARATION OF THE ARRANGEMENTS, BUT HE RECEIVED NO REPLY. YAMAZAKI INDICATED THAT HE HOPED THE DISCUSSION COULD TAKE PLACE BY THE END OF THE MONTH.

4. KAKFA (BRAZIL), IN HIS ROLE AS DEAN OF THE BOARD, QUESTIONED WHETHER IT WAS APPROPRIATE FOR STAFF TO BE PROVIDING MORE THAN A SECRETARIAL SERVICE TO THE JAPANESE ON THESE PROPOSALS, GIVEN THAT THE SUBJECT HAD NOT BEEN PUT TO DIRECTORS FOR GUIDANCE. HE WAS SHARPLY REBUKED BY CAMDESSUS, WHO SAID THAT THIS WAS A BILATERAL ARRANGEMENT WITH THE JAPANESE, AND THE JAPANESE WERE FULLY INVOLVED. POSTHUMUS (NETHERLANDS) QUESTIONED WHETHER THE RELATIONSHIP THE STAFF HAD WITH THE JAPANESE ON THESE ARRANGEMENTS WAS INDEED CONSISTENT WITH GENERAL FUND PRACTICE. CAMDESSUS TRIED TO ASSURE HIM THAT IT WAS.

COMMENT

5. IT IS DIFFICULT TO KNOW WHAT THE US HOPED TO ACHIEVE BY THIS POSTPONEMENT. MOST DIRECTORS HAD INTENDED TO BE RATHER CRITICAL OF THE JAPANESE PROPOSALS TODAY. WHEN THE DISCUSSION RESUMES, THERE MAY BE SOME SLIGHT SOFTENING OF SOME POSITIONS AS DIRECTORS REACT AGAINST THE US' STRONG-ARM TACTICS.

6. MORE WIDELY, THIS LOOKS LIKE AN UNFORTUNATE RETREAT AWAY FROM MULTILATERALISM, WITH THE US NOT PREPARED TO EXPRESS ITS CONCERNS OVER THIS ISSUE (CONCERNS WHICH WE OURSELVES LARGELY SHARE) IN THE FUND BOARD. THEY MAY OF COURSE INSTEAD SEEK TO RAISE THIS ISSUE IN OTHER FORA, SUCH AS THE G7, OR TO EMBARK ON FURTHER BILATERAL LOBBYING. BUT, ESPECIALLY GIVEN THAT THE DANGER TO MULTILATERALISM IS A CENTRAL OBJECTION TO THE JAPANESE PROPOSAL, THESE TACTICS SEEM ILL-JUDGED.

7. THE IMPACT ON JAPAN'S INTEREST IN PURSUING ITS VARIOUS DEBT INITIATIVES IS AGAIN DIFFICULT TO ASSESS. JAPAN WAS CLEARLY HUMILIATED IN THE FUND BOARD TODAY.

8. FUND MANAGEMENT HAS HANDLED THIS WHOLE ISSUE BADLY THROUGHOUT. THEY HAVE BECOME FAR TOO CLOSELY INVOLVED IN THE JAPANESE INITIATIVE, PRESUMABLY AT LEAST IN PART BECAUSE OF THE CENTRAL ROLE THE INITIATIVE ASCRIBES TO THE FUND. THERE IS WIDESPREAD SUPPORT FOR THE VIEWS EXPRESSED BY KAFKA, AND A FEELING THAT CAMDESSUS' SHARP RESPONSE WAS INAPPROPRIATE. ON THE OTHER HAND, THERE IS ALSO STRONG SYMPATHY WITH MANAGEMENT FOR HAVING (WITH THE JAPANESE) HAD TO FACE US PRESSURE TO POSTPONE THE SCHEDULED BOARD DISCUSSION WITHOUT NOTICE: CAMDESSUS SEEMED GRATIFIED BY THE CONCERNS EXPRESSED ON THIS SCORE BY A NUMBER OF DIRECTORS, INCLUDING OURSELVES.

9. FCO PLEASE ADVANCE TO WARE (BOE), BATT (HMT) AND

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FM UKDEL IMF/IBRD WASHINGTON
TO DESKBY 100800Z FCO
TELNO 236
OF 092300Z NOVEMBER 88
INFO ROUTINE LAGOS, ABIDJAN

ABIDJAN FOR SUTHERLAND AFDB
IMF: NIGERIA

SUMMARY

1. JIMENEZ SEEKING TO CLEAR PROPOSED PROGRAM WITH OTHER FUND DEPARTMENTS AND WITH MANAGEMENT. IF INTERNAL AGREEMENT IS REACHED, BOARD PAPER (TOGETHER WITH AGREED LETTER OF INTENT) WILL ISSUE IN MID TO LATE DECEMBER.

DETAIL

2. WE HAVE SPOKEN TO JIMENEZ ABOUT THE LATEST STATE OF PLAY ON NIGERIA. HE SAID THAT HE WAS AWAITING COMMENTS FROM OTHER FUND DEPARTMENTS (E.G. FISCAL AFFAIRS AND ETR) ON A PROPOSED PROGRAM. THE LATTER WOULD THEN BE PUT TO THE MANAGING DIRECTOR FOR CLEARANCE. IF APPROVAL WAS FORTHCOMING A BOARD PAPER WOULD ISSUE IN MID TO LATE DECEMBER.

3. JIMENEZ WAS NOT CONFIDENT THAT INTERNAL APPROVAL WOULD BE FORTHCOMING. WHILE HE WAS ENCOURAGING FUND COLLEAGUES TO VIEW THE PROGRAM AS A PACKAGE, THE SPECIALIST DEPARTMENTS WILL FOCUS ON PARTICULAR POLICY STRANDS IN ISOLATION (E.G. FISCAL AFFAIRS MAY ARGUE THAT THE FISCAL POSITION, WHILE GREATLY IMPROVED, IS STILL NOT TIGHT ENOUGH SEMICOLON SIMILARLY, DESPITE THE PROPOSED SHARP REDUCTION IN BROAD MONEY GROWTH, SOME MAY ARGUE THAT THE MISSION SHOULD HAVE PRESSED HARDER).

4. JIMENEZ'S OWN VIEW WAS THAT TAKEN AS A PACKAGE THE PROGRAM WAS JUST ABOUT ADEQUATE - PROVIDED EXCEPTIONAL EXTERNAL FINANCING COULD BE SECURED. IN ANY CASE, HE THOUGHT THAT THE NIGERIANS WOULD NOT AGREE TO ANYTHING MORE.

5. JIMENEZ SAID THAT THE PROPOSED PROGRAM BUILT ON THE RECENT TIGHTENING OF FINANCIAL CONDITIONS IN NIGERIA. IT ENVISAGED A REDUCTION IN BROAD MONEY GROWTH IN 1989 TO LESS THAN HALF ITS 1988 RATE AND CREDIT EXPANSION IN 1989 RUNNING AT AROUND 40 PER CENT OF ITS 1988 LEVEL. IN ADDITION STEPS

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WOULD BE TAKEN TO UNIFY THE EXCHANGE SYSTEM AND TO STRENGTHEN THE PUBLIC ENTERPRISE SECTOR.

6. THE FUND NOW ESTIMATED THAT THERE WOULD BE A FINANCING GAP OF DOLLARS 5 BILLION IN 1989. THE NIGERIANS WERE NOT AT PRESENT PREPARED TO DRAW ON FUND MONEY SEMICOLON ALTHOUGH JIMENEZ DID SUGGEST THAT THEY MIGHT RELAX THIS POSITION IN THE EVENT THAT OIL PRICES DETERIORATED FURTHER AFTER A PROGRAM HAD BEEN AGREED.

7. JIMENEZ EMPHASISED AGAIN THAT THE PARIS CLUB WOULD NEED TO MAKE AN EXCEPTIONAL EFFORT TO HELP NIGERIA. THE WORLD BANK WAS ALREADY DISBURSING LARGE SUMS, AND DESPITE HIS 'BADGERING' THERE WAS NO PROSPECT OF NEW MONEY FROM THE LONDON CLUB EVEN IN 1989. JIMENEZ SAID HE WAS HOPING FOR MORE FROM THE JAPANESE. WE ASKED WHETHER NIGERIA WOULD BENEFIT FROM THE NEW PARALLEL FINANCING ARRANGEMENTS. HE SAID THAT NIGERIA WAS NOT 'ON TOP OF THE JAPANESE LIST'.

COMMENT

tel. on these attached.
8. THE INDICATIONS ARE THAT IF A PROGRAM EMERGES IN THE NEAR FUTURE IT WILL BE A 'WEAK' ONE. FROM UKDEL'S POINT OF VIEW, GIVEN THE LEADING ROLE WE WILL BE EXPECTED TO PLAY IN THE BOARD, IT WILL BE IMPORTANT FOR US TO BE SEEN TO BE TREATING NIGERIA NO DIFFERENTLY FROM OTHER COUNTRIES. TO TREAT NIGERIA LENIENTLY BY NODDING THROUGH A MANIFESTLY WEAK PROGRAM WOULD SEVERELY DAMAGE OUR CREDIBILITY AND LEVERAGE ON OTHER ISSUES. IF THEREFORE A WEAK PROGRAMME WERE TO COME TO THE BOARD WE WOULD CERTAINLY HAVE TO BE HIGHLY CRITICAL, BUT WE WOULD EXPECT TO BE ABLE TO SAFEGUARD OUR CREDIBILITY WITHOUT HAVING TO GO SO FAR AS TO ABSTAIN SEMICOLON IN THIS REGARD INADEQUATE FINANCING ASSURANCES MIGHT GIVE US THE MOST DIFFICULTY, IF THE FUND WERE TO WISH TO DISPERSE ITS RESOURCES. THE FIRST STEP HOWEVER IS TO SEE WHETHER JIMENEZ'S PROGRAM GETS MANAGEMENT APPROVAL.

9. FCO PLEASE ADVANCE TO LANKESTER, MOUNTFIELD AND EVANS (HMT), T RICHARDSON (ERD) AND LOEHNIS (BANK OF ENGLAND).

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FM UKDEL IMF/IBRD WASHINGTON
TO IMMEDIATE FCO
TELNO 247
OF 142000Z NOVEMBER 88
INFO ROUTINE LAGOS, ABIDJAN

Ch. NB 'X' AMH
WPAJ
15/11

ABIDJAN FOR SUTHERLAND, AFDB.

NIGERIA: IBRD VIEWS

1. WE DEBRIEFED CAIO KOCH-WESER (DIRECTOR) AND JOANNE SALOP (PRINCIPAL ECONOMIST) OF THE WORLD BANK'S WESTERN AFRICA DEPT. AFTER THEIR RECENT MISSION TO NIGERIA.

IMF PROGRAMME/BANK'S TRADE AND INVESTMENT POLICY LOAN (TIPL)

2. THE FALL IN THE OIL PRICE HAD MADE NIGERIA'S CASH FLOW POSITION MUCH WORSE AND ARREARS WERE NOW MOUNTING. CLEARLY, HOWEVER, DESPITE ACTIONS TAKEN BY NIGERIA IN RECENT MONTHS, MUCH MORE NEEDED TO BE DONE, PARTICULARLY ON THE FISCAL SIDE (E.G. A FURTHER CUT IN PETROLEUM SUBSIDY). HOWEVER, KOCH-WESER AGREED WITH JIMENEZ (OUR TELNO 236) THAT THE NIGERIANS WOULD NOT AGREE TO ANYTHING MORE (BECAUSE OF FEAR OF POLITICAL FALL-OUT) UNTIL AFTER IMF PROGRAMME AND BANK'S TIPL APPROVED AND PARIS CLUB RESCHEDULING AGREEMENT SIGNED. HE HOPED THAT THE NIGERIANS COULD BE PERSUADED TO AGREE TO TAKE MORE FAR-REACHING ADJUSTMENT MEASURES IN THE NEXT 6-9 MONTHS, E.G., THE BANK'S TIPL WOULD HAVE SUBSTANTIAL CONDITIONS FOR SECOND TRANCHE RELEASE. (ITS CONDITIONS OF EFFECTIVENESS HAD ALREADY BEEN MET BY THE NIGERIANS).

3. IF EVERYTHING GOES TO PLAN, KOCH-WESER EXPECTS:

(I) NIGERIANS TO ENSURE (BY CUTTING THE SUPPLY OF FOREIGN EXCHANGE) THAT AUCTION EXCHANGE RATE MOVES ABOVE RATE OF FIVE NAIRA/ONE DOLLAR IN NEXT FEW WEEKS,

(II) TIPL TO GO TO BANK BOARD ON DECEMBER 15 FOR APPROVAL SUBJECT TO FUND BOARD APPROVAL OF IMF PROGRAMME IN MID-JANUARY.

JAPANESE HAVE INDICATED A WILLINGNESS IN PRINCIPLE TO PUT FORWARD DOLLARS 250-300 MILLION OF COFINANCING FOR TIPL,

(III) PRE-PARIS CLUB TALKS IN NOVEMBER/DECEMBER, AND FORMAL PARIS CLUB RESCHEDULING MEETING IN JANUARY AFTER IMF BOARD APPROVAL.

4. TIMETABLE CLEARLY DEPENDENT ON ACCEPTABLE IMF PROGRAMME BEING PUT TOGETHER. WE MADE IT CLEAR TO KOCH-WESER AND SALOP THAT UK ACCEPTANCE OF A WEAK FUND PROGRAMME FOR NIGERIA SHOULD NOT BE TAKEN FOR GRANTED.

PARIS CLUB

5. NIGERIA WOULD PROBABLY MAKE A PITCH FOR TORONTO TERMS BUT NOT EXPECT TO GET THEM IN JANUARY. THEY WOULD HOWEVER HOPE THAT FUTURE PC MEETINGS COULD AGREE IMPROVED TERMS. KOCH-WESER HOPES THAT, WITH UK PROMPTING, PARIS CLUB MEETING WILL RESCHEDULE ALL MORATORIUM INTEREST ON NIGERIAN DEBT RESCHEDULED IN 1986. PROBLEM WAS THAT NIGERIA HAD MADE A NUMBER OF SELECTIVE REPAYMENTS (INCLUDING TO UK) WHICH MADE IT DIFFICULT TO ACHIEVE EQUAL TREATMENT FOR ALL CREDITORS. WE AGREED THAT KOCH-WESER SHOULD CONTACT MOUNTFIELD (HMT) TO DISCUSS THIS ISSUE. HE WILL TELEPHONE MOUNTFIELD IN NEXT FEW DAYS AND/OR ARRANGE TO SEE HIM IN LONDON EN ROUTE TO OR FROM GUINEA-BISSAU AT END-NOVEMBER/EARLY DECEMBER.

CONCESSIONAL AID/PRE-CG MEETING

6. TURNING TO THE CONCESSIONALITY OF RESOURCES NIGERIA WOULD NEED IN THE FUTURE, KOCH-WESER MENTIONED THAT THE PROMISED PAPER ON NIGERIA'S IDA ELIGIBILITY WAS ABOUT TO BE CIRCULATED AND THAT AN AGRICULTURAL SECTOR OPERATION WOULD PROBABLY BE THE FIRST MADE ON IDA TERMS. THE STAFF HAS RESPONDED CAUTIOUSLY TO NIGERIAN ENQUIRIES ABOUT FUTURE IDA FLOWS - IT WAS TOO EARLY TO GUESS WHAT MIGHT BE FORTHCOMING. AS FOR THE POSSIBILITY OF A CONSULTATIVE GROUP (CG) FOR NIGERIA, KOCH-WESER HAD SOUNDED OUT THE JAPANESE WHO WERE KEEN TO TAKE PART BUT NOT TO LEAD. HE UNDERSTOOD THAT HMG WOULD NOT WANT TO TAKE UP-FRONT ROLE GIVEN AMOUNTS OF UK FUNDS LIKELY TO BE AVAILABLE FOR NIGERIA. HOWEVER, KOCH-WESER HOPED THAT HMG WOULD AGREE TO ARRANGE/ CHAIR AN INFORMAL PRE-CG MEETING ON NIGERIA OF G7, EEC AND AFDB. THIS COULD BE HELD IN LONDON TOWARDS THE END OF JANUARY AND WOULD, HE THOUGHT, GAIN POLITICAL KUDOS FOR UK IN NIGERIAN EYES. IF AGREEMENT WAS REACHED TO PROCEED WITH A FULL CG, THEN WORLD BANK WOULD ORGANISE AND CHAIR MEETINGS IN THE NORMAL WAY.

FURTHER MEETINGS

7. APART FROM POSSIBLE MEETING WITH MOUNTFIELD, KOCH-WESER WOULD LIKE TO SEE LANKESTER WHEN LATTER IS IN WASHINGTON AT END OF THIS WEEK (WE ARE ARRANGING AN APPOINTMENT). KOCH-WESER ALSO SUGGESTED THAT A MEETING BETWEEN AAA AND CHANCELLOR AT SOME STAGE WOULD PROVE FRUITFUL.

8. FCO PLEASE ADVANCE TO LANKESTER, MOUNTFIELD AND EVANS (HMT), AINSCOW (ODA), T. RICHARDSON (ERD) AND LOEHNIS (BOFE).

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From: T P Lankester
Date: 14 November 1988

- Note above /
1. MR ANSON ✓
2. CHANCELLOR 14/11

cc

Chief Secretary
Economic Secretary
Sir Peter Middleton
Sir Geoffrey Littler
Mr Scholar
Mr Turnbull
Mrs Lomax
Mr Mountfield
Mr Evans
Mr P Davis
Mr Bottrill
Mr Walsh
Mrs Thomson
Mr Tyrie

NIGERIA

I attach our latest assessment of Nigeria's current situation and prospects, and of the options available. This follows meetings I have had with the head of a recently returned IMF Mission and with the Bank of England and other departments. The assessment has been agreed with the Bank and departments.

2. We have concluded that a credible IMF programme and recovery over the medium-term are not feasible without a substantial injection of external support over and above what is likely to be in the pipeline. The Nigerians have begun to check the rise in public spending; but the IMF Staff judge (and we would support them) that not enough has been done to bring the domestic economy into better balance; and without a further compression of domestic demand, there is likely to be an ex ante financing gap on the external side of \$1-1½ billion between now and the end of 1989. This could be reduced by \$600 million if the Nigerians could be persuaded to take a Fund drawing. We believe the Nigerians have reached the end of the road in terms of their ability and willingness to take further policy measures. However, they might be persuaded to take further measures which in turn would reduce imports, given the carrot of some exceptional donor assistance; and the latter could possibly close the remaining external financing gap.

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3. We are thus left with two alternatives, both pretty unpalatable. Firstly, either no new IMF programme or a weak, under-financed programme that breaks down rapidly. At this stage, we are not clear whether the IMF Managing Director will decide to proceed with a programme. The IMF team have taken back to Washington with them a draft Letter of Intent, albeit far from satisfactory. It may be that Camdessus will decide to proceed on this basis. That would leave us in an intensely difficult position because we would be bound to abstain or oppose it in the Board. We ought to tell Camdessus now that we would prefer no programme to a weak, under-financed programme.

4. The consequences of no IMF programme are analysed in our paper. For the export credit agencies, including ECGD, it will make little difference over the next year or two because, in any case, all principal and practically all interest due will have to be rescheduled. For the banks, however, it would make a significant difference. They could expect to get little in the way of further interest payments. We doubt whether the present regime would actually repudiate, but in due course the banks would have to write their loans down by the full 100 per cent. This would be unwelcome though bearable for our big 4 banks; it could cause serious difficulties, though probably would not be fatal, for Standard Chartered. Promissory notes amounting to several hundred million pounds held by UK firms would also be at risk.

5. For the medium-term, the prospects for recovery of the Nigerian economy (barring a big increase in the oil price) would be low indeed and likewise for imports from the UK and other countries. The FCO believe that a breakdown with the IMF will put their policies into reverse and could well within a year or two - because of the continued economic stagnation - bring down the Babangida regime. This seems to me a fair assessment. Continuing stagnation into the 1990s would seriously reduce the chances of getting anything back on ECGD's £2½ billion Nigerian exposure - though I must emphasise that, even with an IMF programme and sustained recovery thereafter, there will have to be reschedulings certainly of principal well into the 1990s.

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6. The alternative of an IMF programme, buttressed by additional external support, will be expensive and certainly cannot be guaranteed to succeed. ODA judge that it might be possible to raise additional aid from bilateral donors of about \$250 million, but to make this a runner the UK would have to contribute \$100 million at least. (We cannot expect anything towards the package from Japan since they are already expected to put in \$200 million.) With this support, we would insist on the Nigerians drawing on the Fund and on some further policy tightening. Further bilateral contributions at around this level would be needed for several years, unless the banks can persuade themselves to put in some new money again or embark on some debt reduction. We do not think there is any chance of this in 1989: the banks have already agreed a rescheduling deal for 1989 without any new money. For later years, new money from the banks might be possible depending on how much arm twisting the IMF and other authorities are prepared to do. (If the banks do not put in any new money, they would stand to do rather well out of this scenario: they would essentially be receiving their interest payments and some principal thanks to the generosity of the public sector.)

7. There is nothing in ODA's aid framework for Nigeria and ODA claim that there is no way they can find any money for this purpose. For 1989 they are heavily committed, but if we were to embark on a Nigerian rescue, we could not accept that they make no contribution from the existing aid provision. By our reckoning, they should have between £15 million and £20 million still unallocated for 1989-90, and if necessary they could make the figure up to £30 million by a combination of reordering some priorities and possibly use of an expected underspend in EC aid. This would leave a balance of around £30 million to come from the Reserve. If it would be helpful to the Reserve position, this £30 million could be the first to be disbursed, ie before 31 March 1989. Contributions for 1990-91 and subsequent years would be decided in the PES negotiations. But realistically we have to

face the fact that the Foreign Secretary would undoubtedly argue strongly that he could not find the full amount from his existing provision, and it is probable that the Chief Secretary would have to offer at least half (ie around £30 million in each year) in new money in order to get agreement.

Assessment

8. I do not think this issue can be fudged. We either have to accept a standoff between Nigeria and the creditors and take the political and financial consequences; or alternatively, we have to be prepared to come to Nigeria's assistance, work hard to persuade others to do the same and persuade the Nigerians to take further policy measures.

9. Needless to say, the FCO favour the rescue option.

10. From the point of view of our narrowly identifiable financial and economic interests, it would be hard to justify any rescue. First of all, it is by no means a foregone conclusion that we and the IMF will succeed in pressuring the Nigerians into further measures, even with an aid package which itself will be hard to assemble. Furthermore, on past form, there is a clear risk that the Nigerians will blow it; and the net benefits to us over the next two or three years are not likely to be all that great against the likelihood of the need for continuing financial assistance from us and others if Nigeria is to pull through.

11. The political argument in favour of helping Nigeria is of course clear. Nigeria is the most important country in black Africa by a long way and Babangida and his people are friends of ours and able to help on such issues as South Africa and Namibia. From a broader and longer term economic perspective, there is also a case for the rescue option. Against the possibility of recovery, increased UK exports, renewed creditworthiness and ECGD getting repaid in the 1990s, the public expenditure cost may not

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be too great. It would also give a bad signal to other countries in Africa if Nigeria goes its own way. Also, the UK would be criticised for ducking its responsibilities under the debt strategy; other creditor governments, particularly the Americans, are certainly expecting the UK to take the lead on Nigeria.

11. Views in the Treasury are divided. Some in OF think the medium term prospects for Nigeria are so poor that it is not worth spending additional money in order to put in place an IMF programme which could easily breakdown again. I myself take the view that we should come to Nigeria's assistance on the basis outlined above and in the paper, notwithstanding the cost and the risks involved.

12. Camdessus is likely to decide in the next week or so whether to proceed with a programme. I shall be in Washington later this week. If we are not prepared to attempt a rescue package, I should if possible tell Camdessus; and also that we do not wish him to come forward with the weak, under-financed programme that is currently on offer. If we are willing to mount a rescue, I could explore with him on a non-committal basis whether it would "buy" a viable programme.

13. Whichever of the two options you decide to go for, you will need to send an early minute to the Foreign Secretary. I attach alternative drafts.

14. Depending on your decision, we will be putting advice to the Chief Secretary on the outstanding Biwater export credit case.

15. I would of course be happy to discuss all this with you first.

12.
T P LANKESTER

DRAFT A

DRAFT LETTER TO SIR GEOFFREY HOWE

Copies to:

Prime Minister
Lord Young

NIGERIA

Your officials will be showing you the note, prepared in the Treasury after discussion with officials from other departments, about the options we face in financial relations with Nigeria.

We now have to decide, quite quickly, the main lines of the policy which we should follow in the next few months. Although the paper describes a number of options, I think the basic choice comes down to this. Should we make a further major effort to persuade the Nigerians to adopt adequate economic policies, although this will involve considerable public expenditure by the UK and others to provide the incentive to Lagos? Or should we recognise that Nigeria is unlikely to pursue the right policies, let events take their course, and be prepared to accept the risk of default?

I find the arguments very finely balanced. British economic interests in Nigeria, while considerable, do not seem to me to be enough to justify a major rescue operation. The political arguments are primarily a matter for you to consider.

However, if you were to conclude that they were enough to tip the balance, I would not dissent. The paper makes clear that a rescue operation would be an expensive business. Clearly, the UK would need to take a prominent part in organising it, and we would be

DRAFT A
(PROGRAMME +
EXECUTIVE SUMMARY)

(eg if there were a donor package of, say, \$250 million, we might be expected to put up perhaps \$100 million).
expected to foot ^{a major} part of the bill. This was, of course, recognised in your bilateral discussions with John Major earlier this autumn. Both sides then reserved their position. But if you felt that assistance was justified, and were prepared to make a significant contribution from within the existing aid programme, John Major and I would be prepared to match this from the Reserve. ~~If the amount turned out to be as indicated above, this would imply~~ ~~It is too early to talk precise figures, but I am thinking in terms of~~ a contribution from the Aid Budget of perhaps £30 million ~~in 1989/90, with a further~~ ^{matched by} £30 million from the Reserve. It would be helpful if ^{as much as possible of the Reserve contribution} ~~some payments~~ could fall in 1988/89, but ~~it may not be possible to agree on quick-disbursing aid in time for this. I would expect that similar amounts would be needed in 1990/1991 and 1991/92.~~

If you ^{favor} ~~agree~~ in principle ^{on this basis,} to a rescue operation ~~of this kind,~~ we shall need to consider how best to organise international support for it. I am quite clear, from earlier discussions, that both the IMF and the United States authorities look to the UK to handle the Nigerian problem, just as the US looks after Mexico and Argentina.

But we ^{would} need also to sound out the IMF. ^{As it happens,} ~~By good chance,~~ Tim Lankester is going to Washington later this week, and has arranged a meeting with Camdessus. ^{This would provide an opportunity} ~~I would like to authorise him~~ to discuss ^{the matter,} ~~this possibility,~~ on a purely exploratory basis, with Camdessus. He would make it clear that we have taken no ministerial decisions yet. This will depend upon the design and content of the IMF programme, and upon the availability of adequate finance. He would certainly need to make it clear to Camdessus that the UK could not support a "weak" IMF programme,

nor one which was inadequately financed. But he could ask Camdessus whether he thought that an international financing package of some \$250 million, put together by a World Bank consultative group, with a UK contribution of say \$100 million, would both close the financing gap and be sufficiently attractive to persuade the Nigerians to adopt a "strong" programme. The precise differences between "weak" and "strong" cannot be set down too clearly at this stage, but we have a rough idea of what would be involved. On the domestic side, it would require action to cut the budgetary deficit, to slow drastically the rate of growth of money supply, to introduce strongly-positive real interest rates, and a substantial devaluation of the naira. In view of Nigeria's past record, we should expect there to be significant upfront prior actions before the programme was put to the IMF Executive Board. Camdessus will have some idea, from contacts with other governments, whether the Americans, Germans and others would be prepared to join. He is already calculating on a substantial contribution from the Japanese. If you agree, I would ask Tim^{Lankster} to explore these options in more detail with Camdessus, and probably with the World Bank, and to report back to us on his return.

I am sending a copy of this letter to David Young, because of the ECGD involvement.

DRAFT B
(DUGGING
IT OUT)

DRAFT B

DRAFT LETTER TO SIR GEOFFREY HOWE

Copies to:

Prime Minister
Lord Young

NIGERIA

Your officials will be showing you the note, prepared in the Treasury after discussion with officials from other departments, about the options we face in our financial relations with Nigeria.

We now have to decide, quite quickly, the main lines of the policy which we should follow in the next few months. Although the paper describes a number of options, I think the basic choice comes down to this. Should we make a further major effort to persuade the Nigerians to adopt adequate economic policies, although this will involve considerable public expenditure by the UK and others to provide the incentive to Lagos? Or should we recognise that Nigeria is unlikely to pursue the right policies, let events take their course, and be prepared to accept the risk of default?

Very reluctantly, I conclude that it is simply impracticable to put together an IMF programme which is both acceptable to the Nigerian Government and has any chance of success. The only way of persuading the Nigerians to accept the degree of austerity required would be to offer an assistance package which is beyond our means to do in isolation, and which has no chance of support from other donors or creditors. Realistically, I fear that there is no alternative but to accept the high probability of Nigerian default. I conclude that we should abandon our attempts to seek a

compromise, and make it clear to the IMF that we do not wish them to put forward a weak programme, containing a large unbridged financing gap, which has no chance of success.

The politics of this (which I know will greatly concern you) are very difficult. Obviously the UK does not wish to be seen to take the responsibility for precipitating the breakdown. But the IMF, and to some extent the other governments concerned, are looking to us to take a lead.

It so happens that Tim Lankester is going to Washington later this week, and has an appointment with Camdessus. I propose to instruct him to raise these issues with Camdessus, and to make it clear to him that the UK is not prepared to support a weak programme. He should ask Camdessus' advice about the chances of persuading the Nigerians to take the necessary stronger measures. If Camdessus concludes, as I think he will, that these are out of reach, Tim should say that he believes British ministers who would not be prepared to support a weak programme. He should go on, entirely without commitment, to speculate about the risk that the UK would be forced to abstain, or even to vote against, such a programme. He would suggest to Camdessus that since the credibility of the Fund is at stake, it would be wrong for management to put forward to the Board a proposal which risked this reaction. He could point out that, if the UK were not prepared to support Nigeria, it is unlikely that any other of the G5 would do so. In this situation, Camdessus would probably conclude that he should not proceed. He would then need to send a mission back to Lagos, to explain the situation to the Nigerians,

and give them the choice between a stronger programme, whatever the domestic political price, or no programme at all. The decision would then be for the Nigerians to take, in full knowledge of the consequence.

I recognise that this is an unpalatable choice. But I see no real alternative. In view of the consequences for ECGD (who would be faced with the probability of a moratorium, rather than a series of long-term rescheduling agreements) I am sending a copy of this letter to David Young.

X α PM

NIGERIA : ECONOMIC POLICIES AND PROSPECTS AND THE OPTIONS FOR THE UK**Introduction**

The developing situation in Nigeria together with the return from Lagos of the latest IMF mission, make it necessary to review the options open to the UK as Nigeria's single largest bilateral creditor. This note which has been prepared by the Treasury - after consultation with Departments, assesses Nigeria's policies and prospects as well as the pros and cons of the various courses of action open to the UK. The analysis in this note is based on only very provisional figures: but if we waited for final IMF documents to be available it would be effectively too late to influence the decision. An annex sets out the key assumptions.

Domestic developments in Nigeria

2. The authorities in Lagos have been grappling since the summer with the consequences of the relaxation of economic policies during 1987 and the first part of 1988 which derailed Nigeria's standby arrangement with the IMF and threatens to undermine the country's structural adjustment programme. Last year's budgetary over-runs were followed by a further expansionary budget for 1988 and the outturn for the first half of the year led to estimates that the Federal deficit might be as high as 15 per cent of GNP for the year as a whole.

3. The swollen budget deficit has contributed to rapid credit growth to the public sector. An ill-judged reduction in interest

rates around the turn of the year also encouraged the growth of private demand for credit. The result has been an overall growth of credit at around 30 per cent. These expansionary policies have led to some recovery in domestic activity but at a cost of rising inflation which is currently also about 30 per cent, an alarming rise from 5 per cent in 1986 and 12 per cent in 1987.

4. The problems caused by the imbalances in the domestic economy have been compounded by the fall in world oil prices which have led to a sharp deterioration in Nigeria's external payments. The average price for Nigerian oil this year is likely to be about \$15 a barrel compared to almost \$18 last year. The Nigerians have tried to offset this by breaching their 1.3mbd OPEC quota and pumping as much as 1.5mbd in recent months. The volume of imports has also had to be reduced. Nevertheless, the IMF estimates that Nigeria's current account deficit will rise to \$1.8 billion in 1988 compared to \$1.1 billion last year.

5. In spite of the deteriorating external position, the Nigerian authorities - in a reversal of the policy measures taken in the first two years of the structural adjustment programme - have been reluctant to allow the naira exchange rate to depreciate adequately. They have underpinned the official rate by allocating excessive foreign exchange to the Central Bank's fortnightly auction. Reserves are running out. The combination of this with rapid domestic inflation has been an estimated loss of almost 20 per cent in competitiveness since the end of 1987. This threatens to undermine the growth of non-oil exports and the production of

domestic substitutes for imports upon which Nigeria's long-term recovery depends.

6. The lack of satisfactory domestic policies has delayed agreement on a new IMF programme and Paris Club rescheduling - although a commercial bank rescheduling agreement is expected to be signed shortly. Meanwhile, arrears have mounted especially to Paris Club creditors.

7. The Nigerian authorities' first attempt to rectify the mistakes of this year's budget was to reduce at least partly the large subsidy on fuel prices. This, however, together with other price increases sparked a rash of strikes and rioting in early May to which the Government responded by importing extra key commodities and urging employers to complete new wage settlements quickly. Some of these were as high as 50 per cent.

8. Growing realisation of the seriousness of the situation, however, opened the way for re-arrangement of the economic team in July with Alhaji Abubakar Alhaji (AAA) becoming Minister of State (Budget and National Planning) with new responsibilities and direct access to President Babangida. He is supported by the Central Bank Governor Ahmed and less certainly by Chief Falae. He has taken over the key functions of the Finance Minister Okongwu and gained influence at the expense of the President's other economic advisers.

9. Progress with economic reform, however, has been patchy, and negotiations with the latest IMF mission were difficult according

to both sides. The three areas of dispute are budgetary policies, credit and interest rates and the exchange rate system.

- **Budgetary policy:** AAA with Babangida's support, at least for the present, has begun to rein back over-spending. Negotiations with other Ministers, however, on next year's budget are not complete. AAA is seeking to limit spending to the same level as in 1988 but this may be unrealistic in light of the existing inflation rate. No measures have yet been identified to increase revenues.

- **Credit and interest rates:** New reserve ratios for banks were introduced in August but it is too early to judge their effect. Interest rates remain heavily negative in real terms and AAA himself is apparently arguing against an increase.

- **Exchange rate:** The Nigerians have indicated a willingness to abandon the foreign exchange auction and allow the naira to be determined freely on the interbank market. They appear to be ready, however, only to see the rate decline modestly by 4-5 per cent to Naira 5 to the dollar next year instead of the 20-30 per cent fall needed to bring it in line with the current free rate.

The Fund Staff have advised us in confidence that the Nigerians' measures do not measure up to the brief from IMF Management with which they were sent to Lagos. Nevertheless, the mission has taken back to Washington a draft Letter of Intent for a new Standby Arrangement.

10. The difficulties in agreeing an IMF programme with the Nigerians are accompanied by problems in identifying how the resulting external payments deficit might be financed. Even on relatively optimistic assumptions about oil revenues and allowing for a small rise in imports, the IMF estimates that Nigeria's current deficit will widen to some \$2½ billion in 1989 with little prospect of any substantial reduction in 1990 or 1991. The deficit may be greater if oil prices do not recover from their present levels.

11. It is impossible at this stage to see how deficits of this magnitude, together with the clearing of 1988's arrears, can be financed even if creditors can be persuaded to accept the programme.

- **IMF** : Both the Fund and the Nigerians are ambivalent about whether IMF resources should be used. The IMF correctly in our view, sees Nigeria's problems as long-term and structural. It is therefore hesitating to involve its own money - although under a one-year Standby Arrangement (SBA) Nigeria might draw about \$600 million, equivalent to half its quota. The Nigerians themselves, however, are reluctant to draw on the Fund following a hostile public debate in Lagos two years ago - though they have hinted recently that a drawing might be acceptable if put into a special BIS account. Nigeria is not at present on the list of countries eligible for the IMF Enhanced Structural Adjustment Facility (ESAF) and in any case could not be allowed more than a

small drawing on the facility if it were not to crowd out others. Such a drawing could only take place after a successful SBA had been in place for a year.

- **World Bank:** The IBRD is keen to help. It is financing on-going projects worth about \$200 million a year and has signed recently a \$270 million loan to help small and medium size businesses. It is also prepared to make a fast-disbursing \$500 million trade and investment policy loan available - although we should not want this to go ahead without an agreed IMF programme. A \$500 million Financial Policy Development loan is also planned to go to the Board in December - but this likewise should depend on an IMF programme being agreed. Nigeria was declared eligible for funds from IDA on 15 September and has been allocated about \$100 million of IDA's money for the period 1 July 1988 - 30 June 1989. The Japanese have indicated they are ready to provide \$200 million in co-financing alongside the IBRD. The African Development Bank also expects to disburse about \$150 million next year.

- **Paris Club:** Nigeria has not yet signed all its bilateral agreements with creditor governments following last year's rescheduling. These will need to be completed before any new Paris Club deal - even if an IMF programme can be agreed. ECGD which has \$3.8 billion (£2.2 billion) of principal and future interest payments at risk in Nigeria compared to \$3.1 billion for France the second largest creditor, has received £110.9 million out of £144.8 million

in respect of reconciled debt due up to 30 June. There is still a considerable volume of debt yet to be reconciled as well. The IMF has suggested that Paris Club creditors will need to reschedule 100 per cent of all remaining principal and interest due to the end of 1989, including new maturities and arrears. A new problem, however, has arisen because Nigeria has made unequal payments to those creditors who have signed agreements. The Paris Club - if it stuck to normal practice - would probably insist that all creditors were paid up to a common date eg 30 June 1988. This would involve a costly settling of arrears estimated at \$300 - 450 million, though it might be possible to compromise on an earlier date at a smaller cost. We and other creditors have resisted any move to extend Toronto terms to Nigeria. It would provide no short-term cash flow benefits as long as all interest is being rescheduled any way. Even a 'normal' rescheduling would involve a very heavy contribution from governments to Nigeria's financing needs. ECGD, for example, would have to capitalise up to £284 million of interest due under earlier agreements (assuming all debt was reconciled) and reschedule a further £480 million, mainly of new maturities due by end-1989. A deal on this scale would be likely to make export credit agencies reluctant to provide much if any new medium-term cover. In this context, 'capitalisation of interest' has the same effect as 'new money' from the banks. It adds to ECGD's exposure, and to its borrowing from the Exchequer, while giving equivalent benefit to the Nigerian balance of payments. All export credit agencies, including ECGD, are

taking a cautious approach to new cover. Any such cover depends on progress of payments under rescheduling agreements and since no further moratorium interest payments are likely, cover is effectively suspended.

- **Commercial banks:** The Nigerians have so far treated bank creditors considerably better than governments and have continued to pay interest to the banks. The latter regard Nigeria despondently as a 'work out' situation and are reconciled to rescheduling medium-term debt over 20 years and short-term claims over 16 years with four year's grace even without an IMF programme. The banks, however, are insisting that pre-1988 interest arrears, commissions and fees should be repaid over the next three years. The banks argue that the rescheduling terms represent a significant easing of Nigeria's cashflow, which compensates for the lack of new money. In fact, there would be a net capital outflow to banks of \$120 million a year in contrast to the large net inflows sought from official creditors. The banks, however, are adamant that they will provide no new money without an IMF programme and are most unlikely to do so even with one. Banks incorporated in the UK have net claims of £870 million on Nigeria. Major banks account for £709 million of this against which they have provisions of £305 million equivalent to 43 per cent. Their exposure averages about 3 per cent of their capital base. In the case of the most exposed bank it is now 17 per cent of its capital. The commercial bank's claims stand at a discount of 76 per cent on the secondary market.

- **Aid:** Nigeria receives negligible amounts of aid from donor governments at present but both the World Bank and the Nigerians themselves have floated the idea that a donor group should be formed as, for example, in Indonesia. In the UK's case, apart from a small allocation for technical cooperation there is no specific provision in the current Aid Framework (July 1988) for Nigeria. This is because Nigeria was previously considered ineligible for capital aid due to its income per head and oil revenues. In the course of this year's PES discussions, the Minister for Overseas Development said that he did not think it could be afforded within the somewhat increased Aid Budget. The Chief Secretary, while noting this view, entered into no commitment about the funding of such a programme. There is however an unallocated margin of £80 million. Leaving room for contingencies, and taking account of the additions agreed in the Survey, and of other changes since the Aid Framework was drawn up, there is about £20 million left available for allocation to country programmes in 1989-90. There is very little left in 1988-89.

The IMF projections for substantial current balance of payments deficits on existing policies, when combined with our assessment of what external finance might realistically be available, reveal a gap of approximately \$1-1½ billion for 1988 and 1989 taken together.

The IMF assumes no drawing on the Fund's resources but even with a Fund drawing, we do not believe Nigeria could finance such large deficits while rebuilding its reserves and repaying essential cash arrears. Nor does it allow for a worse outcome on oil exports than their present assumptions. Even if current deficits of \$2-2½ billion at least to 1991 as projected by the IMF could be financed by additional borrowing, they would raise Nigeria's interest payments from 29 per cent of exports last year to 37 per cent by 1991 and increase the ratio of debt to exports from 360 per cent to almost 450 per cent. (See Annex).

Policy Options

12. The policy options available to the UK need to take account of the Nigerian authorities' ability to implement adequate policies as well as our own political and economic interests.

13. There are real political limits on the Nigerian Government's freedom of action deriving from the need to retain a measure of public consent, to contain unrest, and to balance Federal and sectoral interests. As a military government it will be institutionally freer to direct the economy than a civilian government, but politically just as circumscribed. Any new programme cannot be imposed; it will have to be sold to the military and the urban middle-class and present a prospect of tangible improvement before 1992, when power is to be transferred to a civilian government. Measures such as drawing on the Fund and devaluation will have to be presented very carefully or they will court wide-spread rejection. Babangida will have to shield

his military constituency and may have to pre-empt urban dwellers' unrest by conceding on some unpopular measures eg domestic fuel prices.

14. Nigeria is by any standards a major power in Africa (one in four black Africans is Nigerian). Its size and resources give it a significant role in black Africa and elsewhere in the developing world. Nigeria traditionally aspires to the leadership of black Africa. It is likely to continue to try to assert this role in the OAU, the non-aligned movement, the UN and the Commonwealth. Nigerian foreign policy is important to the UK. In the East/West context, we have a strong interest in Nigeria maintaining its basic pro-Western orientation, thereby limiting the scope for Soviet regional influence. In the North/South context, we have an interest in Nigeria playing a responsible role on Third World issues eg trade, finance, investment and (given its OPEC membership) oil affairs. We have a strong interest in pre-empting Nigerian spoiling tactics over Southern Africa, the major African problem looming over the next decade.

15. The UK also has major economic interests in Nigeria in addition to ECGD's exposure. More than 300 UK firms or their offshoots have investment in Nigeria worth more than £2 billion at current book prices. UK exports to Nigeria were £480 million last year - equal to 22 per cent of Nigeria's imports but less than ½ per cent of total UK exports. Despite the short and medium term difficulties, our main competitors (notably FRG, France, Japan, US and Italy) continue to devote attention to the Nigerian market, with an eye to the opportunities so large a market offers in the

long run, (particularly when and if it succeeds in mobilising its enormous natural resources which give it the capacity for a large and diversified agricultural sector). Since the 1970s the French have established themselves in key sectors, while Japan in 1987 nearly doubled its market share. Nigeria also has promissory notes outstanding of almost \$5 billion, a major proportion of which is for debt to UK companies.

16. But the position of the UK in the international financial institutions also has to be taken into account. Nigeria will be regarded as our client, just as Argentina is regarded as an American client. If we agree, or even worse promote, a weak programme for Nigeria our leverage on other issues will be seriously undermined. We have developed a consistent voting record of not supporting weak programmes over the last couple of years consistent with the Chancellor's line at IMF/IBRD meetings. Support for a weak Nigerian programme would vitiate our efforts.

17. The key to the policy options available to the UK and Nigeria is the nature of any agreement with the IMF. The description of Nigeria's domestic and external economic difficulties above illustrates that the present attitudes of the Nigerians do not provide a viable solution. Unless there is more adjustment, Nigeria will not be able to service its debts fully. The IMF and other creditors look to the UK to give a lead. The main decision for the UK is the guidance that we, together with others, are prepared to give to the IMF Managing Director on the amount of adjustment that creditors should seek in Nigeria and the extent to which we are prepared to finance it.

18. These choices can perhaps be illustrated best by comparing a normal (firm) IMF programme accompanied by conventional financing arrangements with, first, a firm programme accompanied by some exceptional finance, and then the currently envisaged less demanding programme for which finance from creditors has so far not been identified. We also look at the consequences of a Nigerian default.

- a. Firm IMF programme/conventional finance: This would involve Nigeria reducing its current deficit substantially over, say, the next two years so that from 1990 it was able at least to make interest payments not only to banks but also to Paris Club creditors. It would require prior actions by the Nigerians on the budget, interest rates and the exchange rate together with mechanisms to maximise the chances of the programme being implemented fully.. It would involve a further squeeze on domestic demand and a reduction in import volumes of 10 per cent or more although the effects on activity should be offset by higher output of both non-oil exports and of import substitutes. It would still, however, involve a large contribution from official creditors in the form of IBRD loans and generous Paris Club rescheduling for 1988 and 1989. It would require a drawing on the Fund itself to help reconstitute Nigeria's reserves.
- Advantages: It offers a chance of promoting long-term economic recovery in Nigeria and avoids an

unsustainable build up of debt. It is consistent with the UK's approach to the debt strategy and in particular the Prime Minister's comment to Camdessus when he asked her about Nigeria in May that sometimes shock therapy was the only possible course. It minimises the cost to HMG in that it does not require any new cover from ECGD beyond rescheduling and improves the chances of ultimate repayment. It avoids calls on the aid budget. **Disadvantages:** It involves short-term costs for the Nigerians particularly probably the urban middle classes. It implies an outward resource transfer at least temporarily. It still imposes heavy costs on ECGD and other Paris Club creditors in the form of claims paid and moratorium interest capitalised. **Risks:** It increases political strains on the Babangida regime and risks a rupture in UK-Nigerian relations if the UK is seen leading pressure for a programme which the Nigerians regard as severe, particularly if other countries do not support or keep a low profile. It could jeopardise the West's geopolitical interests in Nigeria as a stable force in Africa and the world. It also raises the possibility that the Nigerians will not agree an IMF programme and decide instead to default on payments to both Paris Club creditors and commercial banks. ECGD would then need to add to the £740 million provisions it has

already made against the possibility of ultimate loss on its Nigerian exposure with a further very serious impact on ECGD's financial position. Banks would need to do likewise although we do not believe that Nigeria's bank debts are sufficiently large in themselves to pose a systemic risk. (There could, however, be danger of contagion). UK banks would need to raise their provisions to at least 60 per cent of exposure. This would have a material effect on the profits of one bank, more acutely so in the event of outright repudiation.

- b. Firm IMF programme/concessional finance: This would again involve a strong Fund programme with similar prior conditions to above but it would be accompanied by more generous financing arrangements. It would still involve a fall of 5 per cent or more in Nigerian imports. We should insist that Nigeria draws on the Fund. The need to reduce Nigeria's debt service burden suggests that additional finance might be in concessional form or grant aid rather than additional funds at market rates. Possible candidates for concessional finance include a small contribution from the Fund's ESAF facility from the second year of a programme to the fourth year, or Toronto terms on Paris Club rescheduling which would have some medium-term cash flow benefits. Grant aid might include up to \$100 million a year from IDA, or up to perhaps \$250 million a year from a donors' group in which the

UK would need to play a leading part. **Advantages:** Offers best long-term recovery prospects for Nigeria etc while reducing debt service burden. Improves chance of Nigeria's accepting firm IMF programme. **Disadvantages:** Precedent for other large countries (eg India) relying on both concessional and market funds that may seek both ESAF and Toronto terms. Increased public expenditure costs for the UK and other creditors both directly through national aid contributions and indirectly through their support for ESAF and IDA. For the UK the direct costs could be £60 million a year in aid and up to £60 million a year for Toronto rescheduling. **Risks:** Other countries may not be ready to support such concessions for Nigeria - ie it may not get off the ground. If it does get off the ground, the Nigerians may still not be prepared to take the necessary measures with consequences for banks and ECGD as in (i)

- c. **Weak IMF programme/unidentified finance:** This assumes that the Nigerians are not prepared to take any further measures beyond those already envisaged but that nevertheless creditors including the UK are asked to support an IMF programme on that basis. The Fund's figures show that this would involve continued substantial current deficits into the medium-term financed not only by contributions from the World

Bank and Paris Club but also in the absence of IMF drawings by additional flows from bilateral creditors.

These might be a mixture of Toronto rescheduling, aid and possibly new export credits despite the risks and the undesirable increase in ECGD's exposure. The scale of additional credits might need to be as much as \$1 billion in 1989 to fill the gap. The IMF, however, is still assuming that Nigeria makes at best modest progress in reconstituting its reserves. **Advantages:**

Avoids abrupt short-term adjustment in Nigeria and risk of disruption to UK-Nigerian relations.

Disadvantages: Provides no long-term solution. Postpones economic recovery and prospects for sustainable economic recovery. Adds to Nigeria's debt burden. Undermines general debt strategy and is inconsistent with UK's previous approach. Implies not only heavy public expenditure costs for creditors governments but possibly also increased exposure for their export credit agencies. **Risks:** IMF management and other creditors may be reluctant to support such a programme with either Fund money or their own. The Nigerians may again lose control of economic policy and the programme fail.

- d. **No programme/Nigeria default:** This would involve contacting Camdessus as soon as possible to advise him not to recommend the draft Letter of Intent to the IMF Board as the basis for a programme, because the UK and other creditors would find it impossible to accept such a programme. Negotiations on strengthening the

programme would be difficult. The Nigerians feel that they have already made substantial policy adjustments, and they are likely to be reluctant to tighten policy further. An IMF programme would eventually fail to be agreed. **Advantages:** Refusing to accept a weak IMF programme is consistent with the UK's traditionally tough stance on Fund conditionality. A slow deterioration in the position is less of a threat to the Babangida regime which could benefit (in the short-term) from refusing to be dictated to by the IMF. **Risks and disadvantages:** If the draft Letter of Intent is not accepted as a basis for a programme, it is probable that Nigeria will default on payments to both Paris Club creditors and commercial banks. ECGD would need to make additional provisions against the possibility of ultimate loss on its Nigerian exposure. Banks would need to do likewise although we do not believe that Nigeria's bank debts are sufficiently large, in themselves, to pose a systemic risk. Eventual economic stagnation will place increased political strains on the Babangida regime. Possibility of a rupture in UK-Nigerian relations. While this is probably sustainable from a commercial viewpoint, it could jeopardise the West's geopolitical interests in Nigeria as a stable force in Africa and the World.

19. In terms of timing, any approach by the UK to the IMF Managing Director should probably be done quickly. He will have

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received the report of his mission leader and after other IMF Departments have commented, Camdessus will need to decide whether to recommend the draft Letter of Intent to the IMF Board as the basis for a programme or whether to send the team back to Lagos to seek firmer terms as the Nigerian government finalises the 1989 budget in the next few weeks.

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ANNEX

ECONOMIC ADJUSTMENT AND EXTERNAL FINANCE : ALTERNATIVE ASSUMPTIONS

The attached tables provide illustrative figures for the four scenarios described in the text. They draw on the IMF estimates, the Economic Update provided by the banks' Advisory Committee and our own assumptions.

Oil revenues

2. We have taken the IMF's estimates of oil exports. These could be achieved with various assumptions for production and prices. For illustrative purposes we have shown what would happen if Nigeria produced at its OPEC quota of 1.3 mbd with a further 50,000 barrels a day of condensates. In these circumstances, the IMF's projections could only be achieved with a fairly strong recovery in prices in 1990 and 1991. It is possible, of course, that output will be higher and prices lower .

Scenario A : Firm IMF programme/conventional financing

3. This assumes that Nigeria takes firm measures under an IMF programme to reduce the current deficit. This would imply both higher non-oil exports and lower imports to cut the deficit to a level that can be financed conventionally.

4. We assume the IMF disburses \$600 million a year under a series of SBAs. Approximately \$1 billion a year might be received from the multilateral agencies. In the case of the World Bank, this would include IDA, project loans, the small enterprises loan, the trade policy loan and the financial sector loan. We have assumed that the Japanese will provide \$200 million a year in co-financing although this might be optimistic for later years.

5. The Paris Club is likely to be owed some \$0.9 billion in interest arrears by the end of 1988. We assume that about \$0.4 million of these are repaid next year to bring all creditors level to 30 June 1988. Other interest payments due this year and next

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are rescheduled together with all principal repayments. A modest level of new credits is assumed increasing as the results of the programme come through.

6. If Nigeria's financial situation is as tight as appears, then it is possible that banks will not receive their final \$100-200 million interest payments this year, but we assume that under a Fund programme any arrears would be cleared next year. The banks' rescheduling proposals assume that all principal repayments are postponed to 1992 but arrears from 1987 are repaid at the rate of \$100 million a year.

7. Nigeria also has some cash arrears to repay. These are put tentatively at \$0.6 billion and are assumed to be settled in 1989.

8. We assume that drawings on the Fund will be reflected in an equivalent rebuilding of reserves. A firm IMF programme would also start to reduce the share of Nigeria's exports needed to meet interest payments and would reduce the debt to exports ratio.

Scenario B : Firm IMF programme : Concessional financing

9. This assumes that provision of concessional finance makes possible a slightly less sharp domestic adjustment. The concessional finance includes \$250 million a year in aid, together with ESAF money from the IMF in 1990 and 1991. Assumptions for other sources of finance are unaltered. The extra finance mitigates the import compression needed in 1989, but imports would still need to be cut by 7 per cent.

Scenario C : Weak IMF programme/Unidentified financing

10. This assumes no further change in Nigerian policies. In these circumstances, non-oil exports might not grow so strongly and imports would not be reduced. This would leave current deficits of \$2-2½ billion a year to be financed between 1989 and 1991.

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11. Even if donors were still prepared to make aid available - which seems unlikely - the call of borrowed resources would be particularly large, especially if we follow the IMF's assumption that the Nigerians will not draw IMF money. The World Bank, other multilaterals and commercial banks would be unlikely to provide additional finance. The brunt, therefore, would fall to be provided by governments. This could be as much as \$2 billion in 1989 followed by almost \$1 billion a year in 1990 and 1991. This could take the form of either rescheduled interest or new credits - although ECAs cover policies would be likely to be very circumspect in these circumstances.

12. Such a scenario would allow only a very modest rise in reserves but rising interest payments/exports and debt/exports.

Scenario D : No IMF programme : Nigerian default

13. In the case of no agreement between the Nigerians and the IMF, we might expect some deterioration in Nigerian policies. Non-oil exports might well stagnate. Nigeria might continue to service the World Bank in return for project loans but would receive no new funds from other creditors. Interest arrears to both the Paris Club and banks would mount.

14. The Nigerians would avoid the need for a cut in imports in 1989, but thereafter import growth would be very slow, being dictated by the need to pay cash out of current export earnings.

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CASE A - FIRM IMF PROGRAMME/CONVENTIONAL FINANCING

\$ billion	1987	1988	1989	1990	1991
<u>Current balance</u>					
Exports	7.7	7.1	7.1	7.8	8.4
Oil	(7.0)	(6.2)	(6.0)	(6.5)	(6.9)
Non-oil	(0.7)	(0.9)	(1.1)	(1.3)	(1.5)
Imports	-5.8	-5.6	-5.0	-5.6	-6.2
Trade balance	2.0	1.5	2.1	2.2	2.2
Interest payments	-2.2	-2.4	-2.5	-2.6	-2.7
Other invisibles	-0.9	-0.9	-0.9	-1.1	-1.1
Current balance (excl.official transfers)	-1.1	-1.8	-1.3	-1.5	-1.6
<u>Capital account</u>					
Official transfers	0	0	0.1	0.1	0.1
Direct investment	0.4	0.4	0.3	0.3	0.3
IMF (net)	0	0	0.6	0.6	0.6
Multilaterals (net)	0	0	1.0	1.0	1.0
<u>In</u> IBRD	0.2	0.2	1.0	1.0	1.0
AFDB	0	0	0.1	0.1	0.1
Japan	0	0	0.2	0.2	0.2
<u>Out</u> Repayments	-0.2	-0.2	-0.2	-0.3	-0.3
Paris Club (net)	0.6	1.0	1.0	0.3	0.4
<u>In</u> Credits	0.4	0.1	0.2	0.3	0.4
Rescheduled interest	0.5	0	1.2	0	0
Rescheduled principal	1.5	1.2	1.0	1.2	1.0
<u>Out</u> Repayments due	-1.5	-1.2	-1.0	-1.2	-1.0
Interest arrears	-0.2	0.9	-0.4	0	0
London Club (net)	-0.2	0.1	-0.4	-0.1	-0.1
<u>In</u> New money	0	0	0	0	0
Rescheduled principal	1.1	1.8	1.3	1.1	0.2
<u>Out</u> 1987 arrears	0	-0.1	-0.1	-0.1	-0.1
short-term capital	-0.2	-0.1	0	0	0
Repayments due	-1.1	-1.8	-1.3	-1.1	-0.2
Interest arrears	0	0.2	-0.2	0	0
Other private (net)	-0.1	-0.1	-0.1	-0.1	-0.1
Cash arrears incl E&O	0.3	0	-0.6	0	0
Change in reserves (- = gain)	0.1	0.4	-0.6	-0.6	-0.6
<u>Memorandum items</u>					
Oil production (mbd)	1.3	1.35	1.35	1.35	1.35
Oil price (\$/barrel)	17.3	15.0	14.5	15.9	16.75
Import volume (% change)	-24	-8	12	7	5
Interest payments/exports	28	32	34	32	31
Debt/exports	362	405	434	417	409

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CASE B - FIRM IMF PROGRAMME/CONCESSIONAL FINANCE

\$ billion	1987	1988	1989	1990	1991
<u>Current balance</u>					
Exports	7.7	7.1	7.1	7.8	8.4
Oil	(7.0)	(6.2)	(6.0)	(6.5)	(6.9)
Non-oil	(0.7)	(0.9)	(1.1)	(1.3)	(1.5)
Imports	-5.8	-5.6	-5.3	-5.9	-6.5
Trade balance	2.0	1.5	1.9	2.0	1.9
Interest payments	-2.2	-2.4	-2.5	-2.6	-2.7
Other invisibles	-0.9	-0.9	-0.9	-1.1	-1.1
Current balance (excl.official transfers)	<u>-1.1</u>	<u>-1.8</u>	<u>-1.6</u>	<u>-1.8</u>	<u>-1.9</u>
<u>Capital account</u>					
Official transfers	0	0	0.35	0.35	0.35
Direct investment	0.4	0.4	0.3	0.3	0.3
IMF (net)	0	0	0.6	0.6	0.6
Multilaterals (net)	0	0	1.0	1.0	1.0
<u>In</u> IBRD	0.2	0.2	1.0	1.0	1.0
AFDB	0	0	0.1	0.1	0.1
Japan	0	0	0.2	0.2	0.2
<u>Out</u> Repayments	-0.2	-0.2	-0.2	-0.3	-0.3
Paris Club (net)	0.6	1.0	1.0	0.3	0.4
<u>In</u> Credits	0.4	0.1	0.2	0.3	0.4
Rescheduled interest	0.5	0.0	1.2	0	0
Rescheduled principal	1.5	1.2	1.0	1.2	1.0
<u>Out</u> Repayments due	-1.5	-1.2	-1.0	-1.2	-1.0
Interest arrears	-0.2	0.9	-0.4	0	0
London Club (net)	-0.2	0.1	-0.4	-0.1	-0.1
<u>In</u> New money	0	0	0	0	0
Rescheduled principal	1.1	1.8	1.3	1.1	0.2
<u>Out</u> 1987 arrears	0	-0.1	-0.1	-0.1	-0.1
short-term capital	-0.2	-0.1	0	0	0
Repayments due	-1.1	-1.8	-1.3	-1.1	-0.2
Interest arrears	0	0.2	-0.2	0	0
Other private (net)	-0.1	-0.1	-0.1	-0.1	-0.1
Cash arrears incl E&O	0.3	0	-0.6	0	0
Change in reserves (- = gain)	0.1	0.4	-0.6	-0.6	-0.6
<u>Memorandum items</u>					
Oil production (mbd)	1.3	1.35	1.35	1.35	1.35
Oil price (\$/barrel)	17.3	15.0	14.5	15.9	16.75
Import volume (% change)	-24	-8	-7	6	5
Interest payments/exports	28	32	34	32	31
Debt/exports	362	405	434	417	409

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CASE C - WEAK IMF PROGRAMME/UNIDENTIFIED FINANCING

\$ billion	1987	1988	1989	1990	1991
Current balance					
Exports	7.7	7.1	6.9	7.6	8.0
Oil	(7.0)	(6.2)	(6.0)	(6.5)	(6.9)
Non-oil	(0.7)	(0.9)	(0.9)	(1.0)	(1.1)
Imports	-5.8	-5.6	-5.8	-6.0	-6.3
Trade balance	2.0	1.5	1.1	1.6	1.7
Interest payments	-2.2	-2.4	-2.5	-2.7	-2.9
Other invisibles	-0.9	-0.9	-0.9	-1.1	-1.1
Current balance (excl.official transfers)	-1.1	-1.8	-2.4	-2.2	-2.3
Capital account					
Official transfers	0	0	0.35	0.35	0.35
Direct investment	0.4	0.4	0.3	0.3	0.3
IMF (net)	0	0	0	0	0
Multilaterals (net)	0	0	1.0	1.0	1.0
In IBRD	0.2	0.2	1.0	1.0	1.0
AFDB	0	0	0.1	0.1	0.1
Japan	0	0	0.2	0.2	0.2
Out Repayments	-0.2	-0.2	-0.2	-0.3	-0.3
Paris Club (net)	0.6	1.0	2.1	0.9	1.0
In Credits	0.4	0.1	1.1	0.9	1.0
Rescheduled interest	0.5	0	1.4	0	0
Rescheduled principal	1.5	1.2	1.0	1.2	1.0
Out Repayments due	-1.5	-1.2	-1.0	-1.2	-1.0
Interest arrears	-0.2	0.9	-0.4	0	0
London Club (net)	-0.2	0.1	-0.4	-0.1	-0.1
In New money	0	0	0	0	0
Rescheduled principal	1.1	1.8	1.3	1.1	0.2
Out 1987 arrears	0	-0.1	-0.1	-0.1	-0.1
short-term capital	-0.2	-0.1	0	0	0
Repayments due	-1.1	-1.8	-1.3	-1.1	-0.2
Interest arrears	0	0.2	-0.2	0	0
Other private (net)	-0.1	-0.1	-0.1	-0.1	-0.1
Cash arrears incl E&O	0.3	0	-0.6	0	0
Change in reserves (- = gain)	0.1	0.4	-0.2	-0.1	-0.1
Memorandum items					
Oil production (mbd)	1.3	1.35	1.35	1.35	1.35
Oil price (\$/barrel)	17.3	15.0	14.5	15.7	16.7
Import volume (% change)	-24	-8	2	-1	0
Interest payments/exports	28	32	35	34	35
Debt/exports	362	405	446	438	447

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CASE D - NO IMF PROGRAMME/NIGERIAN DEFAULT

\$ billion	1987	1988	1989	1990	1991
Current balance					
Exports	7.7	7.1	6.9	7.4	7.8
Oil	7.0	6.2	(6.0)	(6.5)	(6.9)
Non-oil	0.7	0.9	(0.9)	(0.9)	(0.9)
Imports	-5.8	-5.6	-5.9	-6.1	-6.5
Trade balance	2.0	1.5	1.1	1.3	1.3
Interest payments	-2.2	-2.4	-2.5	-2.6	-3.0
Other invisibles	-0.9	-0.9	-0.9	-1.1	-1.1
Current balance (excl.official transfers)	-1.1	-1.8	-2.4	-2.5	-2.8
Capital account					
Official transfers	0	0	0	0	0
Direct investment	0.4	0.4	0.3	0.3	0.3
IMF (net)	0	0	0	0	0
Multilaterals (net)	0	0	0	0	0
In IBRD	0.2	0.2	0.2	0.2	0.2
AFDB	0	0	0	0.1	0.1
Japan	0	0	0	0	0
Out Repayments	-0.2	-0.2	-0.2	-0.3	-0.3
Paris Club (net)	0.6	1.0	1.4	1.5	1.6
In Credits	0.4	0.1	0	0	0
Rescheduled interest	0.5	0	0	0	0
Rescheduled principal	1.5	1.2	1.0	1.2	1.0
Out Repayments due	-1.5	-1.2	-1.0	-1.2	-1.0
Interest arrears	-0.2	0.9	1.4	1.5	1.6
London Club (net)	-0.2	0.1	0.6	0.6	0.7
In New money	0	0	0	0	0
Rescheduled principal	1.1	1.8	1.3	1.1	0.2
Out 1987 arrears	0	-0.1	0	0	0
short-term capital	-0.2	-0.1	0	0	0
Repayments due	-1.1	-1.8	-1.3	-1.1	-0.2
Interest arrears	0	0.2	0.5	0.6	0.7
Other private (net)	-0.1	-0.1	0.3	0.3	0.4
Cash arrears incl E&O	0.3	0	0	0	0
Change in reserves (- = gain)	0.1	0.4	-0.2	-0.2	-0.2
Memorandum items					
Oil production (mbd)	1.3	1.35	1.35	1.35	1.35
Oil price (\$/barrel)	17.3	15.0	14.5	15.7	16.7
Import volume (% change)	-24	-8	4	-4	1
Interest payments/exports	28	32	35	35	37
Debt/exports	362	405	449	451	462

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FROM: J. ANSON
14th November, 1988.

CHANCELLOR

- c.c. Chief Secretary
- Economic Secretary
- Sir Peter Middleton
- Sir Geoffrey Littler
- Mr. Scholar
- Mr. Lankester
- Mr. Turnbull
- Mrs. Lomax
- Mr. Mountfield
- Mr. Evans
- Mr. P. Davis
- Mr. Bottrill
- Mr. Walsh
- Mrs. Thomson
- Mr. Tyrie

*Post do a version
with the 12th between
(a) & (b), opinion that
Mr. Evans has to
draw to the
the existing aid
programme, this
is not possible,
can't have 1/2
of the work
done in
14/11/88*

*Ch. Do you want to write along
the lines of draft A (with Mr Anson's
amendments) or draft B?*

NIGERIA: MR. LANKESTER'S SUBMISSION OF 14th NOVEMBER

This is a very awkward case. There are two very big question-marks over the proposed UK contribution to a donor country rescue package: (i) whether the package would actually secure a "strong" IMF programme; and (ii) whether the Foreign Secretary would be willing to meet half the cost from the aid programme if we offer matching funds from the Reserve.

2. The first of these points is for the overseas finance side, and as you will see opinions are divided but Mr. Lankester thinks that on balance it is worth trying. Given the size of our interest in Nigeria, I would not dissent from that.

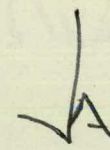
3. On the second point, at the Chief Secretary's Survey bilateral, Mr. Patten warned that if it became necessary to contemplate a substantial bilateral aid programme for Nigeria, he did not think it could be afforded within the Survey settlement. The Chief Secretary noted that view, but gave no commitment about the funding of such a programme at that stage. In practice, it is unlikely that they

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would provide £60 million. AEF think it would be practicable for them to provide £30 million if the Reserve found the other half, but FCO Ministers might of course still resist this. It would also be important that the Reserve contribution should be disbursed in this financial year rather than next, but this would depend on how quickly the package was put in place, and could not therefore be guaranteed. Even on the 50:50 basis, there is a risk therefore of some claim on the Reserve next year; and if the Foreign Secretary pressed for the whole amount to be met from the Reserve, the potential liability would be that much greater.

4. You will want also to have the Chief Secretary's views on the Reserve aspect. But if you feel that the economic arguments for helping Nigeria are powerful enough to justify a UK contribution of the order of \$100 million, I should at least like to see the letter at Draft A amended as indicated in manuscript so as to put the Foreign Secretary, rather than yourself, in the position of demandeur. I have discussed these amendments with Mr. Davis, but have not been able to discuss them with Mr. Lankester, who is out of the office this evening.



J. ANSON

CONFIDENTIAL
COMMERCIAL IN CONFIDENCE



FROM: J M G TAYLOR
DATE: 15 November 1988

MR ANSON

cc PS/Chief Secretary
PS/Economic Secretary
Sir P Middleton
Sir G Littler
Mr Scholar
Mr Lankester
Mr Turnbull
Mrs Lomax
Mr Mountfield
Mr H P Evans
Mr P Davis
Mr Bottrill
Mr Walsh
Mrs Thomson
Mr Tyrie

NIGERIA

The Chancellor was grateful for your minute of 14 November, and Mr Lankester's submission of the same date.

2. He would like to write to the Foreign Secretary in terms intermediate between the two draft letters. He wishes to say that, in his opinion, a rescue package for Nigeria would be money down the drain. If, however, the Foreign Secretary wishes to find the money out of the existing aid programme, and if he feels that this could be justified, then the Chancellor would not wish to stand in his way.

3. I should be grateful for a revised draft along these lines.

A handwritten signature in dark ink, appearing to be 'JMG' or similar initials.

J M G TAYLOR

*Seen in draft*FROM: A R H BOTTRILL
DATE: 15 November 1988

1. MR LANKESTER
2. CHANCELLOR

cc Mr Scholar
Mr Turnbull
Mrs Lomax
Mr Mountfield
Mr Evans
Mr P Davis
Mr Walsh
Mrs Thomson
Mr Tyrie

Copies for
Chief Secretary, Economic Secretary
Sir Peter Middleton, Sir G Littler,
Mr Anson

NIGERIA

I attach a revised draft for you to send to the Foreign Secretary. This illustrates slightly more fully than the previous drafts the financing problems raised by the Nigerians' present proposals and hence the potential burden on the UK and other creditors. The IMF briefed other countries yesterday on the dimension of the problem at this week's Paris Club meeting.

2. I have separated the question of an aid package from the IMF programme. If we do not believe that enough aid is likely to be forthcoming to buy adequate Nigerian adjustment measures, we should regard the aid as purely a political gesture and maintain a firm position on the IMF programme.

ARH

A R H BOTTRILL

MINUTE
DRAFT LETTER TO SIR GEOFFREY HOWE

Copies to
Prime Minister
Lord Young

FOREIGN AND COMMONWEALTH SECRETARY

NIGERIA

Your officials will be showing you the note, prepared in the Treasury after discussion with officials from other departments, about the options we face in our financial relations with Nigeria.

2. We now have to decide, quite quickly, the mainlines of the policy which we should follow in the next few months. The paper describes a number of options, but I think the basic choice comes down to two. Should we make a further major effort to persuade the Nigerians to adopt adequate economic policies, although this will involve considerable public expenditure by the UK and others to provide the incentive to Lagos? Or, should we recognise that Nigeria is unlikely to pursue the right policies, warn the IMF that we are not prepared to support a weak, under-financed programme and be ready to accept the risk of default?

3. I conclude very reluctantly that it is simply impracticable to put together an IMF programme which is both acceptable to the Nigerians and has any chance of success.

4. The IMF estimates that on existing policies Nigeria is likely to run current account deficits of \$2-2½ billion a year at least into the early 1990s. The Fund advises that the Nigerians are not prepared to take further measures which would narrow these deficits. Nor are they ready to draw on IMF resources, and indeed

the Fund has told this week's Paris Club meeting that it would not be prepared to support a programme unless this financing gap can be filled.

5. Banks have already taken a commercial judgement not to provide support. This leaves an unacceptably large burden which would have to be borne by the multilateral agencies and in particular by export credit agencies which already have substantial arrears due from Nigeria and in ECGD's case an uncomfortably large existing exposure.

6. I conclude that the only chance of persuading the Nigerians to accept the degree of austerity required would be to offer an assistance package which is beyond our means to do in isolation, and which has no chance of support from other donors or creditors. Realistically, I fear that there is no alternative but to accept the high probability of at least a temporary Nigerian default. I conclude that we should make it clear to the IMF that we do not wish them to put forward a weak programme, containing a large unbridged financing gap, which has no chance of success.

7. ^{intensely} The politics of this (which I know ~~will greatly~~ concern you) are ~~very~~ difficult. ^{Should you} ~~You may wish to~~ consider ^{that} ~~whether~~ these political factors are so great that you wish to take advantage of what margin you have available within the existing aid budget and what re-ordering of priorities you can achieve to offer at least a modest amount of help to Nigeria, I would not dissent from this; and it would at least show our good intentions. You might also wish to approach other donors.

My own view is that he should

8. In terms of the IMF programme, however, I propose to take advantage of a visit by Tim Lankester to Washington this week to instruct him to make clear to Camdessus that the UK is not prepared to support a weak programme. He should ask Camdessus' advice about the chances of persuading the Nigerians to take the necessary stronger measures. If Camdessus concludes, as I think he will, that these are out of reach, Tim should say that he believes UK Ministers would not be prepared to support a weak programme.

He will try to get Camdessus to postpone a decision until we have an agreed line.

9. He should go on, entirely without commitment, to speculate about the risk that the UK would be forced to abstain, or even to vote against, such a programme. He would suggest to Camdessus that since the credibility of the Fund is at stake, it would be wrong for management to put forward to the Board a proposal which risked this reaction. He could point out that, if the UK were not prepared to support Nigeria, it is unlikely that any other of the G5 would do so. In this situation, Camdessus would probably conclude that he should not proceed. He would then need to send a mission back to Lagos, to explain the situation to the Nigerians, and give them the choice between a stronger programme, whatever the domestic political price, or no programme at all. The decision would then be for the Nigerians to take, in full knowledge of the consequence.

10. I recognise that this is an unpalatable choice. But I see no real alternative. In view of the consequences for ECGD (who would be faced with the probability of a moratorium, rather than a

Tim is in Washington until the middle of next week and will be able to get Camdessus to postpone a decision until we have an agreed line. But we really need to reach a decision by the end of next week.

series of long-term rescheduling agreements) ⁴ ~~I am sending a copy~~
of ~~this letter~~ to David Young.

[NL]

py

FROM: A R H BOTTRILL

DATE: 18 NOVEMBER

MR J M G TAYLOR

cc: Chief Secretary
Economic Secretary
Sir P Middleton
Sir G Littler
Mr Anson
Mr Lankester
Mr Scholar
Mr Turnbull
Mrs Lomax
Mr Mountfield
Mr Evans
Mr P Davis
Mr Walsh
Mrs Thomson
Mr Tyrie

Alex
We have of course now sent
a personal copy of the note to
the Governor.

NIGERIA: BANK OF ENGLAND INTEREST

The Bank of England asked me today if the Governor's office could be kept in touch with the conclusions that ministers reach on policy towards Nigeria. The Bank has of course not seen the Chancellor's letter to the Foreign Secretary and the Governor is apparently not minded to intervene. The Bank has very fairly made its views known about the effects on banks and they are reflected in the paper that we circulated.

2. The Governor, however, would like to be kept informed so that the supervisors are aware of likely developments. He also wishes to be in a position to brief his central bank colleagues where necessary eg at the monthly Basle meeting.

3. May I leave it to you to inform the Governor's private office as appropriate?

ARH

A R H BOTTRILL

CH/EXCHEQUER	
DATE	21 NOV 1988
TO	



10 DOWNING STREET

LONDON SW1A 2AA

From the Private Secretary

20 November, 1988.

Dear Alex,

NIGERIA

The Prime Minister has seen the minutes by the Chancellor of the Exchequer, the Trade and Industry Secretary and the Foreign Secretary about the problems facing the Nigerian economy, and what if anything we can do to help them overcome them. Given the political background and the forthcoming State Visit, she feels that we cannot just give up. She would prefer us, therefore, to follow the course proposed in paragraph 12 of the Foreign Secretary's minute, that is we should make clear to the IMF that we are not prepared to support a weak programme but should explore with them the minimum requirements for a programme we could support and the scope for an international assistance package in which we could participate. The chances of success may not be very high: but a great deal is at stake, and it is worth trying.

I am copying this letter to Lyn Parker (Foreign and Commonwealth Office) and Neil Thornton (Department of Trade and Industry).

(C.D. Powell)

Alex Allan, Esq.,
Foreign and Commonwealth Office.

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FM UKDEL IMF/IBRD WASHINGTON
TO DESKBY 220900Z FCO
TELNO 256
OF 211500Z NOVEMBER 88
AND TO PRIORITY LAGOS



OUR TELNOS 250 AND 251

IMF: NIGERIA
SUMMARY

1. FUND MISSION CHIEF RETURNING TO NIGERIA TODAY TO SEEK FURTHER ADJUSTMENT MEASURES. SENIOR MANAGEMENT BELIEVE AT LEAST A FURTHER 1 PER CENT OF GDP REDUCTION IN BUDGET DEFICIT NECESSARY, THAT MORE THAN THIS WOULD BE DESIRABLE, AND THEY WOULD LIKE TO SEE ALSO SOME DEBT REDUCTION OVER THE MEDIUM-TERM.

DETAIL

2. FURTHER TO OUR TURS, WE HAVE HAD FURTHER DISCUSSIONS WITH THE FUND AND BANK TODAY.

3. AS REGARDS THE BALANCE OF PAYMENTS PROJECTIONS FOR 1989 WHICH THE FUND HAVE DRAWN UP ON THE BASIS OF THE DRAFT LETTER OF INTENT, WE HAVE CONCLUDED THAT THE FINANCING GAP SHOULD BE OF THE ORDER OF DOLLARS 1 BILLION RATHER THAN DOLLARS 450 MILLION. THE DIFFERENCE IS ACCOUNTED FOR PRIMARILY BY WHAT WE SEE AS THE NEED FOR AN ADDITIONAL DOLLARS 400 MILLION BUILD-UP IN RESERVES, BUT THERE ARE SOME OTHER ITEMS (WHICH WE HAVE DISCUSSED WITH BOTTRILL). THE ADDITION TO THE RESERVES SEEMS DESIRABLE IN VIEW OF THE SIGNIFICANT DOWNSIDE RISK ON THE EXPORT PROJECTION WHICH IS BASED ON A OIL PRICE OF DOLLARS 14.50. A FUND DRAWING OF DOLLARS 600 MILLION WOULD LEAVE A RESIDUAL OF DOLLARS 500 MILLION.

4. THIS RESIDUAL GAP COULD AT LEAST IN PART BE FILLED BY A CONCESSIONAL AID PACKAGE. BUT WE WOULD ALSO NEED TO LOOK FOR SOME FURTHER COMPRESSION OF THE CURRENT ACCOUNT DEFICIT TO MAKE THE SUMS ADD UP AND TO GIVE SOME FURTHER MARGIN OF SAFETY.

5. AS INDICATED IN TURS, SENIOR FUND MANAGEMENT DO NOT REGARD THE PROPOSALS IN THE DRAFT LETTER OF INTENT AS ADEQUATE. THEY HAVE ACCORDINGLY TODAY SENT JIMENEZ BACK TO LAGOS TO NEGOTIATE A TOUGHER PROGRAM. THE DEPUTY MANAGING DIRECTOR HAS TOLD US THAT THE FUND ARE LOOKING FOR 'AT LEAST A FURTHER 1 PER CENT OF GDP' CUT IN THE BUDGET DEFICIT FOR 1989 IN WAYS THAT WILL GIVE A SUSTAINED IMPACT IN LATER YEARS. THEY ARE LOOKING PARTICULARLY FOR FURTHER INCREASES IN DOMESTIC

PETROLEUM PRICES. THEIR OTHER PRIORITY IS IN THE FOREIGN EXCHANGE AREA: THEY WILL BE LOOKING FOR A FIRM ASSURANCE THAT THE NEW INTERBANK MARKET WILL BE PROPERLY IMPLEMENTED, INCLUDING A WILLINGNESS TO SEE THE NAIRA RATE FALL TO AN AVERAGE OF 6.2 TO THE DOLLAR FOR 1989. THE DMD EMPHASISED THAT, EVEN IF THEY COULD ACHIEVE A 1 PER CENT FURTHER REDUCTION IN THE BUDGET DEFICIT, THIS WOULD STILL RESULT IN A VERY FRAGILE PROGRAM AND HE WOULD IDEALLY LIKE A SOMEWHAT LARGER ADJUSTMENT. HE WAS HOWEVER VERY CONSCIOUS OF THE POLITICAL DIFFICULTIES OF ACHIEVING EVEN A 1 PER CENT FURTHER ADJUSTMENT THOUGH--IF THERE WERE TO BE A CONCESSIONAL PACKAGE--THIS COULD ALTER THE SITUATION.

6. WE DISCUSSED THE ADJUSTMENT POSSIBILITIES ALSO WITH SENIOR BANK STAFF. KOCH-WESER AGREED THAT, FROM THE POINT OF VIEW OF THE BALANCE OF PAYMENTS, SOME FURTHER COMPRESSION OF THE BUDGET DEFICIT WAS DESIRABLE, BUT HE BELIEVED THAT ANYTHING MORE THAN A FURTHER 1 PER CENT REDUCTION WOULD BE POLITICALLY IMPOSSIBLE. HE EMPHASISED THAT FURTHER IMPORT COMPRESSION WOULD JEOPARDISE THE PROSPECTS FOR ANY SIGNIFICANT GROWTH.

7. IT IS A VERY DIFFICULT JUDGMENT AS TO HOW MUCH ADDITIONAL ADJUSTMENT THE FUND SHOULD PRESS FOR IN ORDER TO PROVIDE THE BASIS FOR A VIABLE PROGRAM. A 1 PER CENT REDUCTION WOULD STILL IMPLY A FISCAL DEFICIT OF 9.5 PERCENT OF GDP (EVEN WITH AN OIL PRICE OF DOLLARS 14.50) WHICH IS STILL SIGNIFICANTLY HIGHER THAN THE OUTTURN FOR 1987. THE VIEW OF LANKESTER AND MYSELF IS THAT 1 PER CENT IS NOT ENOUGH AND THAT--PARTICULARLY IF THERE IS TO BE A CONCESSIONAL PACKAGE--THE FUND SHOULD BE GOING FOR A 2 PER CENT REDUCTION. A REDUCTION OF THIS ORDER MIGHT IMPROVE THE CURRENT ACCOUNT BY, SAY, DOLLARS 200 MILLION.

8. WE AGREE WITH ERB'S EMPHASIS FOR THE NEED FOR REVENUE MEASURES WHICH CARRY THROUGH TO THE MEDIUM-TERM. HE ALSO STRESSED THE NEED FOR SOME DEBT REDUCTION IN VIEW OF NIGERIA'S VERY HIGH DEBT/GDP RATIO WHICH WILL MAKE IT DIFFICULT TO RESTORE THE COUNTRY TO VIABILITY. IN THE ABSENCE OF AN EARLY REDUCTION IN THE DEBT RATIOS, A FUND DRAWING WOULD LEAVE THE FUND HEAVILY EXPOSED. THE DMD SUGGESTED FIRSTLY THAT THE PARIS CLUB SHOULD OFFER NIGERIA TORONTO TERMS AND SECONDLY THAT THE BANKS SHOULD BE ASKED TO AGREE SOME DEBT REDUCTION. HE SAW BOTH OF THESE AS BEING PART OF A COMPREHENSIVE PACKAGE. WE SAID THAT WE WOULD EXPLORE THESE POSSIBILITIES AND THAT, IF MINISTERS AGREED, LANKESTER MIGHT APPROACH THE CHAIRMAN OF THE LONDON CLUB IN RESPECT OF THE BANK DEBT.

9. AS TO THE POSSIBILITY OF NON-FUND FINANCING, WE DISCUSSED WITH THE WORLD BANK THE SCOPE FOR CONCESSIONAL AID

CONTRIBUTIONS FROM OTHER DONORS. THE BANK FEEL THAT THE JAPANESE WOULD BE PREPARED TO DO MORE THAN THE DOLLARS 250 MILLION ALREADY WRITTEN IN TO THE FUND'S PROJECTIONS, PROVIDED THE UK WERE WILLING TO TAKE A STRONG LEADERSHIP ROLE. OTHER DONORS WHOM WE MIGHT PUSH HARD WERE GERMANY, ITALY AND THE EC. THE BANK VERY MUCH HOPED THAT NIGERIA WOULD BECOME ELIGIBLE FOR ESAF BUT THIS WOULD NOT BE AVAILABLE BEFORE NEXT APRIL.

10. WE HAVE EMPHASISED THROUGHOUT THAT THE UK IS STILL CONSIDERING THE POSSIBILITY OF AN AID CONTRIBUTION AND THAT NOTHING AS YET IS DEFINITELY SETTLED.

11. FCO PLEASE ADVANCE TO SIR G. LITTLER, MOUNTFIELD, EVANS, WALSH, AND BOTTRILL (TREASURY), CARRICK, FORT AND RICHARDSON (FCO), WARE (BANK OF ENGLAND), STEPHENS (ECGD), AND AINSCOW, HUDSON AND POWER (ODA).

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MR HEATH'S CALL ON ABUBAKAR ALHAJI, MINISTER FOR BUDGET

NIGERIAN ECONOMY:

SUMMARY

1. WHEN MR HEATH CALLED ON ABUBAKAR ALHAJI (AAA), MINISTER OF STATE FOR BUDGET AND PLANNING, ON 21 NOVEMBER, ABUBAKAR ALHAJI MADE A FURTHER STRONG PLEA FOR A GREATER UNDERSTANDING OF NIGERIA'S ECONOMIC PROBLEMS FROM THE WESTERN POWERS, AND PARTICULARLY FROM BRITAIN. HE WAS CLEARLY DEPRESSED BY THE NEWS THAT THE LETTER OF INTENT AGREED WITH THE IMF TEAM DURING ITS LAST VISIT TO LAGOS HAD NOT BEEN FOUND ACCEPTABLE IN WASHINGTON, AND SAID THAT POLITICAL REALITIES PREVENTED NIGERIA GIVING MORE THAN IT HAD OFFERED SO FAR.

DETAIL

2. MR HEATH CALLED UPON ABUBAKAR ALHAJI AS ONE OF HIS GOVERNMENT CALLS OUTSIDE THE PROGRAMME OF ARTHUR ANDERSEN'S COMMEMORATIVE ACTIVITIES. I ACCOMPANIED HIM. AAA WAS IN A DEPRESSED MOOD. HE SAID HE HAD BEEN ON THE TELEPHONE ALL WEEKEND TO WASHINGTON HAVING DISCOVERED THAT THE LETTER OF INTENT AGREED SO LABORIOUSLY WITH JIMENEZ DURING THE LAST WORLD BANK MISSION TO NIGERIA, HAD NOT BEEN AGREED IN WASHINGTON. HE HAD NOT YET HAD FULL DETAILS, BUT HE STRONGLY SUSPECTED THAT BRITAIN HAD BEEN AMONG THE MOST HARD-NOSED IN THIS. HE KNEW LANKESTER WAS IN WASHINGTON AND THOUGHT IT LIKELY HE HAD GONE TO STIFFEN RESISTANCE TO THE TERMS JIMENEZ HAD AGREED IN LAGOS. HE ALSO SUSPECTED WE HAD HAD ACCESS TO THEIR FIGURES FOR THE PARIS CLUB JANUARY MEETING, AND THAT THIS HAD ALSO MADE US THINK MORE MUST BE DONE. HE SAID HE ASSUMED THAT THE PURPOSE OF JIMENEZ'S TRIP TO NIGERIA STARTING 22 NOVEMBER, WAS TO TRY TO SQUEEZE FURTHER CONCESSIONS OUT OF THE NIGERIAN GOVERNMENT. THIS WOULD JUST NOT BE POSSIBLE. HE APPEALED TO MR HEATH TO TAKE THE MESSAGE BACK TO LONDON THAT NIGERIA WAS UP AGAINST THE POLITICAL LIMITS OF WHAT COULD BE DONE. HUNDREDS HAD DIED IN ALGERIA WHEN THE ECONOMIC SQUEEZE HAD PROVOKED STRONG REACTIONS. THE SAME WOULD HAPPEN IN NIGERIA. UNEMPLOYMENT HAD GREATLY INCREASED. PEOPLE WERE

HUNGRY. THE PRICES OF IMPORTS WERE CURTAILING THE ACTIVITIES OF MANUFACTURERS. THE BUDGET DEFICIT AT NAIRA 8.5 BILLION IN 1988 WAS TO BE BROUGHT DOWN TO 4 BILLION IN 1989. IT WAS NOT POSSIBLE TO DO MORE THAN THIS IN ONE YEAR. NIGERIA HAD TO BE GIVEN A LITTLE MORE TIME - AT LEAST THREE YEARS. NIGERIA, EVERYONE ACKNOWLEDGED, WAS ON THE RIGHT COURSE, AND THEY WERE GOING AS FAST AS THEY COULD GO WITHOUT RISKING THE COLLAPSE OF THE WHOLE POLITICAL SYSTEM. HE DID NOT WANT TO HAVE TO RENOUNCE DEBTS. HE DID NOT WANT TO HAVE TO REPUDIATE THE STRUCTURAL ADJUSTMENT PROGRAMME. HOWEVER, THE REPRESENTATIVES OF THE WESTERN COUNTRIES, WITH THE UK TAKING A SIGNICICANTLY HARDER LINE THAN GERMANY, THE US, JAPAN OR FRANCE, SHOULD NOT EXPECT NIGERIA TO DO THE IMPOSSIBLE. THE REST OF THE WORLD STILL REGARDED NIGERIA AS BEING IN BRITAIN'S ZONE OF INFLUENCE AND IF BRITAIN STAYED SILENT OR DID NOT SUPPORT NIGERIA'S EFFORT TO DIG THEMSELVES OUT OF THEIR HOLE, THEN OTHER COUNTRIES WOULD TAKE THEIR CUE FROM THE UK. THE NIGERIAN GOVERNMENT HAD THOUGHT AT THE TIME OF THE PRIME MINISTER'S VISIT IN JANUARY THAT WE HAD DECIDED TO GIVE THEM OUR SUPPORT, BUT THIS HAD NOT BEEN BORNE OUT BY EVENTS. THE FALLING OIL PRICE WAS COMPOUNDING THEIR DIFFICULTIES. AN OIL PRICE OF LESS THAN DOLLARS 14 IN 1989 WOULD MAKE A REALISTIC BUDGET IMPOSSIBLE.

3. MR HEATH RESPONDED THAT HE COULD APPRECIATE THAT THESE WERE DIFFICULT TIMES FOR NIGERIA BUT WONDERED IF THE NIGERIAN GOVERNMENT COULD NOT DO A LITTLE MORE TO WIN THE IMF AGREEMENT UPON WHICH SO MUCH ELSE DEPENDED. HE SAID HE COULD UNDERSTAND CLEARLY THE DIFFICULTIES WHICH THE MINISTER HAD DESCRIBED, AND AGREED THAT HE WOULD TAKE BACK THE MESSAGE THAT AAA HAD SPELLED OUT.

4. I ASKED AT ONE POINT WHETHER THERE WAS NOT ANY CHANCE THAT NIGERIA MIGHT ACCEPT THE IMF'S STAND-BY LOAN. AAA REPLIED THAT I HAD BEEN IN LAGOS LONG ENOUGH TO KNOW THE POLITICAL REALITIES OF THAT: IT WAS SIMPLY SOMETHING THE GOVERNMENT COULD NOT DO HAVING HAD THE LENGTHY PUBLIC DEBATE ON THE ISSUE TWO YEARS AGO AND HAVING PLEDGED ITSELF NEVER TO ACCEPT IMF MONEY IN THIS WAY. I ALSO SAID THAT THE PETROL PRICE, DESPITE THE TROUBLED HISTORY OF THIS ISSUE, WAS ALSO COMING UNDER INTERNATIONAL SCRUTINY AGAIN AND ASKED WHETHER SOMETHING MORE COULD NOT BE DONE ON THAT. AAA SAID THAT I WAS SPEAKING TO THE CONVERTED. THE GOVERNMENT KNEW THE PRESENT PETROL PRICE WAS LUDICROUS. IT WAS EVEN LOWER THAN THE PRICE IN SAUDI ARABIA. HOWEVER MORE THAN 10 PEOPLE HAD BEEN KILLED IN THE RIOTS WHICH FOLLOWED A TINY INCREASE EARLIER THIS YEAR. THE GOVERNMENT HAD GOOD REASON TO THINK IT WAS TOO EXPLOSIVE AN ISSUE TO TOUCH IN THE NEAR FUTURE.

5. AFTER THIS ABUBAKER ALHAJI BADE GOODBYE TO MR HEATH BUT ASKED ME TO STAY. HE THEN SAID HE WISHED TO DISCUSS THEIR DEBT OF DOLLARS 20M TO GEORGE WIMPEY AND CO, ON WHICH SEE MY SEPARATE TELEGRAM. BEFORE DISCUSSING THE WIMPEY DEBT HOWEVER HE AGAIN UNDERLINED THE DEBT - IMF SITUATION. HE SAID THAT WHEN JIMENEZ RETURNED IT WOULD OF COURSE BE OPEN TO THE NIGERIA TO AGREE TO, AND SIGN, IMPOSSIBLE UNDERTAKINGS KNOWING THAT HE COULD NOT MEET THEM. HE HOPED WE WOULD EXPECT HIM TO BE MORE RESPONSIBLE THAN THAT.

COMMENT

6. CLEARLY AAA WAS FULLY AWARE OF THE SITUATION AS DESCRIBED IN UKDEL IMF/IBRD WASHINGTON TELNOS 250 AND 251 AND SUSPECTED THAT WE HAD TAKEN A STRONG LINE IN WASHINGTON OPPOSING ACCEPTANCE OF THE DRAFT LETTER OF INTENT.

7. IT IS LIKELY OF COURSE THAT NIGERIA VIEWED ONLY IN ECONOMIC TERMS CAN SQUEEZE OUT MORE EITHER BY CUTTING BACK EXPENDITURE YET FURTHER OR INCREASING REVENUE, BUT, AS STATED IN PREVIOUS TELEGRAMS (EG TELNO 1100), I DO BELIEVE THAT AAA IS RIGHT IN SAYING THAT THEY ARE CLOSE TO THE EDGE IN POLITICAL TERMS. THEY HAVE TAKEN A LOT OF VERY TOUGH MEASURES OVER TWO YEARS AND HAVE SEEN NOTHING BY WAY OF NEW MONEY FROM US OR FROM MOST OTHER CREDITOR COUNTRIES. IT IS NEVER EASY TO KNOW WHEN ONE IS CRYING WOLF, BUT I DOUBT WHETHER THIS ADMINISTRATION CAN DO MUCH MORE WITHOUT RISKING ITS VERY EXISTENCE, AND SUGGEST WE MUST TAKE THIS INTO ACCOUNT AS MUCH AS THE FIGURES IN THE ECONOMIC EQUATION IN DETERMINING OUR ATTITUDE.

HEAP

YYYY

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TO DESKBY 240800Z LAGOS

TELNO 794

OF 231800Z NOVEMBER 88

INFO IMMEDIATE UKDEL IMF/IBRD WASHINGTON

UKDEL TELNO 256: IMF - NIGERIA

1. JIMENEZ SHOULD RECEIVE INFORMATION ON 23 NOVEMBER FROM FUND SENIOR MANAGEMENT THAT UK PREPARED TO CONTRIBUTE TO A CONCESSIONAL FINANCING PACKAGE FOR NIGERIA AND TO ENCOURAGE OTHER DONORS TO TAKE PART, PROVIDED THAT THE FUND PROGRAMME IS STRENGTHENED AND THAT OTHER DONORS COME IN. (A UK CONTRIBUTION OF THE ORDER OF 100 MILLION DOLLARS AND A CONTRIBUTION FROM OTHERS OF AT LEAST 150 MILLION DOLLARS, AND PREFERABLY MUCH MORE, WILL BE NEEDED) UKDEL IS REPORTING THESE DEVELOPMENTS IN MORE DETAIL.

2. YOU SHOULD SEEK AN EARLY MEETING WITH AAA PREFERABLY AFTER HE HAS SPOKEN TO JIMENEZ AND YOU HAVE CHECKED WITH JIMENEZ ON THE OUTCOME. YOU SHOULD NOT AT THIS STAGE SPELL OUT THE FIGURES TO HIM. WE HAVE NO WISH TO START AN AUCTION. (IF AAA GETS THE FIGURES FROM JIMENEZ, YOU MAY CONFIRM.)

3. YOU SHOULD INFORM AAA THAT WE ARE PREPARED TO LEAD A RESCUE PACKAGE WITH OTHERS TO HELP FILL THE FINANCING GAP PROVIDED THAT THE NIGERIANS REACH AN AGREEMENT WITH FUND MANAGEMENT THAT WOULD BE ACCEPTABLE TO THE BOARD. LANKESTER'S EFFORTS IN WASHINGTON THIS PAST WEEK HAVE ALL BEEN DIRECTED TO IMPROVING THE CREDIBILITY OF THE PROGRAMME FOR THE BOARD, NOT (NOT) TO STIFFENING FUND MANAGEMENT RESISTANCE (YOUR TELNO 1161). DETAILS OF THE PROGRAMME ARE NOT FOR US TO PROPOSE. WE RECOGNISE THAT THE NIGERIANS HAVE ALREADY TAKEN EXTENSIVE MEASURES BUT A WEAK PROGRAMME WOULD COME UNSTUCK VERY QUICKLY, AND WOULD NOT SECURE THE SUPPORT OF MEMBERS OF THE BOARD. IT IS OF COURSE ALSO FOR THE NIGERIANS TO JUDGE WHICH FURTHER MEASURES MIGHT BE POLITICALLY ACCEPTABLE BUT IF DONORS ARE TO PUT IN A SUBSTANTIAL CONTRIBUTION NIGERIA MUST EXPECT TO DO ITS PART BY SOME FURTHER ADJUSTMENT AND BY DRAWING THE FUND MONEY ALREADY AVAILABLE.

4. YOU SHOULD ALSO TELL AAA THAT IF HE IS CONTENT WITH THE PACKAGE WE PROPOSE, AND CAN REACH AGREEMENT WITH IMF ON ACCEPTABLE TERMS WE INTEND IN THE NEXT DAYS TO LOBBY OTHER PROSPECTIVE DONORS IN SUPPORT OF A FUND PROGRAMME, AN AID PACKAGE AND A PARIS CLUB DEAL. WE CAN THEREFORE PROMISE HIM ALL COOPERATION AND WOULD HOPE TO SEE HIM IN LONDON NEXT WEEK ON HIS

WAY TO WASHINGTON AND WILL TRY TO ARRANGE A MEETING WITH THE
CHANCELLOR.

HOWE

YYYY

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MR WICKS NO 10 DOWNING ST

NNNN

CONFIDENTIAL
FM UKDEL IMF/IBRD WASHINGTON
TO DESKBY 240900Z FCO
TELNO 258
OF 231500Z NOVEMBER 88
AND TO IMMEDIATE LAGOS

MY TELNO 256

IMF: NIGERIA
SUMMARY

1. FUND AND BANK MANAGEMENT INFORMED OF UK PROPOSALS FOR ASSISTING NIGERIA. FUND WELCOMED THESE, BUT STILL CONCERNED ABOUT DEBT OVERHANG IN LONGER-TERM. BANK LESS ENTHUSIASTIC ABOUT STIFFENING OF CONDITIONALITY AND WORRIED ABOUT TIGHT TIMETABLE FOR BRINGING TIPL LOAN TO BOARD.

DETAIL

2. LANKESTER AND I HAD FURTHER DISCUSSIONS WITH FUND AND BANK MANAGEMENT THIS MORNING. WE REPORTED TO ERB THE AGREEMENT REACHED IN LONDON THAT THE UK WOULD PROVIDE UP TO DOLLARS 100 MILLION OF CONCESSIONAL FINANCE FOR NIGERIA IN 1989 PROVIDED THAT:

- (I) THE NIGERIAN GOVERNMENT AGREED TO A FUND PROGRAM THAT INCLUDED:
 - (A) AN ADDITIONAL 2 PER CENT REDUCTION IN THE FISCAL DEFICIT IN 1989, TO 8.5 PER CENT OF GDP, WITH FOLLOW THROUGH IN 1990:
 - (B) A TIMETABLE THAT WOULD ACHIEVE POSITIVE REAL INTEREST RATES BY END 1989:
 - (C) EARLY INTRODUCTION OF THE REFORM OF THE FOREIGN EXCHANGE MARKET AND A WILLINGNESS TO LET THE EXCHANGE RATE GO QUICKLY DOWN TO AT LEAST 6.2 NAIRA TO THE DOLLAR:
- (II) OTHER DONORS AGREED TO CONTRIBUTE AT LEAST DOLLARS 150 MILLION, MAKING A TOTAL PACKAGE OF AT LEAST DOLLARS 250 MILLION.

WE ALSO STRESSED THE IMPORTANCE THAT LONDON ATTACHED TO THE NIGERIANS ACTUALLY MAKING A DRAWING.

3. ERB WELCOMED ALL THE SUGGESTIONS FOR STIFFENING THE ADJUSTMENT MEASURES. ON THE NIGERIANS ACTUALLY DRAWING, HE SAID THAT THIS WAS STILL VERY DIFFICULT POLITICALLY. THE FUND HAD BEEN PRESSING THE NIGERIANS TO COMMIT THEMSELVES TO DRAW IF THE OIL PRICE FELL BELOW THE DOLLARS 14.5 LEVEL ASSUMED IN THE FINANCING PROJECTIONS. HE THOUGHT THIS THIS WOULD BE AN EASIER PRESENTATION FOR THEM TO ACCEPT. WE SAID THAT WE THOUGHT HIS APPROACH ON THIS WAS AN ACCEPTABLE ONE.

4. WE STRESSED THAT THE PACKAGE SHOULD BE PUT TO THE NIGERIANS AS ONE THAT WAS LED BY THE IMF/WORLD BANK--LN OTHER WORDS AS A MULTILATERAL DEAL. IT WAS IMPORTANT THAT IT WAS MADE CLEAR TO THE NIGERIANS THAT FUND MANAGEMENT WAS SEEKING THE TOUGHENING TO THE TERMS IN THE EARLIER DRAFT LETTER OF INTENT, SINCE THE NIGERIANS SEEMED TO HAVE FORMED THE IMPRESSION THAT THE PRESSURE WAS COMING FROM THE UK. ERB AGREED THAT JIMENEZ SHOULD BE TOLD TO MAKE THIS CLEAR.

5. ERB THEN RAISED AGAIN THE QUESTION OF POSSIBLE DEBT REDUCTION. LANKESTER EXPLAINED THAT THIS WOULD BE VERY DIFFICULT BUT THAT WE WOULD BE GIVING FURTHER THOUGHT TO IT. ERB PRESSED QUITE HARD, SAYING AT ONE POINT THAT THE FUND'S WILLINGNESS TO GO AHEAD WOULD DEPEND ON CREDITORS' WILLINGNESS TO EFFECT A DEBT REDUCTION, BUT HE AGREED THAT SUCH ACTION MIGHT TAKE PLACE ONLY AFTER A YEAR OF GOOD PERFORMANCE BY NIGERIA. HIS MAIN POINT WAS THAT THERE SHOULD BE AN UNDERSTANDING UP FRONT THAT SOMETHING ON THESE LINES NEEDED TO BE SERIOUSLY CONSIDERED.

6. HE ALSO TOUCHED ON THE POSSIBILITY OF ESAF MONEY, POINTING OUT THAT ANY ADDITION TO THE COUNTRIES ON THE ORIGINAL LIST WOULD POSE DIFFICULT PROBLEMS. IT WOULD BE HARD TO ADD NIGERIA TO THE LIST, BUT IT WOULD ALSO BE HARD TO FIND REASONS FOR NOT DOING SO. THE AMOUNTS THAT WOULD BE INVOLVED WOULD CREATE SPECIAL PROBLEMS. HE MENTIONED THAT THE MANAGING DIRECTOR IN THINKING ABOUT THIS HAD ALREADY RAISED THE QUESTION OF WHETHER ADDITIONAL AMOUNTS FOR ESAF MIGHT BE SOUGHT. WE SAID THAT THAT WOULD PRESENT GREAT DIFFICULTIES TO OURSELVES AND OTHER DONORS, GIVEN THE ALREADY SUBSTANTIAL ACTION WE WERE PREPARED TO TAKE TO ASSIST NIGERIA. IF NIGERIA WERE TO GET ESAF FUNDS SOME SPECIAL ARRANGEMENT WOULD BE NEEDED TO LIMIT

THE AMOUNT FOR WHICH THEY WERE ELIGIBLE.

7. WE THEN WENT OVER THE SAME GROUND WITH KOCH-WESER AND OTHERS FROM THE WORLD BANK. THEY WERE PLEASED AT THE ADDITIONAL FINANCING PROPOSED AND THOUGHT THAT THE FIGURE OF DOLLARS 250 MILLION WAS FAR SMALLER THAN COULD IN FACT BE ACHIEVED. PROVIDED THE BOARD AGREED THE TIPL IN DECEMBER ANOTHER DOLLARS 200 MILLION COULD BE SECURED FROM JAPAN IN THE CURRENT FINANCIAL YEAR, WHICH WOULD IMPROVE THE PROSPECTS FOR A BIGGER JAPANESE CONTRIBUTION IN 1989. PREDICTABLY THEY WERE LESS THAN ENTHUSIASTIC ABOUT THE TOUGHENING OF THE ADJUSTMENT MEASURES, PARTICULARLY THE FISCAL POLICY. WE EMPHASISED TO THEM THAT THIS WAS AN ESSENTIAL PART OF THE DEAL.

8. THEY THOUGHT IT IMPORTANT TO MAKE CLEAR TO THE NIGERIANS THAT THIS DEAL WAS FOR REAL. TO THAT END THEY SUGGESTED THAT IT WOULD BE HELPFUL IF THE HIGH COMMISSIONER WERE TO SEEK AN EARLY MEETING WITH ABUBAKAR ALHAJI (AAA) TO EXPLAIN TO HIM THAT THE UK WAS PREPARED TO COME IN AND HELP PROVIDED THAT THE NIGERIAN GOVERNMENT WAS WILLING TO SUSTAIN A SUFFICIENT PROGRAM OF ADJUSTMENT AND THAT OTHER DONORS WERE WILLING TO CONTRIBUTE. HE SHOULD NOT GO INTO THE DETAILS OF THE ADDITIONAL ADJUSTMENT MEASURES INVOLVED--THAT SHOULD BE LEFT TO JIMENEZ--BUT HE SHOULD MAKE IT ABSOLUTELY CLEAR TO AAA THAT THE BANK COULD NOT MOVE AHEAD ON ITS OWN LOANS UNLESS THERE WERE AN AGREEMENT WITH THE FUND. WE ENDORSE THIS SUGGESTION AND HAVE PASSED IT ON BY TELEPHONE TO MOUNTFIELD.

9. THE BANK'S OTHER MAIN CONCERN WAS OVER TIMING. BANK BOARD DISCUSSION IS NEEDED BEFORE CHRISTMAS SO THAT THE DECISION ON THE TIPL CAN BE TAKEN INTO ACCOUNT BY THE NIGERIANS IN PREPARING THEIR END-YEAR BUDGET. THE TIMETABLE NOW IS EXTREMELY TIGHT. THEY WOULD WISH TO CIRCULATE A PAPER TO THE BANK BOARD BY THE END OF NEXT WEEK FOR A BOARD MEETING ON DECEMBER 20 OR 22. WE STRESSED THAT THEY SHOULD AVOID AT ALL COSTS CREATING ANOTHER SITUATION OF THE SORT THAT WE HAD ON HONDURAS/ARGENTINA WHERE THE BANK HAD COME TO THE BOARD WITH POLICY LOAN PROPOSALS BEFORE THERE WAS AN AGREEMENT WITH THE FUND. WE WERE ASKED OUR ATTITUDE TO TWO POSSIBILITIES: (I) WHETHER IT WOULD BE SUFFICIENT IF BY THE TIME OF THE BANK BOARD MEETING THERE HAD BEEN AGREEMENT ON A LETTER OF INTENT

WITH THE IMF: AND (II) WHETHER IT WOULD BE POSSIBLE TO AGREE TO FIRST TRANCHE DISBURSEMENT BEFORE THE PROGRAM HAD BEEN APPROVED BY THE FUND BOARD. WE SAID THAT WE WOULD DISCUSS THESE QUESTIONS IN LONDON AT THE BEGINNING OF NEXT WEEK. PROVISIONALLY WE THOUGHT THAT THE AGREEMENT OF A SATISFACTORY LETTER OF INTENT MIGHT BE SUFFICIENT: BUT SAW GREATER DIFFICULTIES WITH DISBURSEMENT BEFORE THE FUND BOARD MEETING.

10. KOCH-WESER SAID THAT GIVEN THE ACUTE TIMETABLE PROBLEM, THE UK OFFICE SHOULD SEEK AGREEMENT TO A SHORTENING OF TIME FOR THE CIRCULATION OF THE DOCUMENTS TO THE BANK BOARD. WE SAID WE WOULD CONSIDER THIS AND LET THEM KNOW OUR ANSWER EARLY NEXT WEEK. THERE CAN BE NO ASSURANCE THAT OTHER DIRECTORS WOULD AGREE TO THIS.

11. IN HIS OBSESSION WITH THE TIMETABLE KOCH-WESER WAS KEEN ON GETTING AAA TO HAVE DISCUSSIONS IN WASHINGTON AND LONDON NEXT WEEK. HE DID NOT BELIEVE AN AGREEMENT COULD BE SEWN UP IN LAGOS. WE STRESSED THAT IT WAS VERY IMPORTANT THAT JIMENEZ WAS GIVEN EVERY OPPORTUNITY TO AGREE A DEAL OUT THERE. IF AAA WISHED TO COME TO WASHINGTON, WE WOULD CERTAINLY ENCOURAGE HIM TO CALL ON THE UK TREASURY ON HIS WAY THERE. BUT IT WOULD BE HIGHLY PREMATURE AT THIS TIME TO SUGGEST THAT: IT WOULD CUT THE GROUND FROM UNDER JIMENEZ. (COMMENT: IT HAS SINCE EMERGED THAT KOCH-WESER HAS URGED AAA TO COME TO WASHINGTON. THE FUND IS UNDERSTANDABLY GREATLY ANNOYED. THEY FEEL THAT AAA SHOULD STAY IN LAGOS, KEEPING CLOSE TO BABANGIDA. IT IS VERY IMPORTANT TO KEEP THE BANK IN LINE ON THIS.)

12. FCO PLEASE ADVANCE TO SIR G. LITTLER, LANKESTER, MOUNTFIELD, EVANS, WALSH, AND BOTTRILL (TREASURY), CARRICK, FORT AND RICHARDSON (FCO), WARE (BANK OF ENGLAND), STEPHENS (ECGD), AND AINSCOW, HUDSON AND POWER (ODA).

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ADDITIONAL 1

MR WICKS NO 10 DOWNING ST

NNNN

FROM: P MOUNTFIELD
DATE: 24 NOVEMBER 1988

CHIEF SECRETARY

cc: Chancellor - 2.1
Economic Secretary
Sir P Middleton
Sir G Littler
Mr Anson
Mr Lankester o/r
Mr Evans
Mr Turnbull
Mr Bottrill
Mr P Davis
Mrs Thomson
Mrs Chaplin
Mr Call
Mr Tyrie

NIGERIA: AID PACKAGE

I understand that the Foreign Secretary confirmed this morning his offer of £10 million from the Aid Programme in 1989/90, but did not clarify the position about the two later years. I am not clear whether you accepted his £10 million offer; it might be worth pressing him to increase this. In case you think it is still worth having a go, I attach a letter in this sense. If you have abandoned hope of improving on the £10 million offer, we should still write about the two subsequent years.

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P MOUNTFIELD

DRAFT LETTER TO SECRETARY OF STATE FOR FOREIGN AND COMMONWEALTH
AFFAIRS

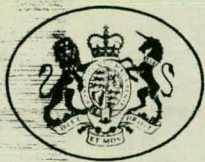
NIGERIA

We had a word at Cabinet yesterday about the proposed British offer of bilateral aid to Nigeria, in the context of its IMF programme. We have already agreed that it would be sensible to make an offer of \$100 million (say roughly £60 million) in Calendar 1989, the bulk of which should fall in our financial year 1989/90. You offered to make £10 million available from within the already-approved Aid Programme towards this. This would leave me to find up to £50 million from the Reserve. I believe you could do more than this. I note that, although there is only £114 million allocated for African Programme Aid in your current Aid Budget (after taking account of the recent PES additions, and of various other changes) you also have £191 million allocated to capital aid in Sub-Saharan Africa. Between these two heads, I am sure that, with some reordering of priorities, you could find room for £15 million, and I must ask you to do this.

It seems likely that, if the UK proposal is successful, it will need to be followed up by further assistance on broadly the same scale in subsequent years. You asked in your letter for an assurance that this could be regarded as an agreed PES bid for both years. I am afraid I cannot agree to this. I recognise, of course, that some additional funding will be necessary if a programme of assistance on this to Nigeria on this scale continues. But I must reserve my position on the respective shares until we have a chance to see the way this is developing,

and can consider the other pressures on your budget, in the course of the PES round next summer.

More generally, I am very pleased to hear that the UK offer has been well received in Lagos, and may have been instrumental in persuading the Nigerians to accept the tougher terms required by the Fund. We must wait and see whether events bear out these initial reports.



CH/EXCHEQUER	
REC.	25 NOV 1988
TO	Mr BOTTRILL
COPIES TO	CST, EST, Sir P. MIDDLETON, Sir G. LITTLE, Mr ANSON, Mr SCHOLAR, Mr LANKESTER, Mr TURNBULL, Mrs LOMAX, Mr MOUNTFIELD, Mr H.P. EVANS, Mr P.G.F. DAVIS, Mr WALSH, Mrs THOMPSON, Mr TYRRE.

Foreign and Commonwealth Office

London SW1A 2AH

25 November 1988

Dear Charles,

Nigeria

The Foreign Secretary has seen a copy of Jeremy Godfrey's letter of 23 November to you about the need to come to a decision on ECGD cover for the Biwater Water Supply project in Nigeria.

We understand that Biwater are claiming that they will be unable to stall their negotiations with the Nigerians much longer without a decision on ECGD cover. If this is the case, the Foreign Secretary would strongly endorse the point in Jeremy Godfrey's letter about the risk of the Nigerians accusing us of a breach of good faith. The Prime Minister, at the State Banquet in her honour in Lagos in January, announced our intention to proceed speedily with negotiations to finance the project's completion; and described it as an important and worthwhile project. It is true that since then the Nigerians have fallen into arrears with their moratorium interest repayments to ECGD. But at the time of the Prime Minister's visit their payments were up to date. As this was then our condition for proceeding, President Babangida could, literally, regard his part of the bargain as having been honoured.

Since then, however, economic conditions in Nigeria have worsened significantly. The Foreign Secretary suggests, therefore, that before reaching a final decision on the Biwater project, we should quickly check with the Nigerians to ensure that they still view the project as a top priority for completion. We will then know whether, given their economic straits and the fact that the project has no perceptible foreign exchange earning potential, the Nigerians still consider that the cost of taking on further commercial credits for this project is justified. Meanwhile the letter from the Prime Minister to Adrian White could issue as drafted.

I am copying this letter to Alex Allan (HMT) and Jeremy Godfrey (DTI).

Yours ever,
Lyn Parker

(L Parker)
Private Secretary

C D Powell Esq
10 Downing Street

FROM: A R H BOTTRILL
DATE: 25 November 1988

PS/CHIEF SECRETARY

cc PS/Chancellor
PS/Economic Secretary
Sir P Middleton
Sir G Littler
Mr Anson
Mr Scholar
Mr Lankester
Mr Turnbull
Mrs Lomax
Mr Mountfield
Mr H P Evans
Mr P G F Davis
Mr H G Walsh
Mrs Thomson
Mr T Jones
Mr Tyrie

NIGERIA : BIWATERS

Jeremy Godfrey's letter of 23 November to Charles Powell at No 10 argued that ECGD should confirm to Biwaters its willingness to guarantee a £22.4 million loan (DML £34.3 million) to Niger State to allow completion of a water project.

2. You will recall that the Prime Minister agreed during her visit to Lagos in January that in view of Nigeria's readiness to settle its then arrears to ECGD, the UK would proceed with negotiations to finance the project. The Nigerians, however, failed to make subsequent payments due to ECGD, and we agreed with ECGD officials that the Biwater loan agreement should not be signed until arrears of payments due to ECGD on 30 June were made in full. These currently still total £33 million.

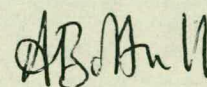
3. Biwaters have now suggested to Lord Young and No 10 that the loan agreement should be signed which would enable a down payment by the Nigerians to be released and Biwaters to start work. The effectiveness of the ECGD-guaranteed loan itself, however, would depend on Nigeria's performance under its bilateral rescheduling agreement which is a default condition in the loan. ECGD was reluctant to accept Biwaters' compromise, partly because the bilateral would actually be in default at the time of signature, but in a change of its previous position ECGD is now ready to recommend signature of the loan.

4. Our own view is that we should still not allow ECGD to sign the loan agreement at this stage. Negotiations with the IMF are progressing but have not been concluded. We should have a clearer idea during the course of next week whether the Nigerians are prepared to take measures which satisfy both the IMF and ourselves. It will take some while longer, however, to put together the necessary donors' financing to accompany the package. On the assumption that both these stages are achieved, a Fund Board agreement would then open the way for a Paris Club rescheduling and the regularising of Nigeria's arrears position. We cannot be sure of the precise timetable but the IMF and Paris Club meetings might be in January.

5. This would involve a postponement of a further few weeks for Biwaters but would safeguard ECGD against collapse of the IMF/donor negotiations which would not only mean no payment of current arrears but also lead to a high risk of claims by Biwater if the loan is signed now. I recommend that ECGD should be told to delay signature either until our original condition of repayment of arrears is met or an IMF programme is approved by the Fund Board - whichever is earlier.

6. We understand that the Foreign Secretary is being advised that we should check with the Nigerians whether in view of the public investment cuts in their 1989 budget, this project is still one of their priorities. This, too, would win us a little time. You might, however, suggest that the Biwater compromise should be explored further but on the condition that the Nigerians are warned that default will be called and the loan not become effective if their arrears position is not regularised either through payments being made or as a result of a Paris Club rescheduling. This should be acceptable to the Nigerians if they expect genuinely to sign an IMF programme and Paris Club deal. It would remove any question of bad faith by the UK.

7. I attach a draft.



A R H BOTTRILL

DRAFT PS REPLY TO JEREMY GODFREY

NIGERIA : BIWATERS

The Chief Secretary has seen your letter of 23 November. He agrees that the general approach we are now adopting to Nigeria offers the best chance of improving the Nigerian economy and safeguarding the UK's stake in the country.

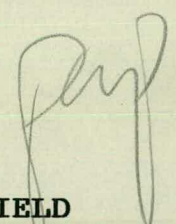
2. Negotiations with the IMF, however, have not yet been concluded, nor has essentially additional financing by other donors been agreed. Both these need to be achieved before we can be confident that Nigeria will have a satisfactory IMF programme which would open the way for a Paris Club rescheduling and a regularising of Nigeria's external payment, including its arrears to ECGD.

3. In the circumstances, I believe that we should stick to the existing position agreed earlier at official level between Departments that the Biwaters loan agreement should not be signed until Nigeria has paid the outstanding arrears to ECGD which currently total some £32 million.

4. We can review the situation in the light of progress with the IMF programme and donor financing package. In the meantime, perhaps our officials might explore further whether the compromise

suggested by Adrian White is viable. If we were to follow this route, I believe that we should need to make it clear to the Nigerians that default would be called and the loan would not become effective if their arrears to ECGD were not cleared.

JM



FROM: P MOUNTFIELD

DATE: 25 NOVEMBER 1988

CHANCELLOR OF THE EXCHEQUER

cc: Chief Secretary
Economic Secretary
Sir P Middleton
Sir G Littler
Mr Anson
Mr Cassell, UKDEL
Mr Turnbull
Mr Evans
Mr Bottrill
Mr P Davis
Mrs Thomson
Mrs Chaplin
Mr Call
Mr Tyrie
Mr Enoch, UKDEL

NIGERIA: VISIT OF MINISTER OF BUDGET AND PLANNING

Alhaji Abukakar Alhaji (AAA) is coming to see you at 8.45am on Monday, on his way to Washington. Mr Lankester and I will be there. His present post is Minister of Budget and Planning; he has effectively displaced Okongwu, who remains Minister of Finance.

2. Line to take

- (i) Welcome your determination to seek an agreement with the IMF.
- (ii) Your decision to take the additional measures necessary to strengthen the programme shows great political courage. Your own part in persuading rest of Government has been crucial.

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- (iii) We have been working very hard behind the scenes to help you. Impression seems to have formed in Lagos that we are trying to toughen Fund resistance. On the contrary, we have been seeking a credible programme which we could persuade the rest of the IMF Board to support, together with adequate supporting finance.
- (iv) From what we hear, key fiscal elements of programme is now at that stage. But perhaps you could clarify envisaged action on this, and on naira exchange rate and on interest rates. Recognise that political difficulties for you at home: but important to have comprehensive programme.
- (v) Still leaves a considerable financing gap, particularly if oil price remains low.
- (vi) Very important you should be prepared to take IMF drawing if your oil price remains at \$14.50 or below. Cannot persuade other donors/creditors to join in if you will not take what is on offer from Fund.
- (vii) Fund and Bank have both recognised need for additional help. UK has now decided to "prime the pump". Geoffrey Howe and I agreed, with Prime Minister's full support, to offer \$100 million in 1989. Hope this will gear up the contributions by other creditors, leading to total package of at least \$250-300 million. Our offer is conditional on at least \$150 million extra from others (excluding \$250 from Japan already promised).
- (viii) Recognise gap will continue beyond 1989. Amounts to be sought then still for discussion. But if need is there, can assure you UK will play its part if you do in a way which secures support of other creditors.
- (ix) SBA in 1989 to be matched by generous Paris Club rescheduling. We will do our best there too. So far, best to concentrate on 1988 arrears and on 1989. Since you will need to reschedule 100 per cent of principal and of interest, including previously-rescheduled debt (PRD) in that period, Toronto terms will hardly make any difference, and difficult for creditors to swallow at this stage.

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Prefer not to risk rebuff by pressing for those now. Also problem over apparent discrimination between different government creditors. Will need to bring everyone current up to common date. Know IMF is discussing this point with you.

- (x) In longer term, further Paris Club debt relief may be needed, and Toronto terms a possibility. Will be discussing this with other creditors. Treasury officials will also discuss with Paris Club Chairman, who happens to be in London today for bilaterals. Cannot make any promises and may not be necessary.
- (xi) Hope you can get a better deal out of the banks. Unsatisfactory that Government creditors should have to carry the burden, while banks continue to take interest out of Nigeria. What are prospects of a better deal - in 1990 if not in 1989? You must persuade to be as generous as government creditors/donors.
- (xii) Revert to IMF programme. Sustainability is the key. Another set-back like 1988's reflationary budget would be disastrous. Will need four or five years' hard grind. Will pay off in the end. Meanwhile, essential that Nigeria meets all obligations following next reschedulings (banks and Paris Club). To allow arrears to build-up again after these exceptional measures would completely destroy Nigerian credibility.
- (xiii) Must assure you, UK very anxious to help. Prime Minister taking close personal interest.

Defensive

- (i) Could not have made an earlier move. Needed to know you had exhausted all other possibilities in negotiation with IMF first.
- (ii) Very conscious of risks. Major effort for Nigeria bound to have knock-on effects in other debtor

countries, not only in Africa. This makes it harder to persuade other creditors. We are doing our best.

- (iii) (AAA indicated he would ask for \$150m, not \$100m.) You must be joking. Represents significant extra cost to UK. Something like £60 million next financial year. Almost all of it additional to Aid Programme. Only just agreed £20 million increase in Aid Programme during PES round, with great difficulty; have now had to add this. Can tell you in confidence this represents one-third of our total programme and in all the rest of Africa. Demonstrates importance we attach to Nigeria.
- (iv) (New export credits?) Can reconsider later, but Nigeria surely does not want to add more to its debt burden than strictly necessary.

Background

3. The offer which you and Sir G Howe authorised this week seems to have done the trick. First reports from Lagos are that AAA is delighted, and says it will make all the difference. On the strength of it, he has Babangida's authority to make the necessary further budget cuts, and reach a settlement with the IMF. For a melodramatic account of his reaction, see Lagos telno 1173, attached. He is now on his way to Washington for that purpose, and has broken journey in London specially to see you.

4. The Fund are less optimistic. They have not yet seen the full details of the revised letter of Intent. They are deferring judgement until then. So must we. Our conditions were:

- (a) a further reduction in the budget deficit for 1989, of at least 2% of GDP;
- (b) changes in the foreign exchange auction leading to a devaluation to at least 6 naira to the dollar;
- (c) a timetable for a return to positive real interest rates by the end of 1989.

We are still not clear whether AAA can keep public spending in cash terms in 1989 to the same level as in 1988 at a time when inflation is around 30 per cent. What does this imply for public sector pay? We also need to be clear that AAA will allow the naira to find its own level - probably around naira 6 to the \$. We are also concerned at AAA's refusal to move more quickly towards positive real interest rates. Current rates at around 13 per cent are heavily negative. We must press AAA on these points. But it will be difficult, now, to draw back.

5. The World Bank, are repeating their line in the recent Argentina case. They are proposing to release loans ahead of approval by the IMF Board, so that Nigeria can take them into account in the preparation of the Budget. This seems quite premature, and would take the heat off Nigeria. We are trying to find some way of making approval of the IBRD loans conditional, while still giving Nigeria something to plan on. This has to be done in a way which will unlock the first tranches of the Japanese loans. A separate submission on this point follows.

6. We have been in touch with the commercial banks. Barclays are in the lead for the UK. They have been very frank with us, and see no chance of improving on the present package, which involves no new money, and requires Nigeria to pay interest, albeit on a fairly narrow spread, on the whole of the outstanding debt - with principal repayments starting in the early 1990s. Mr Lankester, at the request of the IMF who seem to want genuine debt reduction as a condition of the package, will be seeing them again next week. He will not seek to reopen the package in 1989, but will urge them to start thinking again about 1990 and beyond. The Fund see the need for genuine debt reductions and he will gently probe their reactions.

7. The Paris Club position is a bit easier. We have already done some softening up, and most creditors accept that there is little alternative to rescheduling 100 per cent of everything, certainly in 1989. There is a big technical problem, in that some creditors have been paid interest in the first half of 1988, while

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others have not. We have not done very well ourselves. Strictly speaking, everybody should be levelled up to the treatment received by the most-favoured: but that may be too expensive for Nigeria. The IMF calculations assume everyone is paid up to end-June 1988. This is likely to be a sticking point in the negotiations. Toronto terms, as the speaking note says, are hardly relevant at this stage, and the Chairman will be very reluctant to open up that can of worms just yet. We are seeing Samuel-Lajeunesse, Trichet's Deputy, before bilaterals on Monday, and will go over all this ground with him.

8. The financing gap can, on the IMF's assumptions, just about be bridged, if everything is done: budgetary cuts in Nigeria; an aid package; World Bank loans; Paris Club. This assumes a \$600m reserve build - from an almost empty start, to provide a cushion against a fall in the oil price. An alternative, which we are discussing with the IMF, is to reduce the reserve build, but to require Nigeria to take a Fund drawing if the oil price is below \$14.50 during the first quarter of 1989. This would be activated by a contingency trigger in the formal Agreement. As you know, there is enormous political resistance in Nigeria to taking Fund money. But without at least a contingent commitment to do so, it will be difficult to persuade other donors/creditors to be generous.

9. However, the arithmetic depends crucially on the oil price assumption. The IMF are still working on \$14.50 average for 1989. Nigeria's quota is 1.3mbd. They will not be able to cheat much on this if they are to retain credibility in OPEC. Every \$1 of the oil price costs Nigeria about \$450 million in a full year. So the whole operation is still very precariously balanced.

10. If the operation continues as planned, the UK will have to mount a major lobbying exercise in the next couple of weeks, to get the other major donors/creditors on board. We plan to start this by an approach to Finance Ministries in the main Capitals next week, through diplomatic channels. We shall start with the French at our own bilateral on Monday, and Nicholas Bayne's visit to Japan on 28/29 November. There are then several good

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multilateral opportunities: the European Council on 2/3 December (we shall brief the Prime Minister); the DAC High Level Group on 6/7 December (Mr Patten); WP3 on 8, 9 and 10 December, possibly with a G7 Deputies in the margin; ECOFIN on 12 December (which will give you a good opportunity to lobby the key European Finance ministers); Basle on 12 and 13 December, for the Central Bank network; and the Anglo-Japanese bilateral on 13 December. You may also wish to talk on the telephone or write to Secretary Brady, whom we cannot reach by any of these other contacts.

RM

P MOUNTFIELD

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FM LAGOS
TO IMMEDIATE DESKBY 251030Z FCO
TELNO 1173
OF 251015Z NOVEMBER 1988
AND TO IMMEDIATE DESKBY 251030Z TREASURY
INFO IMMEDIATE DESKBY 251200Z UKDEL IMF/IBRD WASHINGTON
INFO IMMEDIATE BANK OF ENGLAND, ECGD, DTI.

ADVANCE COPY

YOUR TELNO 794: NIGERIAN ECONOMY

SUMMARY

1. THE NIGERIAN GOVERNMENT APPEAR TO HAVE MADE PLANS TO MAKE THE NECESSARY EXPENDITURE CUTS AND REVENUE INCREASES THAT SHOULD ENABLE THEM TO OBTAIN IMF APPROVAL OF THEIR PLANS, AND THUS ACTIVATE THE CONCESSIONARY AID PACKAGE LED BY OURSELVES. ABUBAKAR ALHAJI (AAA), MINISTER OF BUDGET, AND AHMED, GOVERNOR OF CENTRAL BANK WILL CALL ON THE CHANCELLOR OF THE EXCHEQUER IN LONDON ON 28 NOVEMBER.

DETAIL

2. I MET WITH JIMINEZ, LEADER OF THE IMF TEAM, ON 24 NOVEMBER TO CONFIRM THAT HE HAD PASSED DETAILS OF THE NEW PROPOSALS TO ABUBAKAR ALHAJI (AAA), BUDGET MINISTER, AND TO HEAR SOMETHING OF AAA'S REACTIONS BEFORE SEEING AAA HIMSELF. I ALSO SPOKE WITH AAA ON THE TELEPHONE, CLEARLY BEFORE HE HAD HEARD ANYTHING FROM JIMINEZ WHEN I ARRANGED A LATER MEETING AND URGED THE NEED TO NARROW THE FISCAL GAP FURTHER.

3. JIMINEZ GAVE ME A LENGTHY AND DETAILED EXPLANATION OF WHY THE NEW TERMS PROPOSED BY WASHINGTON WERE IMPOSSIBLE. HE SAID HE HAD SPENT THE MORNING WITH AAA AND SENIOR OFFICIALS. THEY HAD BEEN CRAWLING OVER THE FIGURES TO SEE WHETHER THERE WAS ANY WAY THEY COULD MEET THE ADDITIONAL 2% REDUCTION IN THE 1989 FISCAL DEFICIT (PARA 2 OF UKDEL IMF TELNO 258) AND HAD CONCLUDED THAT THIS WAS IMPOSSIBLE. THE NUMEROUS FIGURES AND ARGUMENTS HE GAVE ME ARE NOW LARGELY IRRELEVANT IN THE LIGHT OF SUBSEQUENT DEVELOPMENTS.

4. I THEN SAW ABUBAKAR ALHAJI IMMEDIATELY AFTERWARDS. IN THE LIGHT OF WHAT JIMINEZ HAD TOLD ME, I BEGAN BY SAYING THAT I WAS AWARE OF ALL THE DIFFICULTIES, POLITICAL AND ECONOMIC, OF MEETING THE

TARGETS IN THE NEW PROPOSALS, BUT HOPED HE WOULD BE ABLE TO SQUEEZE OUT SOMETHING NEW. AAA CUT ME SHORT, AND SAID I WOULD BE SURPRISED TO KNOW THAT HIS GOVERNMENT WAS VERY RESPONSIVE TO THE NEW PROPOSALS. HE SAID THAT HE HAD IN THE COURSE OF THE DAY KNOCKED A FURTHER N 1.5 BILLION FROM THEIR ALREADY DRASTICALLY PRUNED EXPENDITURE PROPOSALS FOR 1989, AND THAT HE WAS WORKING OUT ADDITIONAL REVENUE PROPOSALS WHICH WOULD BE READY BY THE DAY'S END WHICH WOULD RAISE A FURTHER N 1.3 BILLION. (THIS TO US WOULD APPEAR TO GIVE CLOSE TO THE 2% IMPROVEMENT WE ARE LOOKING FOR). I PRESSED AAA FOR DETAILS. HE WAS NOT PREPARED TO GIVE THESE, AND I SUSPECT WILL NOT REVEAL THEM UNTIL HIS VISITS TO LONDON AND WASHINGTON NEXT WEEK. I SAID I ASSUMED AN EXTRA REVENUE PROVISION OF N 1.3 BILLION MUST MEAN A SIGNIFICANT PETROL PRICE INCREASE, SINCE THERE WAS SURELY NO OTHER WAY TO PRODUCE THAT SORT OF FIGURE. HE SAID, WITH A SMILE, NO COMMENT.

5. IN VIEW OF THIS TOTAL DISPARITY BETWEEN WHAT I HAD HEARD FROM AAA AND FROM JIMINEZ, I THEN TRACKED DOWN JIMINEZ TO SEEK HIS FURTHER VIEWS. HE WAS INCREDULOUS AT MY REPORT OF AAA'S COMMENTS AND WENT OFF IMMEDIATELY TO SEE HIM HIMSELF. I THEN ARRANGED A FURTHER MEETING WITH JIMINEZ IMMEDIATELY AFTER THAT. HE TOLD ME THAT AAA HAD GIVEN HIM THE SAME STORY. HE HAD NOT BEEN GIVEN MANY FURTHER DETAILS, BUT HAD LEARNED THAT MOST OF THE EXPENDITURE CUTS WERE TO BE MADE IN THE NIGERIAN NATIONAL PETROLEUM CORPORATION (NNPC)'S BUDGET. (HE COMMENTED THAT HE HOPED THIS DID NOT MEAN THEY WERE GOING TO KILL THE GOOSE THAT LAID THE GOLDEN EGGS.) THIS MEETING BETWEEN AAA AND JIMINEZ HAD BEEN IN FRONT OF OTHER SENIOR NIGERIAN TREASURY OFFICIALS, WHO THEMSELVES WERE LEARNING OF THE NEW PROPOSED BUDGET CUTS AND REVENUE ADDITIONS FOR THE FIRST TIME. JIMINEZ SAID THEY WERE DUMBFOUNDED. JIMINEZ IS TO MEET WITH THOSE OFFICIALS TODAY, 25 NOVEMBER, WHEN HE EXPECTS TO GET FURTHER DETAILS OF THE PROPOSALS.

6. PIECING TOGETHER REMARKS MADE SEPARATELY BY AAA TO MYSELF AND TO JIMINEZ WE CONCLUDED THAT WHAT HAD HAPPENED WAS THAT ON THE MORNING OF 24 NOVEMBER AAA AND HIS OFFICIALS HAD CONCLUDED THAT THE NEW TERMS THAT THE FUND AND WE WERE SEEKING WERE IMPOSSIBLE, AND THAT THE DEFICIT COULD NOT BE FURTHER REDUCED. AAA HAD GONE TO THE PRESIDENT TO INFORM HIM OF THIS BUT SAID THAT HE HAD BEEN GIVEN A HARD TIME BY BOTH JIMINEZ AND MYSELF OVER THE NEED TO DO MORE. THE PRESIDENT HAD RESPONDED THAT AGREEMENT WITH THE IMF AND ACCEPTANCE OF THE PACKAGE WAS ESSENTIAL. THE PRESIDENT AND AAA HAD THEN SAT DOWN AND WORKED OUT THE NECESSARY CUTS AND ADDITIONAL REVENUES. AAA'S RELUCTANCE TO REVEAL DETAILS WAS

BECAUSE WHEN HE SAW ME AND THEN JIMINEZ NO-ONE ELSE, INCLUDING HIS OWN OFFICIALS, HAD BEEN TOLD.

7. I ASKED AAA ABOUT THE OTHER PROVISIONS IN THE PACKAGE. HE SAID THEY COULD NOT DO MUCH MORE ON INTEREST RATES: THEIR BASE RATE WAS NOW 13.25%. THERE WOULD BE NO GOING BACK, AND IT COULD ONLY MOVE UPWARDS. SUBSEQUENTLY JIMINEZ SAID THAT AAA HAD TOLD HIM THAT THEY MIGHT BE ABLE TO INCREASE THE INTEREST RATE. ONE MEANS OF DOING IT WOULD BE TO ABOLISH OR REDUCE THE HIGH FEES THAT BANKS HERE CHARGE FOR THEIR SERVICES INCLUDING LOANS. THUS INTEREST RATES WOULD GO UP BUT BORROWERS WOULD PAY NO MORE.

8. ON REFORM OF THE FOREIGN EXCHANGE MARKET, AAA SAID THAT WAS NO PROBLEM. HE SHOWED ME A LETTER OF 19 NOVEMBER THAT HE HAD WRITTEN TO CAMDESSUS PLEDGING TO ABOLISH THE FORTNIGHTLY FOREIGN EXCHANGE AUCTIONS BY THE END OF DECEMBER, AND TO INTRODUCE A FREE MARKET RATE WHICH WOULD NOT BE SUBJECT TO GOVERNMENT INTERFERENCE. HE SAID HE FULLY EXPECTED THIS TO RESULT IN A FURTHER SUBSTANTIAL DEVALUATION, A PROCESS WHICH HE SAID WOULD BEGIN AT YESTERDAY'S AUCTION (IT DID: THE NAIRA DEVALUED BY A FURTHER 7.1% AGAINST THE DOLLAR AND 9.2% AGAINST THE POUND).

9. COMMENTING ON THE DONOR CONTRIBUTION FIGURES IN THE PACKAGE, AAA SAID THAT HE FOUND OUR DOLLARS 100 M A LITTLE LOW. HE WOULD PRESS THE CHANCELLOR TO TRY TO MAKE IT DOLLARS 150 M.

10. I STRESSED THAT WE STILL THOUGHT IT IMPORTANT THAT NIGERIA SHOULD BE PREPARED TO MAKE AN IMF DRAWING. AAA SAID FIRMLY THAT THAT SIMPLY WOULD NOT BE POLITICALLY POSSIBLE AT ANY STAGE. JIMINEZ SUBSEQUENTLY TOLD ME THAT AAA HAD INDICATED TO HIM THAT A LINKAGE BETWEEN THE OIL PRICE AND A DRAWING (AS IN PARA 3 OF UKDEL TELNO 258) JUST MIGHT PROVE ACCEPTABLE.

11. BOTH AAA AND JIMINEZ WERE FULLY AWARE OF ALL THE FIGURES IN THE PACKAGE PROPOSAL AND TALKED OF THEM FREELY. DESPITE MY EFFORTS TO DISABUSE HIM, CLEARLY AAA STILL BELIEVES THAT WE WERE THE ONES WHO HAD FORCED THE HARSHER TERMS THAN THOSE IN THE PREVIOUS LETTER OF INTENT. JIMINEZ TOOK THE SAME LINE: WHEN I QUOTED FUND SOURCES (EG AS IN UKDEL TELNOS 250 AND 258) FOR THEMSELVES WANTING STRONGER TERMS, JIMINEZ SAID THAT WE ALONE HAD NOT BEEN PREPARED TO ACCEPT THOSE NEGOTIATED FOR THE DRAFT LETTER OF INTENT AND THE FUNDS SUBSEQUENT STRONGER LINE WAS AN ATTEMPT TO KEEP US ON BOARD. I IMAGINE IT LIKELY THAT HE HAS PUT A SIMILAR

VIEW TO AAA. NEVERTHELESS, AAA WAS CLEARLY PLEASED THAT HE WAS ABLE TO OFFER A POSITIVE RESPONSE, AND APPEARED GENUINELY GRATEFUL FOR THE UK'S CONDITIONAL OFFER OF ASSISTANCE AND PROMISE TO LOBBY FOR FURTHER SUPPORT.

12. I UNDERSTAND A HIGH LEVEL MESSAGE ON THIS ISSUE IS BEING CONSIDERED. I SUGGEST AN EARLY MESSAGE FROM THE PRIME MINISTER TO PRESIDENT BABANGIDA WOULD BE VERY VALUABLE. THIS COULD UNDERLINE OUR LEAD IN THE NEW PROPOSALS(OUR LEAD AT PRESENT HAS BEEN A LITTLE OVER-SHADOWED, SINCE THE DETAILS WERE GIVEN TO THE NIGERIANS INITIALLY BY THE IMF AND NOT BY OURSELVES), AND COULD THANK THE PRESIDENT FOR HIS CRITICAL PERSONAL INVOLVEMENT IN PRODUCING WHAT WOULD APPEAR TO BE AN ACCEPTABLE FURTHER EFFORT ON THE NIGERIAN SIDE. (BABANGIDA WE THINK WILL BE OUT OF THE COUNTRY FROM 28 NOVEMBER TO 3 DECEMBER).

13. AAA HAS CONFIRMED THAT HE WILL CALL ON THE CHANCELLOR IN LONDON AT 0845 ON 28 NOVEMBER (PRESUMABLY THE NIGERIAN HIGH COMMISSION WILL BE GIVEN THE DETAILS). HE AND AHMED, GOVERNOR OF THE CENTRAL BANK, PLAN TO LEAVE HERE ON THE NIGHT OF 26 NOVEMBER, ARRIVE LONDON EARLY 27 NOVEMBER, DEPART FOR WASHINGTON 28 NOVEMBER (THERE IS SOME DOUBT ABOUT WHETHER THEY ARE AIMING FOR THE EARLY CONCORDE FLIGHT TO NEW YORK OR A LATER FLIGHT) AND HAVE TALKS WITH THE WORLD BANK THAT EVENING. THEY PLAN DISCUSSIONS WITH CAMDESSUS AND IMF COLLEAGUES THROUGHOUT 30 NOVEMBER, AND WITH THE STATE DEPARTMENT AND EXIM BANK 1 DECEMBER, BEFORE RETURNING TO LAGOS PROBABLY AGAIN VIA LONDON.

HEAP

YYYY

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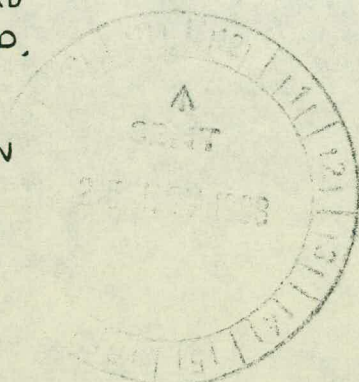
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.MONETARY
MR BAYNE
MR CARRICK
HD/ERD
Hd WAD,

HD/ECD(E)
MR LAVELLE CABINET OFFICE
MR MOUNTFIELD HM TREASURY
B.O.E.
ECCD
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PAGE 4
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10 DOWNING STREET
LONDON SW1A 2AA

26 November 1988

CH/EXCHEQUE	
REC.	28 NOV 1988
AGTIC	Mr BOTTRILL
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	Sir P. MIDDLETON
	Sir G. LITTLER, Mr LANKESTER,
	Mr MOUNTFIELD,
	Mr H. P. EVANS
	Mr P. G. F. DAVIS,
	Mr WALSH,
Mr THOMPSON, Mr TYRRE	

28/11

From the Private Secretary

NIGERIA

Thank you for your letter of 23 November about ECGD support for the Biwater contract in Niger State. I have also seen Lyn Parker's letter of 25 November.

I agree that it will be worth making a final check with the Nigerians to ensure that they still regard this project as a high priority. Meanwhile, provided the Treasury are also content, I will write to Mr. White of Biwater in the terms of the draft enclosed with your letter.

I am copying this letter to Alex Allan (HM Treasury) and to Lyn Parker (Foreign and Commonwealth Office).

(C. D. POWELL)

Jeremy Godfrey, Esq.,
Department of Trade and Industry.

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PS/Chancellor
HMT.



[Handwritten signature]

Reference our conversation on
26 November. Copy passed
direct to No. 11.

With the compliments of

Resident Clerk.

FOREIGN AND COMMONWEALTH OFFICE

LONDON, SW1A 2AH

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FM 10605

TO IMMEDIATE FCO

TELNO 1179

OF 261005Z NOVEMBER 1988

AND TO IMMEDIATE TREASURY

INFO IMMEDIATE UKDEL IMF/IBRD WASHINGTON, BANK OF ENGLAND.

INFO IMMEDIATE ECBD. DTI.

FOR IMMEDIATE ATTENTION OF RESIDENT CLERK

MY TELNOS 1173 AND 1177: NIGERIAN ECONOMY

SUMMARY

1. IMF OFFICIAL BELIEVES THAT THE NIGERIANS HAVE MADE SUFFICIENT FURTHER ECONOMIES AND PROVISIONS FOR NEW REVENUE TO SATISFY US AND THE IMF BOARD.

DETAIL

2. I HAD A FURTHER TELEPHONE CONVERSATION WITH JIMINEZ IMMEDIATELY BEFORE HE LEFT FOR WASHINGTON ON THE NIGHT OF 25 NOVEMBER. HE SAID THEY HAD MANAGED TO REACH "THE MAGICAL FIGURE" THAT SHOULD SATISFY US, ALTHOUGH HE WAS NOT AT ALL PROUD, AND INDEED WAS DEPRESSED, BY THE WAY IT HAD BEEN DONE. SOME OF THE NEW CUTS WERE IN AREAS THAT NIGERIA COULD LEAST AFFORD E.G. PRIMARY EDUCATION, BUT THE FINAL EFFECT WAS VERY CLOSE TO THE REDUCTION OF 2% IN THE FISCAL DEFICIT.

3. JIMINEZ SAID MORE HAD BEEN ACHIEVED BY CUTS THAN BY NEW REVENUE. SOMETHING WAS TO BE DONE WITH PETROL PRICES, BUT NOT VERY MUCH. IT WAS THE MOST THE MILITARY WOULD ALLOW. THE LARGEST AREA OF CUTS WAS IN NIGERIA NATIONAL PETROLEUM CORPORATION'S (NNPC) EXPENDITURE. (COMMENT: PRESUMABLY ACHIEVED MORE EASILY BECAUSE OF LUKMAN'S ABSENCE AT THE OPEC MEETING: HE MAY WELL FIGHT THIS WHEN HE GETS BACK ON THE GROUNDS THAT THE OIL INDUSTRY IS ALREADY UNDER FUNDED, HENCE THEIR CURRENT RELATIVELY LOW POTENTIAL PRODUCTION CEILING). THERE WERE SOME CUTS IN THE PROGRAMMES FOR ABUJA (NEW CAPITAL) AND AJEOKUTA (STEEL) BUT NOTHING VERY LARGE. MILITARY EXPENDITURE HAD NOT BEEN INCLUDED IN THEIR STUDY.

4. ON INCREASED REVENUE. THERE WOULD BE MAJOR INCREASES IN PUBLIC UTILITY CHARGES.

5. JIMINEZ SAID ABUBAKAR ALHAJI (AAA) HAD BEEN VERY NEGATIVE ABOUT INTEREST RATES. HE HAD PROMISED NOTHING IMMEDIATELY, AND SAID THAT ONLY LATER MIGHT HE PUSH THEM UP BY LIMITING THE BANKS' FEES (PARA 7 OF MY TELNO 1173).

6. OVERALL THIS APPEARS TO BE A SATISFACTORY OUTCOME AND CERTAINLY A MUCH BETTER ONE THAN WAS INDICATED BY THE INITIAL REACTIONS OF AAA AND JIMINEZ HIMSELF TO THE ATTEMPT TO REDUCE THE DEFICIT FURTHER. ALTHOUGH IT IS HARD TO SEE FROM THE EVIDENCE AVAILABLE SO FAR QUITE WHERE THE SUFFICIENT ORDER OF EXPENDITURE CUTS AND ADDITIONAL REVENUE ARE COMING FROM, CLEARLY JIMINEZ'S ASSURANCE THAT THE 2% FIGURE HAS BEEN LARGELY MET IS A USEFUL CONFIRMATION OF AAA'S PROMISES.

7. MOST OTHER CREDITOR COUNTRIES WILL NOT YET I THINK KNOW MUCH ABOUT THESE DEVELOPMENTS FROM HERE. I HAVE KEPT THE US AMBASSADOR GENERALLY INFORMED, BUT NEITHER HE NOR OTHERS I THINK HAVE BEEN DIRECTLY IN TOUCH WITH JIMINEZ. WE HAVE HOWEVER HAD AN APPROACH FROM A COUNSELLOR AT THE JAPANESE EMBASSY WHO ALTHOUGH PRESUMABLY UNAWARE OF THIS WEEKS DEVELOPMENTS, SAID HE HOPED THE UK WOULD SOON TAKE THE INITIATIVE IN APPROACHING HIS GOVERNMENT TO PARTICIPATE IN A NIGERIAN RESCUE PACKAGE BECAUSE HE WAS SURE THEY WOULD RESPOND POSITIVELY TO US.

HEAD

VVVV

Extract from last 'prudential' meeting. (26/11)

Nigeria

13. Miss Higgins said the Treasury were doing contingency planning on the effects of a Nigerian default, prompted by the recent US rescue package for Mexico.

14. Mr Barnes emphasised the distinction between total repudiation of outstanding debt (which Miss Higgins confirmed was not the issue at present) and a scenario in which Nigeria was not current on interest or principal repayments. In relation to this second scenario the results of an exercise in May had suggested that the only UK bank seriously affected would be Standard Chartered, for whom a Nigerian default, and its consequences in terms of loss of interest and additional provisioning requirements, would seriously erode profits for the year in which the default occurred, without going so far as to force the bank into loss. Since then Standard Chartered's capital base to sustain any losses had increased. The Bank agreed to update these calculations, but it was unlikely that the results would be significantly different.

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10 DOWNING STREET
LONDON SW1A 2AA

From the Private Secretary

27 November 1988

Dear Alex,

NIGERIA: VISIT BY MINISTER OF BUDGET AND PLANNING

Alhaji Abukakar Alhaji (AAA) came in to see me for a drink this evening. I have known him for some time. he brought with him the Governor of the Nigeria Central Bank.

AAA said that he had successfully completed negotiations with the IMF's representative shortly before leaving Lagos. The result of these was to knock a further 2 billion Naira off Nigerian Government spending. He had also secured - and this was very sensitive information - President Babangida's agreement to a reduction of 6 Kobo in the petroleum subsidy. He would be giving the Chancellor the full details in the morning.

AAA went on to say that President Babangida had wanted him to convey four points to the Prime Minister. These were:

- These further cuts represented a major effort by the Nigerian Government and they really could not do more. AAA added that if he had to go back and tell the military government that people were insisting on yet more cuts, he would be dismissed.
- He very much hoped therefore that we would accept the new programme agreed with the IMF representative and take a lead in persuading other Governments to endorse it rapidly.
- He was grateful for the additional help which we were offering (he showed no inclination to ask for more). But he hoped that it could be genuinely quick-disbursing. Our past loans had taken a very long time to disburse and this had hampered Nigeria's efforts to overcome its problems.
- He also hoped that the United Kingdom would take a lead in helping Nigeria reschedule its debt in the Paris Club early in the New Year. Nigeria was very grateful for the help which it had received in the past.

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One or two other minor points arose. We had some discussion on the oil price. AAA said that his present budget calculations were based on a price of \$12. In fact he believed that the average for next year would be closer to \$15 a barrel. He said that an agreement had been reached over Wimpey (I am afraid this means nothing to me). He also confirmed that the Biwater project in Niger State remained a high priority and should go ahead.

I passed on the main points of this note to the Chancellor when I saw him this evening.

I am copying this letter to Lyn Parker in the FCO.

Yours sincerely,
Chris Powell

(C. D. POWELL)

Alex Allan, Esq.,
HM Treasury.



10 DOWNING STREET

LONDON SW1A 2AA

From the Private Secretary

28 November 1988

CH/EXCHEQUER	
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✓ 2/12

The Prime Minister has asked me to thank you for your letter of 15 November about the Niger State water project.

As you know, crucial decisions on future international support for the Nigerian economy are under active discussion. These will, naturally, affect the question of ECGD support for your project.

The Prime Minister fully understands your problem and whilst she cannot anticipate the final decision she has asked that Malcolm Stephens, the Chief Executive of ECGD, should convey it to you as soon as it is reached in the very near future.

(C.D. POWELL)

A.E. White, Esq.



Handwritten initials and date:
 PJP 28/11/88

Treasury Chambers, Parliament Street, SW1P 3AG
 01-270 3000

Lyn Parker Esq
 PS/Secretary of State
 Foreign and Commonwealth Office
 Downing Street
 LONDON
 SW1

PS/Chief Secretary
 PS/Economic Secretary
 Sir P Middleton
 Sir G Littler
 Mr Anson
 Mr Lankester
 Mr Mountfield
 Mr Turnbull
 Mr H P Evans
 Mr Bottrill
 Mr P Davis
 Mrs Thomson
 Mrs Chaplin
 Mr Tyrie
 Mr Call

Mr Cassell - UKDEL
 Mr Enoch - UKDEL

Handwritten signature:
 Lyn Parker

CALL BY NIGERIAN MINISTER OF BUDGET AND PLANNING

Alhaji Abukakar Alhaji (AAA), the Nigerian Minister of Budget and Planning paid a call on the Chancellor this morning. He was accompanied by Alhaji A Ahmed, the Governor of the Nigerian Central Bank, and HE George Dove-Edwin, the Nigerian High Commissioner. Mr Lankester and Mr Mountfield (both Treasury) were also present.

AAA said that, since June 1988, the Nigerian Government had stopped subsidising public sector enterprises except in very exceptional cases. Charges in the public sector had been revised upwards, and imports had been liberalised. The IMF had approved all of these actions. For 1989, the projected fiscal deficit had been reduced to 4 billion naira, compared to a 8.9 billion deficit in 1988. The IMF had made three further demands. First, that the deficit should be reduced further by 2.8 billion naira. Second, that the exchange rate should depreciate. Third, that positive real interest rates should be imposed. Nigeria had agreed to reduce its deficit by 2 billion naira. This comprised 1.5 billion naira of cuts, and 0.5 billion naira of tax increases. Petrol subsidies would be reduced; indirect taxes on beer and soft drinks increased; and direct taxes on company profits increased. The interest rate had just been increased to 13.25 per cent.

The Governor of the Nigerian Central Bank said that the aim was to get rid of the current dual exchange rate system, and replace it with a single rate system. This would be difficult to impose, but steps were being taken.



AAA said that Nigeria sought the UK's assistance both in bridging the gap created by the collapse in the oil price, and in bringing other Paris Club members on board. He noted with gratitude the UK's intention to provide \$100 million of additional aid. It would be highly desirable if the UK could increase this to \$150 million, thus producing a \$300 million overall package. This would "tidy up the position".

The Chancellor said he greatly admired the courage with which AAA had addressed Nigeria's acute problems. He realised that AAA's approach presented immense difficulties, and said it was highly commendable that AAA had grasped the nettle. For its part, the UK was doing its best to help, within the framework of the international financial community. But this must be in response to Nigeria's best efforts. He noted that Nigeria's first programme had not been satisfactory to the IMF. So the first step was for Nigeria to strengthen its own policy. AAA had identified three areas where the IMF had thought Nigeria's original programme inadequate. The further reductions in the fiscal deficit were welcome. As far as the exchange rate was concerned, as soon as a unitary rate was reached, the better. He noted that the Funds view was that a single rate of over 6 naira was the desired objective. (The Governor of the Nigerian Bank commented that this was Nigeria's own aim - he hoped to achieve this by the end of the year.) The Chancellor said that it was essential for a healthy economy that there should be positive real interest rates.

As far as the financing gap was concerned, the Chancellor noted that the UK was taking an exceptional step in proposing this further aid. We were not doing the same for any other country in the world. We were prepared to give additional aid of \$100 million. It was not possible for us to increase this amount. But we would certainly do our best to get the overall package up to \$300 million by seeking to persuade others to put in more.

The Chancellor noted Nigeria's reluctance to draw from the IMF. But it would be very difficult for Nigeria to seek financial help from other countries until it had borrowed from the IMF. After all, Nigeria had already taken the difficult step of accepting IMF terms, and it seemed curious that it should not now draw from the Fund.

AAA agreed that it was apparently contradictory for Nigeria not to borrow from the Fund. But people in Nigeria were "frightfully ignorant" about international finance. They were prepared to accept the austerity programme provided it were seen to be Nigeria's own. They did not mind if the IMF subsequently approved it. But they would perceive any borrowing from the IMF as meaning that the Fund had imposed its own conditions on Nigeria. He agreed that this was irrational. The Chancellor said that much would depend on the President using his authority to persuade the



Nigerian people that borrowing from the IMF was the right course. AAA said that the President was fully on side. But others within Government still had to be persuaded. Mr Lankester suggested that borrowing from the IMF might be linked to a trigger mechanism related to changes in the oil price. AAA said this had already been explored. The political difficulty remained.

Closing, the Chancellor said it was vitally important that AAA stuck to his guns. This year's Budget had been most unfortunate, to put it mildly (AAA nodded). AAA should persuade the Nigerian Government to accept an IMF loan. We would do what we could to encourage other creditors to come up with \$200 million, leading to a total package of \$300 million. This was, of course, in addition to the \$250 million already promised by Japan. But speed was of the essence.

I am copying this to Charles Powell (No.10), and to John Footman (Bank of England).

Yans
Footman

J M G TAYLOR
Private Secretary

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Handwritten signature/initials

cc:
 Chancellor
 EST
 Sir Peter Middleton
 Sir G Littler
 Mr Anson
 Mr Lankester
 Mr Evans
 Mr Turnbull
 Mr Bottrill
 Mr P Davis
 Mr Mountfield
 Mrs Thomson
 Mrs Chaplin
 Mr Call
 Mr Tyrie

Treasury Chambers, Parliament Street, SW1P

The Rt Hon Sir Geoffrey Howe QC MP
 Secretary of State for Foreign Affairs
 Foreign & Commonwealth Office
 King Charles Street
 London
 SW1A 2AH

20th. November 1988

Dear Geoffrey,

NIGERIA

We had a word at Cabinet on Thursday about the proposed British offer of bilateral aid to Nigeria, in the context of its IMF programme. We have already agreed that it would be sensible to make an offer of \$100 million (say roughly £60 million) in Calendar 1989, the bulk of which should fall in our financial year 1989/90. You offered to make £10 million available from within the already-approved Aid Programme towards this. This would leave me to find up to £50 million from the Reserve. I believe you could do more than this. I note that, although there is only £114 million allocated for African Programme Aid in your current Aid Budget (after taking account of the recent PES additions, and of various other changes) you also have £191 million allocated to capital aid in Sub-Saharan Africa. Between these two heads, I am sure that, with some reordering of priorities, you could find room for at least £15 million, and I hope you will feel able to do this.

It seems likely that, if the UK proposal is successful, it will need to be followed up by further assistance on broadly the same scale in subsequent years. You asked in your letter for an assurance that this could be regarded as an agreed PES bid for both years. I am afraid I cannot agree to this. I recognise, of course, that some additional funding will be necessary if a programme of assistance on this to Nigeria on this scale continues. But I must reserve my position on the respective

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shares until we have a chance to see the way this is developing, and can consider the other pressures on your budget, in the course of the PES round next summer.

More generally, I am very pleased to hear that the UK offer has been well received in Lagos, and may have been instrumental in persuading the Nigerians to accept the tougher terms required by the Fund. We must wait and see whether events bear out these initial reports.

*Yours Ever,
John*

JOHN MAJOR

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FM UKDEL IMF/IBRD WASHINGTON
TO DESKBY 010900Z FCO
TELNO 261
OF 302300Z NOVEMBER 88

NIGERIA

1. FOLLOWING TELECONS WITH CASSELL AND LANKESTER, I PUT FOLLOWING POINTS TO QURESHI ABOUT BANK/FUND COLLABORATION IN THE PACKAGE NOW BEING NEGOTIATED:

(A) RELATION BETWEEN SIGNED LOI AND BANK BOARD PRESENTATION OF TIPL: WE WOULD BE OPPOSED TO PRESENTATION IN ADVANCE OF A LOI, AND WOULD WISH FIXING OF A BOARD DATE TO AWAIT THIS.

(B) RELATION BETWEEN BANK DISBURSEMENTS AND FUND BOARD AGREEMENT: THERE SHOULD BE NO DISBURSEMENTS IN OUR VIEW BEFORE THE FUND BOARD HAD AGREED THE PROGRAM.

2. QURESHI STRESSED THE CLOSE COORDINATION BETWEEN BANK AND FUND THAT HAD BEEN OBSERVED THROUGHOUT THIS CASE. HE BELIEVED THAT A FUND AGREEMENT WAS ON THE VERGE OF ACHIEVEMENT. HE WOULD NOT COUNTENANCE THE BANK PROCEEDING IF THE NIGERIANS DEPARTED TO ANY SIGNIFICANT EXTENT FROM THE TERMS OF THE AGREEMENTS REACHED WITH THE FUND AND BANK. BUT HE COULD NOT ACCEPT ANYTHING IN THE NATURE OF FORMAL CROSS-CONDITIONALITY. AAA HAD REQUESTED A BREAKFAST MEETING WITH HIM TODAY MAINLY TO STRESS THIS POINT. HE HAD ARGUED THAT NIGERIA HAD RESPONDED TO THE BANK'S URGING TO REACH AN AGREEMENT ALSO WITH THE FUND, IN SPITE OF CONSIDERABLE POLITICAL COSTS. IT WOULD MAKE HIS POLITICAL TASK FAR MORE DIFFICULT, AND HE WOULD HIMSELF TAKE STRONG EXCEPTION TO THE BANK MAKING ITS DISBURSEMENTS CONDITIONAL ON FUND AGREEMENT. QURESHI HIMSELF BELIEVED THAT FORMAL CROSS-CONDITIONALITY OF THIS SORT WAS INAPPROPRIATE.

3. I SAID THAT MY AUTHORITIES WERE VERY CONCERNED TO AVOID A DIVERGENCE BETWEEN THE INSTITUTIONS IN CASE OF SLIPS BETWEEN CUP AND LIP. QURESHI REPEATED THAT HE WOULD NOT PROCEED UNLESS QUOTE TOTALLY CONVINCED UNQUOTE THAT THE AGREEMENTS WITH THE BANK AND FUND WERE BEING OBSERVED, AND IF THERE WERE QUOTE ANY SUBSTANTIAL OR SIGNIFICANT DEPARTURE, HE WOULD NOT TOLERATE IT UNQUOTE. I ASKED IF BANK DISBURSEMENTS MIGHT NOT ALREADY HAVE TAKEN PLACE IF, SAY, THE DEAL CAME

UNSTUCK IN JANUARY. QURESHI THOUGHT THIS WOULD NOT BE SO.
4. IN CONCLUSION, QURESHI SAID HE WOULD SEE TO IT THAT THE OPERATION WAS NOT BROUGHT TO THE BOARD IN THE ABSENCE OF A SIGNED LOI (HE WAS NOT DEFINITE ABOUT THE MECHANICS). HE STRONGLY URGED US NOT TO SEEK CROSS-CONDITIONALITY ON DISBURSEMENTS. I UNDERTOOK TO REPORT BACK.

5. IN SUBSEQUENT DISCUSSION KOCH-WESER TOLD ME THAT ON THE BASIS OF CONTACTS WITH CAMDESSUS AND ERB AND ASSURANCES THAT THEY WERE CONTENT MANAGEMENT PROPOSE TO CIRCULATE THE TIPL DOCUMENT TOMORROW FOR BOARD DISCUSSION ON 20 DECEMBER. THE FUND MANAGEMENT EXPECTED A LOI TO BE SIGNED NEXT WEEK. IF THE AGREEMENT BROKE DOWN, THE PROJECT WOULD BE WITHDRAWN. KOCH-WESER ADDED THAT QURESHI'S IMPRESSION THAT DISBURSEMENT WOULD NOT TAKE PLACE TILL JANUARY WAS INCORRECT. DOLLARS 100 MILLION WOULD BE PAID OVER IN DECEMBER AND THE REMAINING DOLLARS 150 MILLION OF THE FIRST TRANCHE DRAWN AS REQUIRED OVER THE NEXT FEW MONTHS. BOTH POLITICALLY AND FROM A CASH FLOW POINT OF VIEW A BANK DISBURSEMENT IN DECEMBER WAS ESSENTIAL TO THE NIGERIANS. A DEBT PAYMENT OF DOLLARS 110 MILLION TO IBRD WAS DUE IN DECEMBER.

6. COMMENT: QURESHI'S ASSURANCES ABOUT BANK/FUND COORDINATION MAY BE HELPFUL TO YOU. WE HAD EARLIER ENVISAGED A LOI MIGHT BE SUFFICIENT IN CERTAIN CIRCUMSTANCES FOR THE BANK TO PROCEED. EG PARA 7(B) OF FCO TELNO 139 TO UKDEL ON ARGENTINA. IF YOU INTEND TO PURSUE THIS FURTHER, DIRECT CONTACT WITH QURESHI OR CONABLE WOULD PROBABLY BE NEEDED TO SHIFT THE BANK FURTHER. I WILL TELEPHONE LANKESTER 1 DECEMBER TO DISCUSS FURTHER.

7. FCO PLEASE ADVANCE TO SIR G. LITTLER, LANKESTER (AND COPY FOR CASSELL), MOUNTFIELD, EVANS, WALSH AND BOTTRILL (HMT), CARRICK, FORT AND RICHARDSON (ERD), WARE (BOE), STEPHENS (ECGD), AND AINSCOW, HUDSON AND POWER (ODA).

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YOUR TELNO 679 TO BONN: AID TO NIGERIA

SUMMARY

1. THE DUTCH WILL CONSIDER WHAT THEY CAN DO FOR NIGERIA BUT HAVE BUDGETARY PROBLEMS.

DETAIL

2. WE HAVE SPOKEN TO THE MFA (ROELL, DIRECTOR, AFRICA AND MIDDLE EAST AND TREFFERSS, DIRECTOR, MULTILATERAL AID AND TO THE MINISTRY OF FINANCE.) ROELL SAID THAT HE ACCEPTED THAT THERE WAS A POLITICAL NEED TO TRY TO HELP THE PRESENT NIGERIAN GOVERNMENT AND HOPED THAT HIS GOVERNMENT WOULD BE ABLE TO SUPPORT AN AID PACKAGE BUT TREFFERS WAS MORE CAUTIOUS. HE SAID THAT HE READILY UNDERSTOOD WHY WE WERE APPROACHING THE MINISTRY AND THE VALUE OF AN AID PACKAGE AT THE PRESENT TIME. THERE WAS A PRECEDENT FOR THE NETHERLAND CONTRIBUTING TO AN AID PACKAGE AFTER AN INF MISSION. HE MENTIONED IN PARTICULAR THE SUDAN.

3. TREFFERS TOOK NOTE OF THE CIRCUMSTANCES DESCRIBED IN PARAGRAPH 3-6 OF TUR AND UNDERTOOK TO CONSULT IMMEDIATELY WITH THE MINISTER FOR DEVELOPMENT CO-OPERATION (BUKMAN) BUT SAID THAT HE THOUGHT THAT IT WOULD NOT BE EASY FOR THE DUTCH TO CONTRIBUTE. HIS MINISTER HAD ALREADY DECIDED UPON PRIORITIES FOR BALANCE OF PAYMENT SUPPORT FOR 1989 AND WAS OPERATING WITH A SUBSTANTIALLY REDUCED BUDGET. THE RECIPIENTS HAD ALREADY BEEN PROMISED THAT ASSISTANCE AND SUPPORT FOR NIGERIA COULD ONLY BE AT THE EXPENSE OF SUPPORT FOR OTHER GOVERNMENTS. IT WOULD BE EASY TO GO BACK TO OTHERS TO REDUCE WHAT HAD BEEN COMMITTED.

4. WE HAVE ALSO GONE OVER THE GROUND FULLY WITH THE MINISTRY OF FINANCE WHO ARE ALSO SYMPATHETIC TO ARGUMENTS ABOUT SUPPORTING THE

INF BUT WHO COMMENTED THAT THE FINAL DECISION WOULD BE FOR BUKMAN.

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FRAME DEVELOPMENT

YOUR TELNO 679 TO BONN : AID TO NIGERIA

SUMMARY

1. THE COMMISSION ARE SYMPATHETIC IN THE PLAN TO ASSIST NIGERIA,
BUT HAVE NO SPARE FUNDS.

DETAIL

2. WE HAVE SPOKEN TO LAIDLER (DIRECTOR, WEST AFRICA DIVISION, DG VIII) AS REQUESTED IN TUR TO EXAMINE POSSIBILITY OF EC FUNDS IN SUPPORT OF NIGERIA INITIATIVE. LAIDLER WAS EXTREMELY SYMPATHETIC TO NIGERIA'S CASE, BUT THOUGHT THE COMMISSION HAD NO ROOM FOR MANOEUVRE. OVER THE PAST YEAR THEY HAVE COMMITTED ALMOST ALL FUNDS AVAILABLE TO NIGERIA UNDER LOME III. NIGERIA HAS NOT ASKED FOR ANY OF THIS TO BE IN THE FORM OF SECTORAL IMPORT PROGRAMMES, SO A NUMBER OF PROJECTS HAVE BEEN AGREED, WITH THE AIM OF SUPPORTING THE PRODUCTIVE SECTOR TO HELP WITH ADJUSTMENT. NIGERIA HAS NOT BEEN INCLUDED IN THE SPECIAL PROGRAMME FOR AFRICA. LAIDLER CHECKED WITH THOSE RESPONSIBLE WHO CONFIRM THAT ONLY 1 OR 2 MECU REMAINS UNCOMMITTED IN THE SPECIAL PROGRAMME, AND EVEN THIS IS NOT CERTAIN UNTIL SEVERAL EXISTING COMMITMENTS ARE FINALISED. ADDITIONALLY, THE SITUATION WAS COMPLICATED SINCE AUCLERT (DDG IN DG VIII) HAD VISITED ONLY LAST MONTH AND HAD CONFIRMED WITH THE NIGERIANS THAT THE CURRENT TYPE OF PROGRAMME WAS EXACTLY WHAT THEY WANTED: THE NIGERIANS HAD NEVER MENTIONED THE POSSIBILITY OF ANY FAST DISBURSING AID FROM THE EC.

3. THE ONLY POSSIBILITY LAIDLER COULD IMAGINE WOULD BE TO AGREE WITH THE NIGERIANS TO USE SOME OF THE FUNDS ALREADY COMMITTED FOR PROJECTS, (WHICH SHOULD NOT SPEND IN THE NEAR FUTURE) FOR IMPORT PROGRAMMES: COUNTERPART FUNDS RESULTING FROM THESE PROGRAMMES COULD THEN BE USED TO FINANCE THE PROJECTS AT A LATER DATE. THIS WAS A SCHEME THE COMMISSION WAS TOYING WITH IN SEVERAL COUNTRIES AS A WAY TO MAINTAIN THE FLOW OF FAST DISBURSING AID BETWEEN THE END OF THE SPECIAL PROGRAMME FOR AFRICA AND THE START OF LOME IV. HOWEVER, AT

THIS STAGE IT WAS BY NO MEANS CERTAIN WHETHER THE SCHEME WOULD WORK AT ALL AND NIGERIA HAD CERTAINLY NOT BEEN SEEN AS A GOOD CANDIDATE GIVEN THE UNCERTAINTY ABOUT THE VALUE OF THE NAIRA, WHICH COULD UNDERMINE THE POSSIBILITY OF UNDERTAKING THE PROJECTS AT A LATER DATE TO WHICH THE EC WAS COMMITTED.

4. LAIDLER UNDERTOOK TO REPORT OUR APPROACH TO OTHER RELEVANT PEOPLE IN SENIOR MANAGEMENT. HE DOUBTED THAT A MINISTERIAL MESSAGE COULD ASSIST MUCH, SINCE HE THOUGHT THE REACTION WOULD BE 'AN OPEN DOOR BUT AN EMPTY CUPBOARD': HE WOULD CERTAINLY SEE WHETHER ANY SMALL GESTURE COULD POSSIBLY BE MADE (MAYBE AT MAXIMUM AROUND 10 MECU) BUT WAS NOT AT ALL OPTIMISTIC EVEN ABOUT THIS AT THE CURRENT STAGE IN LOME III AND SPECIAL PROGRAMME EXPENDITURE, WHICH LEFT VERY LITTLE FLEXIBILITY.

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AND TO IMMEDIATE UKDEL IMF/IBRD WASHINGTON, LAGOS
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AND TO PRIORITY STOCKHOLM, THE HAGUE, TOKYO, UKREP BRUSSELS
AND TO PRIORITY KHARTOUM, ABU DHABI, RIYADH

YOUR TELNO 679 TO BONN: NIGERIA: IMF PROGRAMME

SUMMARY

1. THE CANADIANS WILL CONSIDER CAREFULLY WHETHER THEY CAN CONTRIBUTE TO AN INTERNATIONAL AID PACKAGE FOR NIGERIA. CIDA ARE SYMPATHETIC IN PRINCIPLE, BUT SINCE NIGERIA IS NOT ONE OF THE 30 COUNTRIES AT PRESENT QUALIFYING FOR AID MONEY THERE WILL BE DIFFICULTIES.

DETAIL

2. WE SPOKE TO BURGER (DIRECTOR/INTERNATIONAL FINANCE AND DEVELOPMENT DIVISION, FINANCE CANADA), PAYNTER (DIRECTOR-GENERAL/ECONOMIC POLICY BUREAU, DEPARTMENT OF EXTERNAL AFFAIRS) AND BASSETT (VICE-PRESIDENT/ANGLOPHONE AFRICA, CANADIAN INTERNATIONAL DEVELOPMENT AGENCY (CIDA)), DRAWING ON PARAGRAPHS 3 - 6 OF YOUR TUR AND LEAVING WITH THEM A SPEAKING NOTE OF THE MAIN POINTS. THEY ALL PROMISED TO CONSIDER SERIOUSLY AND RAPIDLY THE POSSIBILITY OF PARTICIPATING IN AN INTERNATIONAL AID PACKAGE FOR NIGERIA. THEY ACCEPTED THAT THE WHOLE DEBT STRATEGY WOULD BE IN JEAPORDY IF NIGERIA WERE TO GO INTO DEFAULT, BUT THEY POINTED OUT THAT FOR CANADA IT WOULD BE PARTICULARLY DIFFICULT TO FIND AID FUNDS FOR NIGERIA.

3. BURGER (FINANCE) SAID THAT CANADA HAD NOT HAD A MAJOR RELATIONSHIP WITH NIGERIA OVER THE LAST DECADE. THEY ONLY HAD CANADIAN DOLLARS 4 AND A HALF MILLION EXPORT CREDIT INSURANCE OUTSTANDING. CIDA HAD ALREADY FORGIVEN THE EXISTING OVERSEAS DEVELOPMENT ASSISTANCE REPAYMENT. THEY NO LONGER HAD ANY BILATERAL AID PROGRAMME. HE ALSO ADDED THAT IT LOOKED AS THOUGH THE CREDITORS WERE GOING TO HAVE TO SHOULDER A DISPROPORTIONATE AMOUNT OF NIGERIA'S DEBT WITHOUT NIGERIA HERSELF BEING PREPARED TO DRAW MONEY FROM THE IMF. HE THEREFORE SUPPORTED THE PROPOSAL IN PARA 4 OF YOUR TUR FOR A TRIGGER MECHANISM TO ENABLE THE NIGERIAN AUTHORITIES TO JUSTIFY MAKING A DRAWING.

4. BURGER EXPRESSED FEARS THAT NIGERIA WOULD NOT BE WILLING TO

MAKE A RAPID ENOUGH ADJUSTMENT TO BRIDGE THE FINANCING GAP EVEN WITH A NEW AID PACKAGE. HE DOUBTED WHETHER NIGERIA WOULD BE ELIGIBLE FOR THE ESAF BECAUSE OF THE STRICT CONDITIONALITY REQUIRED, BUT THOUGHT SHE MIGHT BE ABLE TO QUALIFY UNDER STRUCTURAL ADJUSTMENT FUND. HE SAW THE CCFF AS A POSSIBILITY.

5. AT THE END, HOWEVER, BURGER EMPHASISED THAT THEY WOULD LOOK CAREFULLY AT THE PROPOSAL. CIDA CLAIMED TO HAVE NO RESERVES FOR THIS YEAR AND VERY LITTLE FOR THE NEXT TWO YEARS, BUT MAYBE SOMETHING COULD BE FOUND. HE MENTIONED AID TO GUYANA AND WE SAID THAT WE WERE LOBBYING HARD IN SUPPORT OF THE CANADIAN INITIATIVE (YOUR TELNOS 210 AND 211 TO UKDEL IMF).

6. BASSETT (CIDA) WAS IMMEDIATELY SYMPATHETIC TO OUR PROPOSED AID PACKAGE. HE SAID HE WAS FAMILIAR WITH THE PROBLEM AND HAD REALISED THAT SOMETHING WOULD HAVE TO BE DONE VERY RAPIDLY. THE PROBLEM WPBNMYS

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..(-, -ID STRATEGY STIPULATING THAT CANADA WOULD CONCENTRATE ON 30 NAMED COUNTRIES AND NIGERIA WAS NOT ONE OF THEM. THE FUNDS WOULD THEREFORE HAVE TO COME OUT OF THOSE ALLOCATED TO ANOTHER COUNTRY. HE WAS LEAVING FOR SENEGAL AT THE END OF THIS WEEK BUT WAS DUE TO HAVE TALKS WITH THE ODA IN LONDON ON 12 DECEMBER ON HIS WAY BACK TO CANADA. I SUGGESTED THAT HE MIGHT ALSO TOUCH BASE WITH TREASURY OFFICIALS. BASSETT SAID THAT MEANWILE HE WOULD ASK ROSS (DIRECTOR FOR WEST AFRICA) TO LOOK URGENTLY INTO THE POSSIBILITY OF FINDING FUNDS FOR A NIGERIAN AID PACKAGE AND TO REPORT BACK TO US.

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INFO IMMEDIATE LAGOS

YOUR TELNO 679 TO BONN : NIGERIA AND THE IMF

FROM UK EXECUTIVE DIRECTOR AFRICAN DEVELOPMENT BANK

SUMMARY

1. AFDB NET DISBURSEMENTS TO NIGERIA IN 1989 MIGHT REACH USD 253 M, WITH SLIGHTLY LESS IN 1990. BUT SUCH IS AFDB'S EXPERIENCE WITH NIGERIA THAT IT COULD BE VERY MUCH LESS. PAST DIFFICULTIES OVER CONDITIONALITY HAVE LED THE AFDB TO OPT IN FUTURE FOR PROJECT LENDING TO NIGERIA, DESPITE PRESSURE FROM THE IBRD. HOW MUCH AFDB MONEY AT 7.46 PER CENT DOES NIGERIA REALLY NEED ?

DETAIL

2. DISBURSEMENT IN 1989 WILL BE MAINLY FROM EXISTING LOANS. FOLLOWING INFORMATION AMENDS DATA SENT VIA CARTER, IFID, ODA, AND TAKES ACCOUNT OF SENIOR MANAGEMENT'S CONCERN TO INCREASE PACE OF DISBURSEMENT TO NIGERIA. THIS PRINCIPALLY INCLUDES THE WILLINGNESS OF THE BANK TO GIVE IN ON THE CONDITIONALITY FOR THE USD 232 M EXPORT STIMULATION LOAN APPROVED IN MID-1987 BUT NOT YET SIGNED. AFDB HAD BEEN INSISTING ON THE FUNDS BEING AVAILABLE TO ALL SIZES OF COMPANIES, WHILST NIGERIANS HAD WANTED TO RESTRICT IT TO SMALL AND MEDIUM-SIZED FIRMS. THERE WERE OTHER PROBLEMS TOO, ALL OF WHICH HAVE BEEN EXAGGERATED IN THE HEAT OF DEBATE.

3. EXPORT STIMULATION LOAN AGREEMENT IS EXPECTED SOON AND SOME USD 155 M MIGHT DISBURSE IN 1989. OTHER DISBURSEMENTS FROM EXISTING LOANS IN 1989 ARE FORECAST AS :

IBADAN WATER	USD 14 M
FORESTRY	USD 13 M
INDUSTRIAL CREDITS	USD 10 M
AGRIC CREDITS	USD 41 M
BAUCI WATER	USD 12 M

IN ADDITION, USD 26 M OF A USD 77 M INDUSTRIAL CREDIT LOAN TO

BE APPROVED IN 1989 COULD DISBURSE IN THAT YEAR. ALL OTHER LOANS FOR 1989 APPROVAL ARE UNLIKELY TO START TO DISBURSE. THIS GIVES FORECAST TOTAL OF USD 271 M, MINUS REPAYMENTS OF USD 18 M : NET USD 253 M.

4. FOR 1990, FIGURES IN RELATION TO EXISTING LOANS ARE :

EXPORT STIMULATION	USD 77 M
IBADAN WATER	USD 3 M
FORESTRY	USD 15 M
INDUSTRIAL CREDITS	USD 11 M
BAUCI WATER SUPPLY	USD 31 M
TOTAL	USD 137 M

PLUS PIPELINE PROJECTS :

INDUSTRIAL CREDITS	USD 51 M
ANAMBRA UTILITIES	USD 60 M
MIDDLE RIMA IRRIG	USD 25 M
TOTAL	USD 136 M

MINUS REPAYMENTS OF USD 30 M GIVES NET USD 243 M. MY OWN VIEW IS HOWEVER THAT THESE FIGURES ARE OPTIMISTIC AND THAT THE LAST TWO OF PIPELINE PROJECTS MIGHT MOVE VERY MUCH MORE SLOWLY.

5. BECAUSE OF DIFFICULTIES IN IMPLEMENTING THE 1987 EXPORT STIMULATION LOAN, BANK MANAGEMENT ARE RELUCTANT TO PROVIDE FURTHER POLICY-BASED LOANS TO NIGERIA. THEY ARGUE THAT THEY HAVE NO CLOUT WITH COUNTRIES SUCH AS NIGERIA, ZAIRE AND COTE D'IVOIRE (RECENT EXPERIENCE CERTAINLY BEARS THAT OUT). EVEN WHEN THEY CO-FINANCE WITH IBRD THEY END UP BEING PUSHED INTO BREACHING CONDITIONALITY. THEY CLAIM THEREFORE THAT THEY HAVE AGREED WITH THE NIGERIAN AUTHORITIES THAT AFDB SHOULD CONCENTRATE ON PROJECT LENDING IN NIGERIA. THEY HAVE THUS SUSPENDED THEIR PREVIOUS POLICY INTENTION OF PROVIDING BUA 500 M (USD 645) OVER THREE YEARS (EXPORT STIMULATION LOAN WAS TO BE FIRST TRANCHE OF THAT).

6. AGAINST THAT BACKGROUND AFDB WOULD BE UNLIKELY TO PROVIDE MORE PBL TO NIGERIA, EVEN IF THE PIPELINE WAS NOT ALREADY TOO HEAVY FOR PBL TO AFRICA GENERALLY. THERE SEEMS TO BE NO REAL PROSPECT OF GETTING OTHER COUNTRIES TO MOVE DOWN THE QUEUE.

7. ABOVE INFORMATION IS BASED ON DISCUSSIONS WITH THE VICE PRESIDENT AND PROGRAMME DIRECTOR. PRESIDENT IS AWAY UNTIL 6 DEC. I WOULD PREFER TO AWAIT HIS RETURN BEFORE PRESSING NIGERIA'S CASE, SINCE ANY CHANGE OF STANCE WILL ONLY COME AT THAT LEVEL.

8. FINALLY, I WAS SURPRISED THAT YOU DID NOT RAISE THE QUESTION OF TERMS OF AFDB LENDING TO NIGERIA. IN PRACTICE THEY COULD HAVE AS MUCH AFDB MONEY AS THEY WANT, BUT AT A RATE OF INTEREST OF 7.46 PER CENT HOW MUCH CAN THEY AFFORD ? NO AFDB MONEY IS ALLOCATED TO NIGERIA. SHOULD NOT WE AND NIGERIA BE PRESSING FOR SOME ?

SUTHERLAND

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TELNO 262
OF 010100Z DECEMBER 88
AND TO IMMEDIATE ABIDJAN, BONN, COPENHAGEN, OSLO
AND TO IMMEDIATE OTTAWA, PARIS, ROME, STOCKHOLM
AND TO IMMEDIATE THE HAGUE, TOKYO, UKREP BRUSSELS
AND TO IMMEDIATE KHARTOUM, ABU DHABI, RIYADH, LAGOS

Handwritten notes in red ink:
Relentless
← from father
OBS spec.

ABIDJAN FOR SUTHERLAND (AFDB)

IMF: NIGERIA

SUMMARY

1. AGREEMENT REACHED BETWEEN FUND AND NIGERIA ON 15-MONTH STAND-BY ARRANGEMENT. FUND PAPER TO BE ISSUED SHORTLY. BOARD DISCUSSION EXPECTED BEFORE END-JANUARY. MAJOR PROBLEM REMAINS THE NEED TO SECURE NECESSARY FINANCING. BOARD GIVEN SUMMARY DETAILS OF THE FINANCING GAP.

DETAIL

2. ERB (DEPUTY MANAGING DIRECTOR) ANNOUNCED AT THIS AFTERNOON'S BOARD MEETING THAT THE MANAGING DIRECTOR HAD REACHED AGREEMENT WITH THE NIGERIAN MINISTER OF FINANCE ON A 15-MONTH FUND STAND-BY ARRANGEMENT. ERB SAID THAT A FUND DOCUMENT WOULD BE ISSUED SHORTLY FOR DISCUSSION BEFORE THE END OF JANUARY. ERB TOLD DIRECTORS THAT THE MAIN OUTSTANDING PROBLEM WAS THE NEED TO SECURE THE NECESSARY FINANCING TO ENSURE PROGRAM VIABILITY.

3. JIMENEZ (FUND MISSION CHIEF) THEN GAVE A FAIRLY FACTUAL BACKGROUND STATEMENT (COMMENT: POSSIBLY IN RESPONSE TO OUR REQUEST FOR THE FUND TO PROVIDE G10 AND ARAB DIRECTORS WITH SOME QUANTIFICATION, FOLLOWING TELCON MOUNTFIELD/HEYWOOD AND YOUR TELNO 212).

4. HE STARTED BY SUMMARISING DEVELOPMENTS IN THE NIGERIAN ECONOMY OVER THE PERIOD SINCE 1982: THE COLLAPSE IN OIL EXPORTS, THE RISING DEBT SERVICE BURDEN, AND FALTERING POLICY ADJUSTMENT EFFORTS, CULMINATING IN RAPIDLY MOUNTING DOMESTIC IMBALANCES.

RECENT DEVELOPMENTS

5. OVER RECENT MONTHS THE NIGERIAN AUTHORITIES HAD TAKEN A NUMBER OF IMPORTANT MEASURES IN AN ATTEMPT TO REVERSE THE DETERIORATING ECONOMIC POSITION. THE PROGRAM WHICH HAD NOW BEEN AGREED WAS DESIGNED TO STRENGTHEN THESE EFFORTS AND TO BRING ABOUT A MAJOR REDUCTION IN DOMESTIC IMBALANCES. TO

ILLUSTRATE THE RECENT PROGRESS MADE BY THE AUTHORITIES, JIMENEZ MADE THE FOLLOWING POINTS:

- (I) THE FEDERAL GOVERNMENT'S CASH DEFICIT WAS NOW EXPECTED TO BE ONLY 12 PER CENT OF GDP IN 1988, AGAINST A BUDGETTED LEVEL OF 16 PER CENT OF GDP,
- (II) DOMESTIC FINANCING OF THIS DEFICIT WAS LIKELY TO BE LESS THAN 8 PER CENT OF GDP AGAINST INITIAL EXPECTATIONS OF 14 PER CENT OF GDP,
- (III) AS A RESULT, BOTH CREDIT GROWTH AND MONEY SUPPLY GROWTH WOULD BE LOWER THAN ORIGINALLY ENVISAGED.

1989 PROGRAM

6. REVERTING TO THE PROPOSED 1989 PROGRAM, JIMENEZ HIGHLIGHTED SEVERAL FEATURES:

- (I) THE FISCAL DEFICIT FOR 1989 WAS TARGETTED AT 8.4 PER CENT OF GDP,
- (II) DOMESTIC FINANCING OF THE DEFICIT IN 1989 WOULD BE REDUCED TO 1.3 PER CENT OF GDP,
- (III) NET DOMESTIC CREDIT WAS PROGRAMMED TO RISE BY SLIGHTLY OVER 9 PER CENT IN 1989 (AGAINST A GROWTH OF 27 PER CENT EXPECTED IN 1988),
- (IV) BROAD MONEY GROWTH WAS TARGETTED TO BE JUST UNDER 11 PER CENT IN 1989 (AGAINST 33 PER CENT IN 1988).

7. JIMENEZ SAID THAT THE PROGRAM WOULD SUPPORT THE NIGERIAN AUTHORITIES' FOREIGN EXCHANGE POLICY AND HELP BRING ABOUT A FALL IN INFLATION. REGARDING EXCHANGE RATE POLICY, JIMENEZ REPORTED THAT THE INTERBANK EXCHANGE RATE HAD BEEN LIBERALISED DURING THE PREVIOUS WEEK, AND THE AUCTION RATE HAD BEEN ALLOWED TO RISE. HE SAID THAT UNDER THE PROGRAM THE AUTHORITIES WOULD UNIFY THESE EXCHANGE RATES AND MANAGE THE SINGLE RATE THROUGH THE INTERBANK MARKET.

FINANCING GAP

8. JIMENEZ SAID THAT THE STAFF'S CENTRAL SCENARIO ASSUMED AN AVERAGE OIL PRICE FOR 1989 OF DOLLARS 14.50. IT WAS ALSO ASSUMED THAT NIGERIA'S OPEC QUOTA WOULD BE MAINTAINED AND THAT IMPORTS WOULD BE SHARPLY COMPRESSED. ON THIS BASIS, THE STAFF WERE PROJECTING A FINANCING GAP OF DOLLARS 9.8 BILLION FOR 1989.

9. REVIEWING THE PROSPECTS FOR FILLING THIS GAP, JIMENEZ SAID THAT:

- (I) AN AGREEMENT WAS DUE TO BE SIGNED WITH THE LONDON CLUB IN JANUARY. ALTHOUGH THIS WOULD PROVIDE NO NEW MONEY, IT DID GRANT SUBSTANTIAL RELIEF ON NEW MATURITIES, IT WOULD STRETCH OUT PAYMENTS OVER 20 YEARS, AND REDUCED THE INTEREST RATE MARGIN OVER LIBOR. IN TOTAL THIS AGREEMENT WOULD PROVIDE DEBT

RELIEF OF DOLLARS 2.9 BILLION IN 1989.

- (II) PRELIMINARY DISCUSSIONS HAD BEGUN WITH THE PARIS CLUB. THE AUTHORITIES HAD REQUESTED THAT ALL 1989 MATURITIES TOGETHER WITH ARREARS (INCLUDING PREVIOUSLY RESCHEDULED DEBT) BE RESCHEDULED. IF THIS WERE AGREED, IT WOULD PROVIDE DEBT RELIEF OF DOLLARS 4.5 BILLION IN 1989.
- (III). IF NON-PARIS CLUB OFFICIAL CREDITORS WERE ALSO PREPARED TO RESCHEDULE ON SIMILAR TERMS, THE TOTAL DEBT RELIEF RESULTING FROM RESCHEDULING IN 1989 COULD AMOUNT TO DOLLARS 8.6 BILLION.
- (IV) FINALLY, VARIOUS PROGRAM LOANS WERE UNDER NEGOTIATION WITH, FOR EXAMPLE, THE WORLD BANK AND CERTAIN COFINANCIERS, INCLUDING JAPAN.

10. BRINGING ALL THESE POSSIBLE SOURCES TOGETHER STILL, HOWEVER, LEFT A RESIDUAL GAP OF DOLLARS 300 MILLION. JIMENEZ SAID THAT THE UK HAD EXPRESSED A WILLINGNESS TO PROVIDE DOLLARS 100 MILLION AND HAD AGREED TO USE BEST EFFORTS TO SEEK CONTRIBUTIONS FROM OTHER DONORS. THE FUND WAS THEREFORE CONFIDENT THAT THE FINANCING GAP COULD BE CLOSED.

11. FINALLY, JIMENEZ REPEATED THAT THE ESTIMATED RESIDUAL FINANCING GAP OF DOLLARS 300 MILLION WAS BASED ON THE ASSUMPTION OF A DOLLARS 14.50 OIL PRICE. THE NIGERIANS HAD INDICATED AGREEMENT TO CERTAIN 'CONTINGENCY MECHANISMS', INCLUDING FURTHER FISCAL RETRENCHMENT, IN THE EVENT THAT THE OIL PRICE TURNED OUT TO BE LOWER THAN ANTICIPATED. JIMENEZ SAID THAT THE NIGERIANS HAD NOT (REPEAT NOT) AGREED TO DRAW FUND MONEY.

12. THE BOARD SIMPLY TOOK NOTE OF JIMENEZ' STATEMENT. NO QUESTIONS WERE RAISED.

13. FCO PLEASE ADVANCE TO SIR G. LITTLER, LANKESTER (AND COPY FOR CASSELL), MOUNTFIELD, EVANS, WALSH AND BOTTRILL (TREASURY), CARRICK, FORT AND RICHARDSON (FCO), WARE (BANK OF ENGLAND), STEPHENS (ECGD), AND AINSCOW, HUDSON AND POWER (ODA).

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MR WICKS NO 10 DOWNING ST

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PUP

FROM: T P LANKESTER

DATE: 1 December 1988

CHANCELLOR OF THE EXCHEQUER

cc Chief Secretary
Economic Secretary
Sir P Middleton
Sir T Burns
Sir G Littler
Mr Mountfield
Mr Evans
Mr Bottrill
Mr Walsh
Mr P Davis
Mrs Thomson
Mr Tarkowski
Mr Savage
Mrs Chaplin
Mr Tyrie
Mr Call

INTERNATIONAL ISSUES: NIGERIA

This is a progress report for your meeting on Friday.

2. The Managing Director has reached an agreement with Nigeria on a programme. It is on the lines that AAA outlined to you on Monday.
3. There has been a further 2 per cent of GDP fiscal adjustment, which is what we were looking for. This amounts to Naira £2.8 billion, rather more than the Naira £2 billion that AAA mentioned to you.
4. There is no explicit assurance about moving to positive real interest rates. But the IMF Mission Chief tells us that the banks are already charging between 19 and 23 per cent to borrowers, and Governor Ahmed has told the Fund that these rates are very likely to go higher as banks ration credit within the tightly constrained credit ceilings. (The Nigerians, as AAA told you, have just put up their minimum lending rate to 13½ per cent; but this - plus a 1 per cent margin - is the rate at which the government borrows, not the rate at which the banks lend.) The Fund are programming

an inflation rate of 22 per cent for 1989 over 1988; if achieved, the Nigerians should be in the right ball park for achieving positive real rates at least on the lending side.

5. The exchange rate systems will be unified shortly, leading almost certainly - as the Governor told you - to a Naira rate in excess of 6 to the dollar.

6. In terms of policy measures, therefore, the Nigerians have just about met our requirements - though we would have preferred something a bit more specific on interest rates.

7. The Nigerians are not prepared to commit themselves to a Fund drawing at this stage. All that they have been prepared to agree is that understandings would be reached on a drawing at the time of the first review (in March) in the event of the financing of the programme - including the price of oil - turning out less favourable than assumed. This is better than nothing, though not as good as we would have wished. However, we think this is as far the Nigerians can be pushed and that we will have to accept it. But we will need to watch this very carefully at the time of the review.

8. Fund management will not put this programme to their board until they have a clearer assurance that the residual funding gap of \$300 million is going to be covered by the bilateral donors (see below).

World Bank

9. We have an assurance from the Bank that their \$500 million trade policy loan will not be put to their Board till a letter of intent has been signed. Subject to this, the Bank board will consider this loan on 20 December with a first disbursement of \$100 million immediately thereafter. The Fund board will not consider the programme until after some time in late January. But once the letter of intent is signed (as we expect it to be next week), the programme is effectively agreed and therefore we think it acceptable for the Bank to proceed on this basis. (The

position is completely different from Argentina where the Bank wanted to go ahead - and indeed did so - without a letter of intent even in sight).

Bilateral aid

10. We have put our offer on the table, and FCO are now mounting an intensive lobbying operation in support. The Prime Minister will join this at the Rhodes Council; Mr Patten will do his part at the DAC High Level meeting this weekend; we shall ask you to do the same at ECOFIN in 10 days time. Preliminary indications are that US, FRG and France all see the need for at least a token effort, but that the contributions may not be large. Japan, on the other hand, is expected to put in at least another \$100 million, on top of the \$250 million already assumed in the IMF calculations. Canada has raised the question of possible over-funding; we are discussing with ODA whether any part of our offer can be made conditional on the oil price remaining low. But this is a point on which we would like the World Bank to take the lead, at the Donor Group they are convening in London in January.

11. Meanwhile, the Chief Secretary is on the point of agreeing with Mr Patten on the financing of the UK contribution: probably £15 million out of the existing Aid programme, and about £40 million from the Reserve in 1989-90, with similar shares in later years.

Paris Club

12. The IMF arithmetic also assumes a major Paris Club contribution, involving rescheduling 100 per cent of all principle and interest falling due in 1989, and all arrears accruing in 1988, including those under previous rescheduling agreements. This is the maximum "conventional" treatment the Paris Club can give. We have discussed this informally with the Deputy Chairman, when he was in London last Monday. He thinks it will be possible to get general agreement on this, provided the US does not block it. Preliminary soundings of the US since then suggest they will be sympathetic.

13. However, the IMF would like to go further, and consider Toronto terms. We think this would be premature. It will not actually bring any relief in 1989 (since 100 per cent of all interest falling due that year will be rescheduled anyway). It will begin to bite from 1990 onwards. But our guess is that the other creditors will be very reluctant to commit themselves now to Toronto terms in 1990 and beyond - particularly if there is any prospect of the oil price increasing above \$14.50. And it might even be counter-productive to seek such an undertaking in advance. We have put these points to the Deputy Managing Director, and asked him to discuss them with the Chairman of the Paris Club. Subject to your views, we do not propose to lobby actively for Toronto terms at this stage. As you know, they would be particularly expensive for the UK: maybe £60 million in a full year, once the full effect began to work through in the early 1990s.

Prime Ministerial Message

14. FCO want the Prime Minister to send a congratulatory message to President Babangida. We have asked them to hold this up until you have decided whether to press the Nigerians for them to take a Fund drawing. I think the Prime Minister should tell Babangida that Nigeria ought to draw if necessary (ie if the financing assumptions turn out to be too optimistic).

Publicity and Parliament

15. The Press are beginning to get wind of the deal. We need to consider whether anything should be said to Parliament. We have discussed this with ODA. Our preliminary view is that Mr Patten should answer an arranged PQ early next week, announcing that the UK is prepared to put in \$100 million in 1989, and explaining why this exceptional action is being taken. We are clearing a draft with ODA and FCO, and will submit it for approval later.

Since Tim
wrote this
note, Alex
has asked him
to consider what
might be
said in
Beth's speech

↑
This is dead but
you should announce
@ Bowen Wells

A Robertson

MP T P LANKESTER

CONFIDENTIAL

CC - CXI EST



Sr PMIDDLETON, BIRG-LITTON
 Mr ANDREW, Mr SCHOLAR,
 Mr LANCASTER, Mr TURNBULL
 Mrs LONAX, Mr MOUNTFIELD
 Mr HEWSON, Mr P DAVIS
 Mrs THOMSON
 Mr T JAMES, Mr TERRY

Treasury Chambers, Parliament Street, SW1P 3AG

Jeremy Godfrey Esq MP
 Private Secretary to the
 Secretary of State for Trade and Industry
 1 - 19 Victoria Street
 London
 SW1

1 December 1988

Dear Jeremy,

NIGERIA : BIWATERS

The Chief Secretary has seen your letter of 23 November in which you recommend that notwithstanding the serious doubts which remain about Nigeria's recovery, we should extend cover for the Biwater project. The Chief Secretary has also seen Lyn Parker's letter of 25 November which suggests that we should check with the Nigerians the priority which they apply to this project. Charles Powell's letter of 27 November confirms that the Biwater project remains a high priority and that the Nigerians consider that it should go ahead.

In view of our political commitment to Nigeria, the Chief Secretary is reluctantly prepared to agree that ECGD cover of about £34.3 million should be offered to Biwater for the completion of the scheme. This is clearly not justified solely on economic grounds; it is much too early to extend further credit to Nigeria. The condition laid down by the Prime Minister in January was that the Nigerians should be current on arrears. At that time they were. But this was not subsequently sustained. The Nigerians were some £33 million in arrears at the end of June and a further payment of some £70 million is due at the end of January 1989. But as the Nigerians have just reached an agreement with the IMF (UKDEL Tel no 267) which the Managing Director believes is sufficient for them to establish a Stand-by Agreement, the Chief Secretary agrees to ECGD cover, even though the normal requirement for a bilateral rescheduling agreement and evidence of acceptable performance under the IMF programme is not yet available. This concession is limited to the cover to be made available to Biwater for the completion of the water scheme. Any further ECGD cover will have to be considered against the normal criteria; I understand that ECGD themselves are very reluctant to contemplate any further credit after Biwater, and we do not expect Nigeria to press hard on this point.

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I should also point out that there is some industrial, commercial doubt about this scheme. The World Bank has told the Overseas Development Administration confidentially that the project is poor with incorrect technology and that it has maintenance requirements which are unlikely to be met by the State authorities concerned. It is not a project ECGD or Treasury would wish to pursue, but for the degree of commitment given before we knew of the World Bank attitude.

We do however need to ensure that ECGD does not enter into an unqualified commitment to guarantee the whole of the loan for this project. I understand that ECGD intend to monitor both the drawdown of the loan and progress towards a bilateral rescheduling agreement. Any reluctance on the part of the Nigerians to conclude negotiations on the bilateral will, as is normal, entitle ECGD to call a default under the Loan Agreement. In that event ECGD would be able to cut-off further drawdown in relation to future work under the agreement. The Chief Secretary considers that this is the minimum condition that we should impose to contain ECGD's additional exposure. It would be appropriate for both Biwater and the Nigerians to be aware that a condition applies in this case where we have agreed exceptionally for cover to be made available.

I am copying this letter to Charles Powell (No.10) and Lyn Parker (FCO)

Yours,

Peter Wanless.

PETER WANLESS
Assistant Private Secretary

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FM BONN

TO IMMEDIATE FCO

TELNO 1229

OF 021342Z DECEMBER 88

INFO PRIORITY UKDEL IMF/IBRD WASHINGTON, LAGOS

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INFO ROUTINE TOKYO, UKREP BRUSSELS, OSLO, OTTAWA, ABIDJAN

INFO ROUTINE KHARTOUM, ABU DHABI, RIYADH

YOUR TELNO 679: NIGERIA: IMF PROGRAMME

SUMMARY

1. THE GERMANS ARE CAUTIOUS BUT WILL CONSIDER CAREFULLY WHETHER THEY CAN HELP NIGERIA. CHANCELLOR KOHL HAS BEEN BRIEFED IN CASE THE SUBJECT IS RAISED WITH HIM AT RHODES.

DETAIL

2. ACTION TAKEN WITH LINHART (HEAD OF AFRICA DIRECTORATE IN THE FEDERAL AID MINISTRY), BEHRENS (HEAD OF DEPARTMENT RESPONSIBLE FOR AFRICA IN THE SAME MINISTRY), PIESKE (AUS-EQUIVALENT, FEDERAL FINANCE MINISTRY), SCHOENFELDER (HEAD OF DEPARTMENT RESPONSIBLE FOR THE IMF IN THE FEDERAL FOREIGN MINISTRY) AND KORFF (HEAD OF THE GERMAN DELEGATION TO THE PARIS CLUB, FEDERAL ECONOMICS MINISTRY), DRAWING ON PARAGRAPHS 3-7 OF YOUR TUR AND LEAVING THEM WITH THE SPEAKING NOTE OF THE MAIN POINTS. THEY ALL PROMISED TO CONSIDER CAREFULLY THE POSSIBILITY OF PARTICIPATING IN AN INTERNATIONAL AID PACKAGE FOR NIGERIA BUT WERE CAUTIOUS AND NON-COMMITTAL AS TO THE OUTCOME.

3. LINHART WAS PREPARED AT FIRST TO GO NO FURTHER THAN TAKING NOTE OF OUR REPRESENTATIONS AND UNDERTAKING THAT THEY WOULD BE DISCUSSED WITHIN THE MINISTRY. WHEN PRESSED, HOWEVER, HE WAS PREPARED TO CONCEDE THAT A GERMAN CONTRIBUTION FROM HIS MINISTRY'S 1989 BUDGET WAS NOT RULED OUT ENTIRELY, BUT WOULD HAVE TO BE VERY CONSIDERABLY SMALLER THEN THE PROPOSED BRITISH ONE. EVEN THAT WOULD HAVE TO BE CONSIDERED IN COMPETITION WITH MORE URGENT CALLS ON THE MINISTRY'S BUDGET: THE POOREST COUNTRIES AND SUBSTANTIAL TRADE/AID COMMITMENTS SUCH AS THE SHANGHAI SUBWAY SYSTEM. BEHRENS POINTED OUT THAT NIGERIA WAS A RESOURCE-RICH COUNTRY. HE ACCEPTED OUR ARGUMENT THAT A COUNTRY WHICH NOW INTENDED TO ABANDON UNWISE POLICIES AND ACCEPT IMF PRINCIPLES SHOULD BE ENCOURAGED, BUT HITHERTO ANY NEW SOURCE OF INCOME - OIL OR GAS DISCOVERIES FOR EXAMPLE - HAD BEEN IMMEDIATELY

DIVERTED INTO THE POCKETS OF THE ARMY AND BUREAUCRACY, RATHER THAN BEING PUT TOWARDS SENSIBLE ECONOMIC DEVELOPMENT, WHICH HARDLY INSPIRED CONFIDENCE IN THE NIGERIANS' WILLINGNESS TO CHANGE. IT WAS THEREFORE DIFFICULT TO ARGUE FOR MORE MONEY FOR NIGERIA FROM A LIMITED BUDGET. HE ACCEPTED THE POINT THAT OUR OWN CONTRIBUTION WAS DEPENDENT ON A SATISFACTORY AGREEMENT BETWEEN NIGERIA AND THE IMF, WHICH IF ACHIEVED OUGHT TO PROVIDE THE NECESSARY CONFIDENCE.

4. PIESKE WAS ALSO CAUTIOUS AND MADE SIMILAR POINTS TO LINHART ABOUT THE FRG'S LIMITED AID RESOURCES BEING CHANNELLED TO THE POOREST COUNTRIES. THE FRG HAD ALREADY REACHED A RE-SCHEDULING AGREEMENT WITH NIGERIA AND HAD RE-INTRODUCED HERMES (ECGD-EQUIVALENT) COVER UP TO DM 300 MILLION, WHICH IN HIS VIEW SUGGESTED THAT THEY HAD ALREADY DONE A LOT FOR NIGERIA. LAST TIME THE NIGERIANS HAD APPARENTLY REACHED AGREEMENT WITH THE IMF THEY HAD NOT IN FACT MADE ANY DRAWINGS AND THE SHORT-FALL HAD BEEN COVERED BY THE PARIS CLUB. WAS THIS NOT LIKELY TO HAPPEN AGAIN? WE DREW ATTENTION TO THE OIL PRICE TRIGGER PROPOSAL BUT PIESKE WAS SCEPTICAL GIVEN THE NEW UPWARD TREND IN THE OIL MARKET FOLLOWING THE OPEC AGREEMENT. HE CONCLUDED BY ASKING HOW WE INTENDED TO PUT TOGETHER A PACKAGE IF OUR CONDITIONS COULD IN FACT BE MET.

5. SCHOENFELDER SAID THAT THE LETTER OF INTENT NOW AGREED BY THE FUND WITH THE NIGERIAN FINANCE MINISTER ON A 15 MONTH STANDBY ARRANGEMENT WAS AN IMPORTANT STEP IN THE RIGHT DIRECTION. THERE WERE STRONG POLITICAL ARGUMENTS FOR HELPING NIGERIA: THE IMPORTANCE OF THE BILATERAL RELATIONSHIP (NIGERIA HAD BEEN ONE OF THE LARGEST RECIPIENTS OF GERMAN DEVELOPMENT AID PRIOR TO 1982), THE SIZE OF GERMAN INVESTMENT IN NIGERIA AND THE FACT THAT THE FRG WAS THE SECOND LARGEST CREDITOR AFTER THE UK. THE FOREIGN MINISTRY WOULD ENSURE THAT THESE POLITICAL CONSIDERATIONS WERE TAKEN FULLY INTO ACCOUNT IN CONSIDERING THE FEDERAL GOVERNMENT'S RESPONSE TO THE UK INITIATIVE. BUT THE FIRST STEP WAS FOR THE FEDERAL AID AND FINANCE MINISTRIES TO PREPARE A TECHNICAL ANALYSIS. IT WAS TOO SOON TO VENTURE EVEN A PRELIMINARY VIEW ON WHETHER THE FRG WOULD BE ABLE TO HELP. HOWEVER, CHANCELLOR KOHL HAD BEEN BRIEFED TO SAY THAT THE MATTER WAS UNDER ACTIVE CONSIDERATION IN CASE THE PRIME MINISTER RAISED IT WITH HIM AT RHODES.

6. KORFF, WHO HAD ALREADY SPOKEN TO MOUNTFIELD, WAS ALSO ALERT TO THE WIDER POLITICAL AND ECONOMIC ARGUMENTS FOR HELPING NIGERIA. LIKE PIESKE, HOWEVER, KORFF WAS PARTICULARLY CONCERNED ABOUT THE NIGERIANS' REFUSAL TO DRAW MONEY FROM THE IMF FOLLOWING THE PUBLIC CONSULTATION EXERCISE IN 1986. THIS MEANT THAT BILATERAL CREDITORS

HAD TO MAKE UP THE FINANCING GAP WHEN MONEY WOULD HAVE BEEN AVAILABLE FROM THE IMF. HE HOPED THAT THE BRITISH GOVERNMENT COULD PERSUADE THE NIGERIANS THAT THIS ATTITUDE WAS TOTALLY UNREASONABLE GIVEN THEIR PRESENT FINANCIAL CIRCUMSTANCES.

COMMENT

7. IN VIEW OF THIS GENERALLY CAUTIOUS REACTION FROM GERMAN OFFICIALS, WE SEE ADVANTAGE IN MAKING A POLITICAL APPEAL TO CHANCELLOR KOHL AT RHODES. YOU MAY ALREADY HAVE BRIEFED THE PRIME MINISTER TO DO SO. WE SEE NO NEED FOR A MINISTERIAL MESSAGE AT THE PRESENT TIME BUT THIS POSSIBILITY MIGHT NEED TO BE REVIEWED IN THE LIGHT OF ANY DISCUSSIONS AT RHODES.

MALLABY

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TELNO 690

OF 020955Z DECEMBER 88

INFO IMMEDIATE UKDEL IMF IBRD WASHINGTON

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INFO PRIORITY ABIDJAN, BONN, COPENHAGEN, OSLO, OTTAWA, PARIS

INFO PRIORITY STOCKHOLM, THE HAGUE, TOKYO, UKREP BRUSSELS

INFO PRIORITY KHARTOUM, ABU DHABI, RIYADH, LAGOS

YOUR TELNO 679 TO BONN: NIGERIA/IMF: ITALIAN REACTIONS

SUMMARY

1. ITALIAN OFFICIALS RECOGNISE THE SCALE OF THE PROBLEM BUT SEE LITTLE PROSPECT OF ITALIAN PARTICIPATION IN A QUICK DISBURSING FINANCIAL PACKAGE FOR NIGERIA.

DETAIL

2. I CALLED ON 30 NOVEMBER ON SARCINELLI (DIRECTOR-GENERAL TREASURY) AND ON 1 DECEMBER ON GALLI (DIRECTOR-GENERAL FOR DEVELOPMENT) AND LEFT A SPEAKING NOTE BASED ON TUR. I ALSO GAVE A COPY TO SALLEO (ECONOMIC DIRECTOR) AND HEAD OF CHANCERY CALLED ON 1 DECEMBER ON SELVAGGI (HEAD OF AFRICA ECONOMIC DIVISION). THEIR REACTIONS WERE ALL SLIGHTLY DIFFERENT BUT THE CENTRAL MESSAGE WAS THAT FOR TWO SETS OF REASONS THE ITALIANS WOULD HAVE GREAT DIFFICULTY IN PARTICIPATING IN A QUICK DISBURSING FINANCIAL PACKAGE FOR NIGERIA.

3. THE FIRST SET OF REASONS IS TECHNICAL. ACCORDING TO GALLI, FINANCIAL SUPPORT OF THE KIND WE ENVISAGE WOULD NOT FALL WITHIN THE TERMS OF ITALIAN AID LAW. ACCORDING TO SARCINELLI, THERE ARE NO OTHER FUNDS AVAILABLE IN ITALY FOR GIVING THIS KIND OF HELP. ACCORDING TO SELVAGGI, ITALIAN AID IS CONCENTRATED ON THE POORER COUNTRIES IN AFRICA. IT WOULD REQUIRE A COLLECTIVE MINISTERIAL DECISION, PROBABLY ENDORSED BY PARLIAMENT, TO OVERCOME THESE PROBLEMS. GALLI ADDED THAT THE NIGERIAN AMBASSADOR HAD BEEN TO SEE HIM ONLY A FEW DAYS AGO AND DID NOT PRESS FOR ANY URGENT HELP. IN THEORY, COMMODITY AID COULD BE GIVEN IF A DECISION WERE TAKEN TO CHANGE ITALIAN AID PRIORITIES, BUT THIS WOULD NOT BE A QUICK DISBURSIN AID OF THE KIND NEEDED IN THE PRESENT CASE.

4. SALLEO TOLD ME IN CONFIDENCE (PLEASE PROTECT) THAT THERE WAS

THE ADDITIONAL INTERNAL PROBLEM THAT THE RECENTLY REPLACED DIRECTOR-GENERAL FOR DEVELOPMENT HAD OVERSPENT HIS AUTHORISED BUDGET FOR AID TO AFRICA BY 25%. THIS HAD INFURIATED ANDREOTTI WHO HAD HAD HIM TRANSFERRED. BUT THE RESULT WAS THAT EVEN IF OTHER DIFFICULTIES COULD BE OVERCOME, THERE WOULD BE NO MONEY IN THE KITTY AT PRESENT.

5. THE SECOND SET OF REASONS WAS POLITICAL. THERE IS STILL STRONG RESENTMENT IN ROME ABOUT WHAT IS SEEN AS THE EXTREMELY ROUGH TREATMENT THE ITALIANS RECEIVED AT THE HANDS OF THE NIGERIAN GOVERNMENT OVER THE TOXIC WASTE ISSUE EARLIER IN THE YEAR. EVEN IF ITALIAN MINISTERS WERE PREPARED TO SWALLOW THEIR PRIDE AND FIND A WAY OF CONTRIBUTING TO AN INTERNATIONAL FINANCIAL PACKAGE OF THIS KIND, THEIR OFFICIALS BELIEVE THAT THEY WOULD FACE CONSIDERABLE DIFFICULTIES WITH PUBLIC AND PARLIAMENTARY OPINION.

6. WE HAVE POINTED OUT FORCIBLY AT ALL LEVELS THE WIDER INTERNATIONAL FINANCIAL POLICY CONSIDERATIONS WHICH ARISE IN THIS CASE. I APPEALED TO ME INTERLOCUTORS AS G7 PARTICIPANTS TO RAISE THEIR SIGHTS ABOVE THE TECHNICAL AND INTERNAL POLITICAL DIFFICULTIES AND TAKE ACCOUNT OF THE POSSIBLE CONSEQUENCES SHOULD THE NECESSARY FINANCIAL SUPPORT NOT BE RAISED. SARCINELLI ANA SALLESO BOTH SAW THE POINT BUT WERE SCEPTICAL ABOUT WHETHER THEIR MINISTERS WOULD FEEL ITALY SHOULD PLAY A PART IN A NIGERIAN RESCUE PACKAGE.

7. GALLI HAS UNDERTAKEN TO CONSULT HIS MINISTERS AND LET ME HAVE A DEFINITIVE RESPONSE AS SOON AS POSSIBLE. BUT I DOUBT IF WE SHALL BE ABLE TO LOOK TO ITALY FOR MORE THAN MORAL SUPPORT, AND EVEN THAT MAY, IN THE CIRCUMSTANCES BE PRETTY QUALIFIED.

THOMAS

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OF 020925Z DECEMBER 88

AND TO IMMEDIATE ODA, ABU DHABI, BONN, UKREP BRUSSELS, COPENHAGEN
AND TO IMMEDIATE THE HAGUE, KHARTOUM, LAGOS, OSLO, OTTAWA, PARIS
AND TO IMMEDIATE RIYADH, ROME, STOCKHOLM, TOKYO, WASHINGTON
AND TO IMMEDIATE UKDEL IMF/IBRD WASHINGTON

YOUR TELNO 679 TO BONN AND MY TELNO 291 : AID TO NIGERIA

FROM UK EXECUTIVE DIRECTOR TO AFRICAN DEVELOPMENT BANK

SUMMARY

1. EVEN ON FURTHER REFLECTION, AFDB SENIOR MANAGEMENT SEE NO WAY TO ADD TO EXISTING AND PROGRAMMED AFRICAN BANK FLOWS TO NIGERIA. THEY PARTICULARLY RESIST ANY IDEA OF NEW POLICY-BASED LOANS BEFORE 1990, OR ACCESS TO MORE THAN TOKEN ALLOCATION OF SOFT AFRICAN DEVELOPMENT FUND LOANS. THEY CONFIRM FORECAST FLOWS IN 1989 AT USD 250, WITH SIMILAR SUM IN 1990.

DETAIL

2. SINCE THE DETAILED DISCUSSION REPORTED IN MY TELNO 291 (NOT TO ALL), VICE PRESIDENT RESPONSIBLE FOR NIGERIAN PROGRAMME (LOUNES) HAS REFLECTED FURTHER ON THE POSSIBILITY OF SIGNIFICANT NEW AFDB MONEY FOR NIGERIA, AS WELL AS ON THE PROSPECTS OF SPEEDING UP THE DISBURSEMENT OF THE EXISTING AND SCHEDULED PROGRAMME. HE EXPECTS LITTLE. ABOVE ALL, HE IS ADAMANT THAT THERE CAN BE NO PBL BEYOND THE EXPORT STIMULATION LOAN APPROVED IN MID-1987 BUT UNLIKELY TO BE SIGNED BEFORE JAN OR FEB. WHILST HE ACCEPTS THE GRAVITY OF NIGERIA'S POSITION, AND THE IMPLICATIONS FOR SUB-SAHARAN AFRICA AS A WHOLE, HE FEELS THAT ANY LARGE RESPONSE FROM THE AFDB WOULD RISK UNDERMINING THE BANK'S OWN POSITION.

3. QUITE ASIDE FROM THE FIRM CLAMP ON AFDB'S PBL IN 1989 (LIKELY TO BE 35 PER CENT, AGAINST NON-REGIONAL'S HOPE FOR 20-25 PER CENT), THERE IS NO SYMPATHY FOR NIGERIA TO JUMP THE QUEUE. VP LOUNES ARGUES THAT THE AFDB SIMPLY DOES NOT HAVE THE POLITICAL CLOUT TO CONDUCT AN 'INTELLIGENT AND CIVILISED' POLICY DIALOGUE WITH NIGERIA, OR TO ENFORCE CONDITIONALITY EVEN IF THEY CAME IN ON THE COAT-TAILS OF THE IBRD. IT WOULD, HE SAYS, BE IRRESPONSIBLE FOR THE AFDB TO EXTEND MORE PBL TO NIGERIA IN THE CLIMATE LIKELY TO PREVAIL. IF THE IBRD WERE ABLE TO OPERATE ITS PBL EFFECTI

VELY DURING 1989 THE AFDB COULD HOWEVER CONTEMPLATE AN

ALLOCATION FOR NIGERIA IN 1990.

4. ON THE PROSPECTS OF QUICKENING THE PACE OF PROJECT DISBURSEMENT LOUNES SAYS THAT THE BANK WOULD BE PR

EPARED TO CONSIDER SOME RELATIVELY FAST-DISBURSING REHABILITATION LOANS DURING 1989, AND THE BANK FOR ITS PART WOULD MOVE QUICKLY IN PROCESSING PROJECTS IN THE PIPELINE. BUT THE DIFFICULTIES OF WORKING WITH THE COMPLEX FEDERAL AND STATE BUREAUCRACIES WERE FOR THE NIGERIANS, NOT THE AFDB TO RESOLVE.

5. NIGERIA HAD BEEN PENCILLED IN FOR A TOKEN ALLOCATION OF THE SOFT AFRICAN DEVELOPMENT FUND (IDA-TYPE TERMS) RESOURCES. ANY SIGNIFICANT ALLOCATION WAS HOWEVER RULED OUT : TOO MANY OTHER COUNTRIES (EG EGYPT) WOULD ALSO EXPECT BETTER TREATMENT.

COMMENT

6. ATTITUDES IN THE AFDB TOWARDS NIGERIA ARE INFLUENCED VERY MUCH BY THE FRANCOPHONE MENTALITY WHICH DOMINATES MUCH POLICY THINKING. BUT BANK STAFF ARE AS MUCH BEMUSED BY AS PREJUDICED AGAINST NIGERIAN AUTHORITIES. I DOUBT VERY MUCH IF I WILL GET ANY DIFFERENT RESPONSE FROM THE PRESIDENT UPON HIS RETURN NEXT WEEK. I SHALL HOWEVER TRY. I SHALL ALSO CONTINUE TO TRY TO WIN SUPPORT FROM MY NON-REGIONAL COLLEAGUES. ANYTHING THAT POSTS IN PARIS, TOKYO, WASHINGTON AND OTTAWA CAN DO TO ENCOURAGE HOST GOVERNMENTS TO GIVE SYMPATHETIC INSTRUCTIONS TO THEIR EXECUTIVE DIRECTORS WOULD BE HELPFUL.

SUTHERLAND

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OF 021400Z DECEMBER 88
INFO ROUTINE TOKYO, LAGOS



NIGERIA: JAPANESE SUPPORT

I PUT TO KOCH-WESER (COUNTRY DIRECTOR, IBRD) THE LINE GIVEN IN RESPONSE TO OUR REPRESENTATIONS BY MATSUURA, UTSUMI AND KASHIWAYA (TOKYO TELNO 1054).

2. KOCH-WESER SAID THAT THE JAPANESE SPOKESMEN HAD GIVEN THE QUOTE OFFICIAL OFFICIAL LINE UNQUOTE. ACTION WAS IN FACT IN HAND TO SORT OUT THE ARREARS PROBLEMS TO WHICH REFERENCE WAS MADE. THE BANK STILL BELIEVE THAT DOLLARS 250 MILLION WILL BE AVAILABLE FOR COFINANCING THE TIPL - UNDERSTOOD TO BE COMPOSED OF DOLLARS 200 M OECF AND DOLLARS 50 M EXIM, AND CONDITIONAL UPON SOLUTION OF THE ARREARS PROBLEM - AND THAT THE JAPANESE ARE INTERESTED IN PROVIDING MORE, ASSUMING THERE IS QUOTE UK LEADERSHIP UNQUOTE. KASHIWAYA CONFIRMED AS MUCH TO KOCH-WESER HIMSELF RECENTLY. PERHAPS IF ONE READS RATHER HEAVILY BETWEEN THE LINES OF THE TUR ONE CAN SEE SIGNS OF THIS IN REFERENCES TO A DOLLARS 500 MILLION NIGERIAN REQUEST (PARA 5).

3. AS SEEN FROM HERE, WE WOULD STILL OF COURSE BE WELL ADVISED TO TAKE FULL ACCOUNT OF THE JAPANESE OFFICIAL POSITION AND PARTICULARLY THEIR CONCERN OVER ARREARS ISSUES, AND NOT APPROACH THEM AS THOUGH THEIR FUNDS WERE ALREADY COMMITTED. WE ASSUME THAT SOLUTION OF THE JAPANESE ARREARS PROBLEM IS ENVISAGED BY THE BANK AS TAKING PLACE IN THE CONTEXT OF THEIR OWN EARLY DISBURSEMENTS OF BALANCE OF PAYMENTS SUPPORT AND/OR JAPAN'S OWN GRANT (PARA 2 OF TUR). THE FIGURES QUOTED IN PARA 4 OF TUR DO NOT LOOK TOO INTIMIDATING.

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AND ROUTINE ODA, ABIDJAN, ABU DHABI, BONN, UKREP BRUSSELS
AND TO ROUTINE COPENHAGEN, THE HAGUE, KHARTOUM, LAGOS, OSLO, OTTAWA
AND TO ROUTINE PARIS, RIYADH, ROME, STOCKHOLM, TOKYO

AID TO NIGERIA: YOUR TELNO 679 TO BONN
SUMMARY

US STATE DEPARTMENT SYMPATHETIC TO THE NEED TO ASSIST
NIGERIA. BUT THEY THOUGHT THAT A FINANCIAL CONTRIBUTION FROM
THE US WOULD BE QUOTE VERY DIFFICULT UNQUOTE. NEVERTHELESS,
SOME HOPEFUL SIGNS.

DETAIL

2. AT A MEETING TODAY FAINT, POCOCK AND HEYWOOD LOBBIED
US STATE DEPT (BOGOSIAN, DIRECTOR, OFFICE OF MONETARY AFFAIRS,
DIBBLE, HUFF AND JACKSON) AND TREASURY (BLAKE AND PLEUS) ALONG
THE LINES OF YOUR TUR. THEY WERE ALREADY PRETTY WELL IN THE
PICTURE. USAID THOUGH INVITED DID NOT ATTEND, BUT THE AFRICA
BUREAU WILL PUT THEM IN THE PICTURE.

3. BOGOSIAN SAID THAT THE US HAD A CONSIDERABLE INTEREST
IN NIGERIA BECAUSE OF ITS SIZE AND ITS IMPORTANCE FOR THE
REGION AS A WHOLE. HOWEVER THERE WAS NO USAID PROGRAM IN
NIGERIA. BUDGETS HAD ALREADY BEEN FULLY COMMITTED FOR THE
CURRENT FISCAL YEAR AND WERE VERY TIGHT - IF NIGERIA WERE TO
RECEIVE MONEY IT WOULD HAVE TO BE AT THE EXPENSE OF OTHER
AFRICAN PROGRAMS. THIS WOULD RAISE VERY DIFFICULT ISSUES INDEED.

4. WE STRESSED THE IMPORTANCE OF NIGERIA BOTH FINANCIALLY
AND POLITICALLY, AND THE DEMONSTRATION EFFECT ON OTHER AFRICAN
COUNTRIES. WE DID NOT NECESSARILY EXPECT A US CONTRIBUTION
COMMENSURATE WITH THE UK'S OFFER OF DOLLARS 100 MILLION, BUT
SOME CONTRIBUTION WOULD BE MOST IMPORTANT. BOGOSIAN
CONFIRMED THAT THE US AGREED ON THE IMPORTANCE OF BRINGING
NIGERIA INTO THE ADJUSTMENT FOLD.

5. HE WAS INTERESTED TO KNOW WHICH OTHER CREDITORS WOULD
BE CONTRIBUTING TO THE PACKAGE. WE EXPLAINED OUR LOBBYING
EFFORTS IN DONOR CAPITALS, TOGETHER WITH THE EC, THE AFDB AND
OTHER INSTITUTIONS, AND CONFIRMED THAT WE HOPED THAT JAPAN
WOULD MAKE A SIGNIFICANT CONTRIBUTION. WHEN BOGOSIAN ASKED
WHETHER US FINANCE WOULD BE NECESSARY IF JAPAN AND OTHERS WERE
LIKELY TO HELP, WE STRESSED THE IMPORTANCE EVEN A FAIRLY

[Depends
on what is
meant by
'hopeful']
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SYMBOLIC US CONTRIBUTION WOULD HAVE IN INFLUENCING OTHER POTENTIAL DONORS. BOGOSIAN WONDERED HOW QUOTE SYMBOLIC UNQUOTE: A DOLLAR FIVE MILLION CONTRIBUTION WOULD SURELY BE EMBARRASSING. BUT A SUM OF, SAY, DOLLARS 30-50 MILLION WOULD BE AMONGST THE LARGEST US AID PROGRAMS IN AFRICA AND WOULD BE VERY DIFFICULT TO FIND. USAID WERE ALREADY SO CONSTRAINED IN AFRICA THAT EVEN DOLLARS 1 MILLION WAS FIERCELY ARGUED OVER. IT WAS DIFFICULT TO TAKE FUNDS FROM POOR AFRICAN COUNTRIES FOR NIGERIA. WE RESPONDED THAT NIGERIA WAS CLEARLY A POOR COUNTRY TOO.

6. IN CONCLUSION, BOGOSIAN SAID THAT HE WOULD REPORT TO HIS SUPERIORS THAT WE HAD MADE A FORMAL REQUEST FOR A CONTRIBUTION. HE ADDED THAT THE US WAS ENCOURAGED BY THE STEPS THE NIGERIANS WERE TAKING AND IMPRESSED BY THE LEADERSHIP ROLE ADOPTED BY THE UK IN THE MOBILISATION OF AN AID PACKAGE. HE SAID THAT USAID WOULD BE WILLING TO LOOK AT THE POSSIBILITY OF MAKING A CONTRIBUTION ALTHOUGH HE REPEATED THIS WOULD BE DIFFICULT (DIBBLE INTERJECTED THAT IT MIGHT BE POSSIBLE TO USE THE QUOTE OPEX MONEY UNQUOTE - PRESUMABLY A REFERENCE TO THE LAPSED LIBERIAN PROGRAM).
PARIS CLUB

7. BOGOSIAN SAID THAT MILAM WANTED TO ATTEND THE PARIS CLUB SESSION ON NIGERIA, AND SUGGESTED WE SHOULD URGE THE NIGERIANS TO LOOK AT THE POSSIBILITY OF GETTING TO THE PARIS CLUB IN THE WEEK BEGINNING 23 JANUARY. IT WAS AGREED THAT THIS WOULD DEPEND ON WHETHER THE FUND BOARD HAD AGREED THE SBA PROGRAM BY THIS STAGE. BOGOSIAN SAID THAT THE US WOULD QUOTE WORK ON UNQUOTE THEIR POSITION IN THE PARIS CLUB. THE NEGOTIATION WOULD NOT BE AN EASY ONE.
SAUDI ARABIA

8. BOGOSIAN SAID THAT THE NIGERIANS HAD ASKED THE US TO APPROACH SAUDI ARABIA TO MAKE A CONTRIBUTION. HE UNDERSTOOD THAT AAA WAS GOING TO VISIT RIYADH QUOTE IN THE NEXT FEW DAYS UNQUOTE AND STRONGLY ADVISED THAT THE UK FOLLOW AAA'S VISIT WITH AN APPROACH TO RIYADH QUOTE AT THE HIGHEST LEVEL UNQUOTE. AFTER THAT, THE US WOULD BE PREPARED TO USE THEIR INFLUENCE TO FOLLOW UP THE NIGERIAN/UK APPROACHES. BOGOSIAN EMPHASISED, HOWEVER, THAT HE THOUGHT IT WOULD BE COUNTER-PRODUCTIVE FOR THE US TO WEIGH IN WITH THE SAUDIS AHEAD OF AAA'S VISIT.
COMMENT

9. WHILE BOGOSIAN WAS CAREFUL TO LEAVE US IN NO DOUBT THAT A US FINANCIAL CONTRIBUTION WOULD BE VERY DIFFICULT, THIS WAS A MORE PROMISING MEETING THAN WE HAD EXPECTED. THE US CLEARLY SUPPORT OUR ATTEMPTS TO CONCERT A DONOR PACKAGE AND

SEEMED TO RECOGNISE THE IMPORTANCE OF A US CONTRIBUTION. THEY WERE VERY KEEN TO KEEP IN TOUCH WITH DEVELOPMENTS AND WERE QUITE POSITIVE ABOUT NIGERIA'S REFORM PROGRAM AND PRIOR ACTIONS.

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NIGERIAN ECONOMY

THE NIGERIAN PRESS HAVE PICKED UP A VOICE OF AMERICA RADIO REPORT THAT THE IMF HAVE PROVIDED NIGERIA WITH A DOLLARS 500 MILLION STAND BY FACILITY. (THESE HAVE BEEN THE ONLY PRESS REPORTS OF SUCH DEVELOPMENTS).

THIS HAS LED THE INFORMATION MINISTER, MOMOH, TO SAY THAT NIGERIA HAD NOT TAKEN THE IMF LOAN AND WOULD NOT TAKE IT. HE SAID 'THERE IS A DIFFERENCE BETWEEN IMF ENDORSEMENT OF NIGERIA AND TAKING A LOAN'.

BARDER

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