

PO-CH/NL/0459 PT B

Part B.

**CONFIDENTIAL**  
(Circulate under cover and notify REGISTRY of movement)

Begins : 7/6/88.  
Ends : 28/12/88.

**THIS FOLDER HAS BEEN REGISTERED ON THE REGISTRY SYSTEM**

PO CH | NL / 0459.  
PT.B.

Chancellor's (Lawson) Papers:  
African and Sub-Saharan Debt Relief Initiatives ..

DD's : 25 Years

*Richard*  
9/2/96.

PO CH | NL / 0459  
PT.B.

*pur*

FROM: J C MAY  
DATE: 7 June 1988

PS/CHANCELLOR

cc Sir G Littler  
Mr Lankester  
Mr H P Evans  
Mr Mountfield  
Mr P G F Davis

**SUB-SAHARAN AFRICA**

As requested in your minute of 3 June I attach a brief report on the background to the recent Development Council meeting which passed a resolution on the adjustment process in sub-Saharan Africa.

J C MAY

Ch  
Development - speak I'm afraid,  
but worth having a (clear!) paragraph  
as part of the letter for Toronto - I'll  
set a hand.

*Mills*

**DEVELOPMENT COUNCIL: RESOLUTION ON THE ECONOMIC SITUATION AND ADJUSTMENT PROCESS IN SUB-SAHARAN AFRICA**

Meeting on 31 May, the Development Council adopted a resolution on the adjustment process in sub-Saharan Africa. This was the culmination of a process begun last November when the Development Council agreed to a special programme of assistance for LIDDS in sub-Saharan Africa. The resolution on structural adjustment sets out in broad terms the approach which the Community should follow in supporting the structural adjustment process in the region, and will be of considerable importance in informing the Community's approach to the forthcoming negotiations on a replacement to Lome III.

2. The key elements in the resolution from the UK's point of view are:

Structural adjustment is seen as an essential condition for any sustained recovery of economic growth: fast disbursing aid in support of adjustment is seen as complementary to, and not in some way different from, longer term support for development measures.

Sectorial policies should mesh with macro-economic adjustment measures.

The stress on the leading role played by the World Bank and IMF in structural adjustment and the need for effective coordination between these bodies and the Community.

3. As always, the resolution reflects a great deal of work at official level. On our side, we were anxious to remove language that spoke of long term development "not being sacrificed" to adjustment. That misconception would hamper attempts to restore the basis for growth through adjustment and strengthen the hand of those who wish to set up a separate - and additional - adjustment facility under the new Lome Convention. Success at this stage does not, however, mean that the matter will go away. We were also successful in stressing the leading role of the IMF/World Bank and in avoiding any mention of a specific - and by implication somewhat separate - Community approach to the problem.

4. The question of how to support structural adjustment will come up again in the negotiations for a new Lome Convention due to start at the end of this year. The overall UK objective will be to contain the size and the UK share of the next European Development Fund. To this end we will be placing emphasis on the need to improve the effectiveness of aid provision. On the question of adjustment itself the Commission has proposed a new facility to provide for more flexible and faster support for adjustment and will also argue for additional finance. We will be pressing for greater emphasis on adjustment but through the better use of existing resources.

5. If the Chancellor wishes to refer to the Development Council resolution in any future speech I suggest he welcomes it, in particular its recognition of the need for continued adjustment efforts to secure sustainable long term economic growth, its recognition of the leading role of the IMF and World Bank and the need for more effective coordination by donors, and the increasing emphasis on the provision of fast disbursing aid to support adjustment.

*pus*

FROM: A R BOTTRILL

DATE: 9 JUNE 1988

PS/CHANCELLOR

cc: Economic Secretary  
Sir P Middleton  
Sir G Littler (or)  
Mr Lankester (or)  
Mr Mountfield (or)  
Mrs Thomson (or)

PM'S QUESTIONS: SUB-SAHARAN AFRICAN DEBT

*(not sent)*

No.10 has asked for briefing on President Mitterand's initiative on Sub-Saharan African debt for the Prime Minister's questions this afternoon. I attach draft supplementary and background notes.

*A B Bottrill*

A R BOTTRILL

NOTES FOR SUPPLEMENTARIESDoes the Prime Minister agree with President Mitterand's initiative on Sub-Saharan African debt?

I received a letter from President Mitterand yesterday setting out his proposals, and I expect to discuss them further when I see him tomorrow. At least one of the French alternative proposals - that creditors should lower interest rates on rescheduled debt - is close to the initiative which my Rt hon. Friend the Chancellor of the Exchequer has already put forward.

French proposals to cancel a third of rescheduled debt more generous than the Chancellor's initiative?

Need to consider overall effects. The French are <sup>contributing</sup> ~~containing~~ this with early repayment of principal which could affect debtor countries' cash flow adversely.

Prospects for agreement at Toronto?

I believe that we now have good prospects to bring to fruition the efforts that the UK has made in the past year to achieve an international agreement to bring relief to debt-distressed, low-income countries which are following approved adjustment programmes.

BACKGROUND NOTE

The French initiative on Sub-Saharan African debt described in President Mitterand's letter of 7 June to the Prime Minister suggests that creditor countries should choose between three options to help debt-distressed, low income countries:

- (i) Cancellation of one-third of official export credit claims becoming due for rescheduling in the Paris Club with the remainder of such debt being subject to market interest rates and repaid over 10 years.
- (ii) Rescheduling of debts in the Paris Club over 25 years (as opposed to 20 years at present) at market interest rates.
- (iii) Rescheduling of debts over 15 years but at interest rates reduced by at least a half.

2. The French themselves intend to choose the first option. The second is similar to one proposed by the Americans - with the important exception that they have not yet agreed to extend maturities beyond 20 years. The third is close to the Chancellor's initiative. This looks for a reduction of about 3 percentage points in interest rates, which would be rather less than a halving compared to UK current interest rates (LIBOR) of  $8\frac{1}{2}$  per cent.

PERSONAL AND CONFIDENTIAL

FROM: A G TYRIE  
DATE: 9 JUNE 1988

CHANCELLOR

## PRESENTATION OF SUB-SAHARAN DEBT

On the radio this morning I think that you did not succeed in fully recovering the PR ground lost to the French. It sounded as if you were concentrating too much on the fact that it was your initiative rather than on what we've actually done.

This all may be water under the bridge now but if you're asked 'do you approve of this?' I think the answer should be:

'Yes of course, because it's what we've already done. We have already written off our aid loans and we have rescheduled a large part of of our export credits. Furthermore we have suggested that low income sub-Saharan countries should be offered lower interest rates. It's not yet clear whether the French are prepared to go as far as us on all of this, but I hope so'.

Now that the French have stolen a march on us on the PR front I think it will be difficult to get coverage for the (otherwise excellent) Hudson draft release. Furthermore, if we do get coverage it could be written up (wrongly) as a response to the French.

PP  
A G TYRIE

FROM: P MOUNTFIELD  
DATE: 10 JUNE 1988

NOTE FOR RECORD

PARIS CLUB: G5 HEADS OF DELEGATIONS BREAKFAST: 8 JUNE 1988

Present:

Trichet  
Samuel-Lajeunesse  
de Rosen (Fr)  
Von Korff (FRG)  
Kondo (Japan)  
Milam (US)  
P Mountfield (UK)

A. Debt of the poorest

This discussion took place before publication of Mitterand's letter to Summit Heads of Government. Everyone knew it was coming, but the French expressed themselves unsure about content. (I believe it was finally settled during the morning, but they must have known the main elements: the debate had raged internally for a couple of weeks.) In retrospect, I think Trichet was preparing the ground for what followed.

Trichet reported on the Sherpas' discussion. He said the US seemed, in Baker's Abidjan speech, to have accepted the idea of a 'menu' approach with options, as proposed by Canada. There seemed to be a near-consensus about the seven. But Korff objected: he would have preferred the Paris Club to look at the Canadian compromise proposal before the Sherpas endorsed it. And Kondo said that, although Japan would probably not block a consensus, Gyohten had not finally agreed to anything at the Sherpas meeting. Milam said Baker had backed the Canadian idea after being lobbied at ministerial level at the OECD meeting; it was a pity there had been no prior consultation.

I suggested that, in order to make progress before Toronto, the Club's afternoon session should examine the Canadian proposal in detail but ad referendum; I have no mandate from the Chancellor to agree finally to anything Kondo suggested adding a third option: 'equivalent measures'. Up to and including Takeshita himself, Japan had decided to make very large sums available to Africa. I said it was difficult to measure equivalence and impossible to assure additionality; though Japan's enormous contribution was no doubt additional, others would abuse this option and get a free ride.

Trichet then admitted that Mitterand was studying 'un immense dossier' and would shortly be writing to Heads of Government. Korff said Kohl was holding a Cabinet meeting that day to decide the German policy; this would probably lead to an extension of RTA to a wider range of African countries, though by tranches and subject to tight conditionality. FRG was also reviewing its policy on interest rates, but he did not expect a change of policy to be announced before the IMF Annual meeting in Berlin in September. FRG would also look carefully at the Canadian 'menu' proposal. But it risked breaching the important principle of creditor solidarity.

Trichet (perhaps preparing the ground for Mitterand's letter) strongly urged us to consider the 'menu' approach. Provided there was a reasonable trade-off between reduced receipts and increased risk, all creditors would be making comparable efforts. The idea was now in the public domain and expectations had been aroused. Too much insistence on unanimity would force the US or Japan into a corner, and block the expected progress.

We agreed to pursue these points in the afternoon session.

## **B. Yugoslavia**

Rosen said he had met Skapin (the Yugoslav deputy Finance Minister) two weeks earlier. As reported by telex, he had tried to persuade him that the novel elements in the Yugoslav proposal were

non-negotiable. This included the suggested MYRA; a longer-term than 10 years; and 'new money'. If the Club was prepared to reschedule interest, this would help to bridge the gap. Korff said FRG would disburse its 'prefunding' loan of DM172 million next week.

### **C. Nigeria**

Milam said that US Exim was about to reopen cover (despite my earlier attempts to persuade Bonn to go slow until some progress had been made with the IMF). Korff and Lajeunesse both said their agencies would also reopen shortly. I said ECGD was about to announce a new credit (Biwaters) but this was an existing commitment and did not represent any change of policy. We remained very cautious, and were, indeed, worried about the risk of breakdown in the negotiations with the banks. When the IMF mission returned from Lagos, I wanted them to make contact with the Chairman of the Paris Club and start talking about rescheduling official debt; 'exceptional efforts' would be needed. I offered to join in such private talks if the Chairman would find this useful; Trichet immediately agreed.

*P.P.* *T. Potter*  
**PETER MOUNTFIELD**

#### **Copies to:**

**PS/Chancellor (Personal)**

**Sir G Littler**

**Mr Lankester**

**Mr Evans**

**Mr Bottrill**

**Mr Walsh**

**Mr P Davis**

**Mrs Thomson**

**Mr Miles, BOE**

**Mr Jagers, BOE**

**Mr Richardson, FCO**

**Mr Hulse, FCO**

**Mr Ireton, ODA**

**Mr Breach, ECGD**

**Mr Short, CO**

12/1

Alex.

This is marked

"PS/Ch (personal)". Some of

it is quite interesting, but you

will see why I thought it best not  
to show it to Ch! 25/10/86

FROM: P MOUNTFIELD

DATE: 10 JUNE 1988

NOTE FOR THE RECORD

PARIS CLUB: HEADS OF DELEGATIONS DINNER 8 JUNE 1988

A. YUGOSLAVIA

Trichet reported on his discussion with Rikanovic that afternoon. Most of this resurfaced next day and need not be recorded here. The main point was Rikanovic's wish to secure \$500 million of 'new money' from government creditors. His formal proposal was to get this in the form of 'financial credits'. Trichet and de Rosen had convinced him that this was outside Paris Club competence. But part of this sum could be found by rescheduling interest, which was not part of the Yugoslav demand. Creditors (Trichet told him) would probably accept this, as a wholly-exceptional measure. But this would only produce about \$200 million in 1988. Rikonovic wanted a minimum of \$400 million - apparently because the commercial banks had insisted on a contribution of this size from governments. Rikonovic had therefore suggested a commitment by the Paris Club to reschedule interest in 1989. Although this would not directly help cash-flow in 1988, he could borrow against it. Trichet told him creditors would not be prepared to go beyond the end of the SBA (July 1989). Maybe a goodwill clause for future years would be possible; but Rikanovic said he could not borrow against this. Trichet also said that other elements of the Yugoslav demand (MYRIA; 17 years' repayment; enhanced surveillance after 1989) were also unacceptable.

B. DEBT OF THE POOREST

Trichet read and translated the text of President Mitterand's letter to Heads of Government. He said that copies would go

immediately to the seven Summit countries, and then to the other creditors. (For the first time it would become embarrassingly necessary to decide whether to include eg Brazil and Kuwait.)

Under questioning, he clarified a number of points:

- The write-off proposal applied only to one-third of the debt falling due for rescheduling in a particular Paris Club operation, not to the total stock of debt of eligible countries. (But over time, most or all of the stock would be covered). The remaining two-thirds could be rescheduled over ten years at commercial rates of interest.
- It applied to commercial (=COFACE, ECGD, &c) debt. His assumption was that old aid loans would continue to be rescheduled on concessional terms.
- France would probably not act unilaterally. If the proposal were accepted, and all three options were included in future Paris Club agreements, France would adopt the first (write-off) option.
- The position of the 'uninsured portion' of the debt had not been worked out.
- The write-off option will require legislation in France (just as RTA would).
- It would be necessary to define a reference rate from which the halving of interest rates in the second option could be measured. The easiest course would be to take the rate used in earlier reschedulings (ie the Canadian proposal).
- He had not thought through the question of subordination (ie the relative status for the three new categories of debt in the event of a further rescheduling). I pointed out that this was critical to the measurement of risk.
- The intention was to produce a balanced package of options, trading-off concessionality and extra risk. The ground rules would need to be established fairly clearly in advance, by agreement among creditors. The debtors should not be allowed to bid up one part of

the package (eg the reduction of interest rates) without recognising the need for changes in the other inter-related elements.

- The cost to France, if applied to all eligible countries, could be as high as Fr. 1 billion a year. This would not come out of the existing Aid Budget and would be borne centrally by the Tresor. (It would however probably score in DAC as oda.)
- The details would be set out in the working paper which the Secretariat had already promised to circulate before the special meeting on 11/12 July. (See note of plenary session.)

The general reaction was mixed. FRG said privately to me that this move clinched the deal; no-one could block the French proposal. USA carefully reserved Baker's position but was obviously impressed by the move. Canada and Sweden agreed with me, again privately, that the French had neatly scooped the pool, putting forward a package which no-one would be able to reject. Kondo told me later that he was 'shocked'. But Japan would probably accept the menu approach, and select the 25-year option. Some of the smaller creditors (Netherlands, Belgium, Spain) were very hostile, resenting the way in which they saw G7 railroading them. Switzerland and Denmark were privately content. Formally I reserved the Chancellor's position; but I said this was an important new proposal which we would all want to study very urgently and carefully. I also said, off the record, that it reminded me of the Punch cartoon of Peel stealing the Whigs' clothes while they were bathing. The UK had stolen Sweden's clothes; Canada had stolen ours; USA had removed Canada's; and France had taken the lot. This led Trichet off into a wonderful impersonation of Lord Cockfield attacking the Chancellor at the last ECOFIN, which I had better not record in detail.

### C. UNCTAD AND DEBT

Trichet reported an invitation from the Secretary General of UNCTAD to attend ('in a personal capacity') a small meeting in July which would help the S-G prepare a report to the UN General Assembly,

on Debt questions. He thought that he should probably accept; UNCTAD - despite the activities of the Secretariat - was now much more moderate in its language. Everyone agreed.

**D. OAU DEBT CONFERENCE**

Trichet said he had received a message from the President of OAU and had circulated a draft reply. Now that OAU had postponed its debt conference until 1989 (at earliest) there was no need to concert a Paris Club position.

*T. Pott*  
*P.P.* P MOUNTFIELD

**Copies to:**

**PS/Chancellor (Personal)**

**Sir G Littler**

**Mr Lankester**

**Mr Evans**

**Mr Bottrill**

**Mr Walsh**

**Mr P Davis**

**Mrs Thomson**

**Mr Miles, BOE**

**Mr Jagers, BOE**

**Mr Richardson, FCO**

**Mr Hulse, FCO**

**Mr Ireton, ODA**

**Mr Breach, ECGD**

**Mr Short, CO**



(Von Korff) says privately that he believes Kohl will follow Mitterand's lead. But I suggest you talk to Tietmeyer and see if he can confirm this. Kohl may try to save up his final gesture until the annual meetings in Berlin, for domestic political reasons. The Prime Minister may need to intervene to shift him.

3. All this presupposes that the UK should support Mitterand. I strongly recommend that we should (despite some technical problems which need to be sorted out: see below). It gives us, in substance, what we have wanted all along - a reduction in interest rates (or an equivalent write-off of principle) by all the main creditors of Africa. The US (and probably Japan) will settle for longer-term rescheduling instead: but their share of the debt is pretty small except in Zaire (80 per cent of US Sub-Saharan African exposure) and Egypt. The benefit to the poorest African debtors will be very considerable; and diplomatically, we can claim it as a victory for British logic. The Chancellor may want to keep this card up his sleeve until the last moment. (I note that he did not play it in his statement of 9 June). But I hope he will do so at Toronto.

4. If so, you will need to watch out for the language of the Communique. Some possible guidelines:

- (a) it should firmly endorse the idea of a three-dish menu (not four) involving a trade-off between generosity and risk;
- (b) it should not endorse the precise details of the Canadian or French proposals; the numbers should be taken as illustrative;
- (c) it should be, in form, a recommendation from the seven and a declaration of their unanimous intention. The seven cannot dictate terms to the other ten or twelve creditor (who will have to be bullied into agreement later, eg at ECOFIN for the Community countries);
- (d) if possible, it should set a timetable for completion of the technicalities. (If it will keep Kohl happy, this could be 'in time for the Berlin meeting').

5. That leaves the technicalities, some of which are quite expensive. The Paris Club Secretariat has promised a paper on these after the Summit which we are due to discuss in Paris on 11 and 12 July. I shall need to get your instructions nearer the time. But we can already see the main issues.

- (i) The three-dish menu depends on a careful calculation of the relative costs and risks of the three options. These lie along a trade-off curve which the French tell me they have worked out very crudely. They have been through the same intellectual processes as us. The longer the credits are outstanding, the greater the risk. The difference between the NPVs of the claims of the three different groups of creditors represent an implicit risk-premium. How big should it be?
- (ii) the nature of the risk depends on what happens if the debtor has to reschedule again during the currency of the agreement, before France (10 years) or UK (perhaps 15 years) has been paid off. Do the more generous creditors then take precedence (seniority) over the others? The US have a legal hang-up, and apparently cannot accept the formal subordination of their claims. There are ways round this problem. For example (a Swedish proposal, put to me over lunch last week) we could establish an informal Paris Club rule that we would all accept that the more generous creditors would be given better treatment in a future rescheduling. (This would be like the informal rule that we never change the cut-off date). But the problem needs to be clarified before we can settle the exact trade-offs between the three groups.
- (iii) Once that has been settled, we can define the slope of the trade-off curve. (Sorry for the technical jargon, but it is the easiest way of presenting the problem). The French proposals are pretty good, but we need to check the figures. They do involve what Mr Lankester originally proposed - pushing the Americans out to 25 years. But they also involve the UK (assuming we take the third option in the list) moving out from

10 to 15 years; we shall have to persuade ECGD to accept that.

- (iv) The French proposal also asks the UK to increase the concessionality, from a reduction of three percentage points to a halving of our normal interest rate (LIBOR + 0.5%). I do not yet know how expensive that will be: at a guess, about another £10 million in a full year. Obviously we need to warn the Chancellor and the Chief Secretary; you will want to carry Mr Anson with you before we settle this finally. ODA will not mind, provided we give them the extra money, which they will pass on to ECGD, as already agreed.
- (v) The eligibility rules need tidying up. Mitterand's letter speaks of 'the criteria approved since Venice'; but these are very vague, since the Paris Club has proceeded 'case by case' without rigorously defining the elephant it has nevertheless recognised. We shall have a fight about this, to include as many friendly Anglophones as possible without bringing in Nigeria or Egypt if we can avoid them.

6. Perhaps we could have a word about all these points before you leave for Toronto?

RM

P MOUNTFIELD

PS. I now learn - since scribbling this on the way home from Paris - that Mr Lankester has asked for some draft Communique language. I will be circulating a rough attempt later today.

FROM: A BOTTRILL

DATE: 14 JUNE 1988

PS/CHANCELLOR

cc: Chief Secretary  
Economic Secretary  
Sir P Middleton  
Sir G Littler  
Mr Anson  
Mr Lankester  
Mr H P Evans  
Mr Mountfield  
Mr H G Walsh  
Mr Gieve  
Mrs Thomson  
Mr Hudson

AFRICAN DEBT

The attached annexes should be included with Mr Mountfield's note of today's date.

*AB Bottrill*

A BOTTRILL

Bottrill  
14/6

## Costs of alternative options for debt relief to low-income countries

1. No methods have been agreed yet for assessing the costs of the various options. Our own first step has been to compare the net present value of future payments flows under different schemes. This not only provides a single statistic for comparing the final result of each option but also allows them to be compared over time. A potential source of controversy is the appropriate rate of discount to use. We have adopted 8 per cent as being consistent with a 5 per cent real rate of return (as normally assumed in the Treasury) coupled with an assumed 3 per cent a year inflation rate.

Table 1: Comparison of net present values on \$100m rescheduled debt

	Paris Club base case	Longer maturities	Lower interest rates					Debt cancellation	
			(a)	(b)	(c)	(d)	(e)	(a)	(b)
Grace/tenor	10/10	15/10	10/10	10/5	7/8	5/10	5/5	5/5	0/10
Interest rate	8	8	5	5	5	5	5	8	8
Year									
5	32	32	20	20	20	20	20	21	44
10	54	54	34	34	52	58	83	67	67
15	84	68	60	77	79	80			
20	100	89	75						
25		100							

2. Table 1 shows that for those countries charging market interest rates the net present value is the same of course however long the repayment period. In the case of the normal Paris Club 20-year term and President Mitterrand's suggested longer 25-year term with no debt write-off and no interest reduction, this is put at 100. If a third of the debt is written off the NPV is 67, ie a reduction of 33 per cent. In the cases where interest rates are lowered, the final NPV differs according to the length

of the repayment period. Repayment over 20 years would imply an NPV of 75, ie a reduction of 25 per cent. The NPV rises to 83 or a loss of only 17 per cent if repayments are over 10 years.

3. The path of net present values over time reveals some disturbing features. The argument for countries accepting lower interest rates in return for early repayment is that they should be subject to less risk. This depends, however, on whether their claims are given seniority. If they are not, then in the early years those countries enjoying market interest rates will typically also have higher net present values. Only if low interest rate countries insist on a grace period as short as five years on a 15-year maturity will their NPV exceed the market interest rate creditors by the tenth year. Even by the fifteenth year low interest countries' NPV will still be below that of the market interest countries if the latter stick to 20-year loans. Only if these are pushed out to 25 years will the low interest countries be ahead by the fifteenth year - although their total NPV will still be more than 20 per cent below that of the market interest countries.

4. An alternative comparison is to consider the additional risk premium received by those countries opting for longer repayment periods at market interest rates. These can be expressed as the extra annual rate of return that they earn during the period that they are at additional risk compared to the countries which offer lower interest rates.

**Table 2: Implied risk premiums earned by countries accepting longer maturities compared to low interest creditors**

	Lower interest cases				
	(a)	(b)	(c)	(d)	(e)
Grace/Tenor	10/10	10/5	7/8	5/10	5/5
<u>20-year creditors</u>					
No subordination	33	5½	4¾	4½	1¾
Subordination for 10 yrs	2¾	2½	2½	2¼	1¾
Subordination throughout loan period	1½	1¼	1¼	1	1
<u>25-year creditors</u>					
No subordination	5¾	2½	2½	2¼	1¼
Subordination for 10 yrs	2	1¾	1½	1½	1¼
Subordination throughout loan period.	1¼	1	1	1	¾

5. Table 2 shows the results where creditors receive market interest rates over 20 years or alternatively 25 years. In the cases where market interest rate creditors refuse any subordination of their loans, they are at additional risk only for the period after the low interest creditors have been repaid. If low interest countries are repaid over 15 years and market interest countries are repaid over 20 years for example, the latter receive an implied additional risk premium of  $4\frac{1}{2}$ -5 per cent a year during the last five years. If the market interest creditors agree to extend payments over 25 years, then their premium falls to 2- $2\frac{1}{2}$  per cent a year.

6. If market interest creditors agree to subordinate their loans to those of the low interest creditors at least for the life of the loan, then they are at extra risk for much longer periods and the implicit risk premium they receive falls to about 1 per cent in both cases. An in-between case would be where market interest creditors agreed to subordinate their claims at least for the first 10 years of the loan. This would increase the period for which they were at risk and give them a premium of about 2 per cent.

7. It is clearly a matter of judgment how great a premium the low interest countries might allow the market interest countries. A rate of close to 5 per cent would seem unacceptable. This suggests at a minimum that market interest creditors should be pressed to accept repayments over 25 years rather than 20 years. We should also be pressing for seniority for the low interest countries loans preferably for their whole duration but at least for part of the period.

## Debt of low-income African countries at end-1986

<u>Country</u>	\$m			
	Total debt	of which official	of which ECAs	of which ECGD
Benih	1073	771	392	15
Burkina Faso	664	598	108	-
Burundi ✓	556	461	33	-
Central African Republic ✓	435	375	61	-
Chad ?	179	157	33	-
Comoros ?	161	108	2	-
Equatorial New Guinea ?	164	40	6	-
Ethiopia	2196	1348	325	24
Gambia ✓	314	255	85	9
Ghana ✓	3285	2279	189	83
Guinea ✓	1530	938	388	6
Guinea-Bissau ✓	318	165	39	-
Kenya ?	4791	3789	889	152
Lesotho	193	171	9	1
Liberia	1562	1196	254	16
Madagascar ✓	2958	2141	847	15
Malawi ✓	1115	1019	127	9
Mali ?	1772	1051	132	10
Mauretania ✓	1807	795	248	6
Mozambique ✓	1379	853	365	57
Niger ✓	1493	837	278	6
Rwanda	457	381	24	1
Sao Tome ✓	34	27	2	-
Senegal ✓	3416	2250	816	10
Sierra Leone ?	645	403	61	2
Somalia ?	1815	1068	135	14
Sudan ?	8616	5447	3087	165
Tanzania ✓	4224	2944	1287	120
Togo ✓	1183	1018	508	11
Uganda ✓	1191	951	120	15
Zaire ✓	6876	5964	3382	65
Zambia ?	5146	3489	934	117
<b>Total (32)</b>	<b>61548</b>	<b>43289</b>	<b>15156</b>	<b>988</b>

✓ = eligible for World Bank SAP  
 ? = under review for SAP.

## Public expenditure cost of debt relief for low-income African countries

The public expenditure cost of providing interest relief will depend on what portion of debt is rescheduled at each stage and for how many countries. ECGD had at the end of 1987 some £928 million of principal claims outstanding on 32 low-income African countries including some £582 million of previously rescheduled debt. If this principal was all rescheduled further, then the public expenditure cost of reducing interest rates by 3 per cent would amount eventually to almost £30 million a year.

### ECGD claims on low-income African countries at end-1987

	32 countries <sup>(1)</sup>	Cost of relief	Nigeria	Cost of relief
Unscheduled principal	346	10	975	29
Interest becoming due in future on unrescheduled principal	111	3	198	6
Rescheduled debt (P and I)	582	17	1246	37
Interest becoming due in future on rescheduled debt	317	10	477	14
Total	<u>1356</u>	<u>40</u>	<u>2896</u>	<u>86</u>

(1) excludes Nigeria

2. ECGD will also be owed a total of £428 million in interest payments in future years on its existing stock of claims. If this interest is also rescheduled and capitalised, then the public expenditure cost would rise by £12 million a year to a total of about £40 million. This would build up slowly over the maturity of existing loans. ECGD, for example, is due to receive only £182 million in total in 1989, including all principal and interest payments so that the public expenditure cost of giving 3 per cent interest relief on this would be £5½ million.

3. Inclusion of Nigeria in the scheme would make a big difference. ECGD has £2.2 billion of principal outstanding to Nigeria including £1.0 billion unrescheduled debt and £1.2 billion of previously rescheduled debt. If only the <sup>un</sup>rescheduled principal was affected, the cost would be an extra £29 million a year. If previously rescheduled debt and all future interest payments were included the cost could rise to a hefty £86 million.

*par*

FROM: P MOUNTFIELD

DATE: 14 JUNE 1988

- 1. MR LANKESTER
- 2. CHANCELLOR

*agreed  
P. 146*

cc: Mr Evans  
Mr Walsh  
Mr Bottrill  
Mrs Thomson

copies attached for:

- Chief Secretary
- Economic Secretary
- Sir P Middleton
- Sir G Littler
- Mr Anson
- Mr Gieve
- Mr Hudson

*Oh  
For background tomorrow. Can  
discuss substance @ meeting  
on Thursday*

AFRICAN DEBT

*it is essentially a revision of  
his note to G52, that you have  
already seen (telis).*

This note suggests the UK position for Toronto and beyond. The Chancellor may like to have this by him for the Prime Minister's briefing meeting tomorrow and for his press conference. The note lists the issues which have to be decided before Toronto, and suggests a line on each. It proposes some communique language to be tabled at an appropriate moment in Toronto. Mr Bottrill is separately providing as much statistical back-up as possible. We discussed this with officials from FCO, ODA, ECGD and the Bank earlier today. What follows is on lines agreed with them.

Recent background

2. Mitterand's proposal was published while I was in Paris last week and I was able to clarify bits of it. Essentially the French have taken the Canadian compromise proposal, endorsed by Baker, and grafted on a third option (cancellation of part of the debt, as proposed by Mitterand in his election address). This gives

*Separate  
string*

a range of options: the most-generous creditors write off part of the debt, and their balance is repaid over ten years: the middle group halve their interest rates and get out over fifteen years; the meanest charge a commercial rate but are locked in for twenty five years. The figures are meant to be illustrative, not final proposals, but it will be difficult to vary them. This is a very ingenious package which puts the US, Germans and Japanese neatly on the spot.

3. Trichet elucidated some of the details at the Paris Club meeting last week:

- The write-off proposal applied only to one-third of the debt falling due for rescheduling in a particular Paris Club operation, not to the total stock of debt of eligible countries. (But over time, most or all of the stock would be covered). The remaining two-thirds could be rescheduled over ten years at commercial rates of interest.
- It applied to commercial (=COFACE, ECGD, &c) debt. His assumption was that old aid loans would continue to be rescheduled on concessional terms.
- France would probably not act unilaterally. If the proposal were accepted, and all three options were included in future Paris Club agreements, France would adopt the first (write-off) option.
- The position of the 'uninsured portion' of the debt had not been worked out.
- The write-off option will require legislation in France (just as the write-off of aid loans).
- It would be necessary to define a reference rate from which the halving of interest rates in the second option could be measured. The easiest course would be to take the rate used in earlier reschedulings (ie the Canadian proposal).
- He had not thought through the question of subordination

(or written off)  
really?

(ie the relative status for the three new categories of debt in the event of a further rescheduling). I pointed out that this was critical to the measurement of risk; see below.

- The intention was to produce a balanced package of options, trading-off concessionality and extra risk. The ground rules would need to be established fairly clearly in advance, by agreement among creditors. The debtors should not be allowed to bid up one part of the package (eg the reduction of interest rates) without recognising the need for changes in the other inter-related elements.
- The cost to France, if applied to all eligible countries, could be as high as Fr. 1 billion a year. This would not come out of the existing Aid Budget and would be borne centrally by the Tresor. (It would however probably score in DAC as oda.)
- The details would be set out in the working paper which the Secretariat had already promised to circulate before the special Paris Club meeting on 11/12 July, to work out a complete scheme.

You will see from this that the three-dish menu depends on a careful calculation of the relative costs and risks of the three options. These lie along a trade-off curve which the French have worked out (very crudely). They have been through the same intellectual processes as we. The longer the credits are outstanding, the greater the risk. The difference between the NPVs of the claims of the three different groups of creditors represent an implicit risk-premium. How big should it be? The nature of the risk depends on what happens if the debtor has to reschedule again during the currency of the agreement, before France (10 years) or UK (perhaps 15 years) has been paid off. Do the more generous creditors then take precedence (seniority) over the others? Unless they do, we think the risk premium which the US is getting would be far more than they deserve for waiting another 5 or 10 years for their money. Once that has been settled, we can define the slope of the trade-off curve. The French proposals are pretty good, but we need to check the figures. They do involve what Mr Lankester

originally proposed - pushing the Americans out to 25 years. But they also involve the UK (assuming we take the third option in the list) moving out from 10 years to 15.

4. There are seven issues on which we need a UK line.

(a) Do we accept the idea of a three-dish menu?

I believe we should. If agreed by the 7 it gives us, in substance, what you have argued for all along - a reduction in interest rates (or an equivalent write-off of principal) by most main creditors of Africa. I believe FRG will join us and France. The US (and probably Japan) will settle for longer-term rescheduling instead: but their share of the debt is pretty small except in Zaire (80 per cent of US Sub-Saharan African exposure). The benefit to the poorest African debtors will be very considerable; and diplomatically, we can claim it as a victory for British logic. You may want to keep this card up your sleeve until the last moment. But I hope you will do so at Toronto. The condition of your agreement should be, I suggest, acceptance of the idea of equitable burden-sharing.

(b) Do we keep the menu to three dishes, as Mitterand proposes? Or do we let the Japanese introduce a fourth option: 'equivalent measures'?

Japan claims it cannot give debt relief but should be given credit instead for its very generous new aid programme. Two problems: how to measure and compare aid with debt relief; and how to ensure that the aid is genuinely additional. Too difficult: keep the menu to three.

(c) Should the UK accept the interest rate reduction option? If so, do we agree to halve interest rates, or reduce (as you first, tentatively, suggested) by three percentage points?

1. No  
2. Yes for M.H.

This option comes closest to your original proposal, and we have assumed you will want to opt for it - though there is not much to choose in principle between this and the French 'write-off one-third' method, since both involve an actual reduction in the net present value of our claims. The amount of the reduction is debatable. You originally favoured 'minus three percentage points' because it seemed fairer to high-interest rate countries than 'halving'. The reduction could not be much more than three points without Japan going below zero. Our conclusion is that you should try for your original proposal, but settle for halving if necessary (for additional costs, see Mr Bottrill's separate note). But should you also accept rescheduling over fifteen years? You were originally prepared to combine twenty years with an interest rate reduction: the idea of a shorter term only came in when Canada first suggested a trade-off. Conclusion: 15 years is acceptable if the US accepts 25 - see below.

? If of France,  
- 1/3 off of interest

- (d) Should the third option be 25 years (as Mitterand suggests) or 20 years - the present Paris Club maximum?

Baker indicated in his Abidjan speech that he was not prepared to go beyond 20, which meant that he was making no new concessions, simply allowing others to be generous. Later Washington reports suggest a rethink is going on. Conclusion: insist on 25.

- (e) How to secure seniority for the more generous creditors?

The US claim to have legal problems in formally subordinating their own claims to those of other creditors - even if the other creditors are being more generous. That is why the original Canadian compromise suggested a trade-off between generosity and tenor. However, it is now clear that the trade-off is not fair unless the first two groups also get seniority

Summary

in the event of a further rescheduling. If we cannot get legal subordination, we could at least establish an internal Paris Club convention on 'rules of the game', so that we and the French get an advantage if (for example) Zaire has to reschedule again before our claims have been paid in full (ie year 10 for France, year 15 for us). You will not be able to get this worked out in detail in Toronto. But you should try to get communique language which establishes the principle.

(f) Which countries are eligible?

Mitterand speaks of the criteria established at Venice, but these were never spelt out clearly. You originally proposed a triple test: poverty; debt-distress; and adjustment. Several different lists have been established, with slight variations of these criteria. We think the simplest solution is to use one already in use by the World Bank to define eligibility for their Special Action Programme for Africa. It has the advantage of existing already: this cuts down the haggling. It has the support of the Donor Community already (at the World Bank's meeting on Africa in March). It excludes, for the moment, Nigeria and Egypt. It may not be necessary to spell this out in the communique.

WS

(g) Would the UK proceed unilaterally if it cannot get agreement? (You may be asked this at the Press Conference).

Answer:  
Pessimistic &  
wholly hypothetical  
question.

French intentions are not entirely clear. Mitterand seemed to say yes; Rocard seemed to say no. Officials told me France would only proceed as part of a Paris Club deal. Your line tomorrow might be that the UK wants to give the maximum benefit to the African debtors; this means persuading all the creditors to join in by one means or another. So we shall be insisting on a multilateral approach.

5. The draft communique passage below tries to pin down the Summit members on all these points. The essential points are:

- (a) it should firmly endorse the idea of a three-dish menu (not four) involving a trade-off between generosity and risk;
- (b) it should not endorse the precise details of the Canadian or French proposals; the numbers should be taken as illustrative;
- (c) it should be, in form, a recommendation from the seven and a declaration of their unanimous intention. The seven cannot dictate terms to the other ten or twelve creditor (who will have to be bullied into agreement later, eg at ECOFIN for the Community countries);
- (d) if possible, it should set a timetable for completion of the technicalities. (To keep Kohl happy, this could be 'in time for the Berlin meeting').

R1

PETER MOUNTFIELD

DRAFT COMMUNIQUE PASSAGE

*No [unclear] [unclear]!!*

[Limit to Africa if possible]

[SUB-SAHARAN AFRICAN DEBT]

[Direct quote]

Heads of Government recalled their decision at Venice to ease the debt burden of the poorest African countries that are undertaking adjustment efforts.

*not true: "agreement should be reached, especially in Paris Club, on longer repayment & grace periods to ease the debt service burden"*

[Cannot say more. No actual progress on RTA]

They welcomed the progress made since then in the Paris Club, by way of agreement on longer repayment periods for these countries. They took note of the various proposals made in recent weeks towards a definitive solution of the problem.

[Kept vague]

*?? and grace periods  
This all looks too French*

[Two key words:  
- equitably  
- defined]

[N6: direct, ie not Japanese idea of 'equivalent measures']

Heads of Government agreed to implement a new scheme of debt relief, the burden of which should be shared equitably among creditor governments on a clearly-defined basis. In their view, this basis should provide for differing forms of direct debt relief. [Some creditors might reduce the interest rates charged, in exchange for a shorter repayment term. Other would extinguish part of the debt, recovering the balance in a shorter time. A third group might wish not to make immediate concessions, but to accept the greater risk of rescheduling their claims over longer periods than have been agreed so far.] The relative contributions of these different groups would need to take account of [these] differing levels of risk, particularly of those which might arise in the event of any further rescheduling.

[Enumerate all 3 if possible; with UK option first. If not, at least insist on trade-off sentence below]

[ie more than 20 years, to make US give]

[Emphasise idea of trade-off. Keep, in addition to 3 options]

[Stake out position on subordination]

[Timetable and remit: clear lead but no dictation to other PC creditors]

Heads of Government urged the Paris Club to complete the definition of a workable scheme, to enable finance ministers of the creditor countries to reach final agreement at the time of the IMF/IBRD annual meetings in Berlin in September.

*now mounted  
out - below*



FROM: A C S ALLAN  
DATE: 14 JUNE 1988

*pr*

CHANCELLOR

*Ch  
Another thing I'd get  
we-press conference is set out  
of all communique on this  
AA*

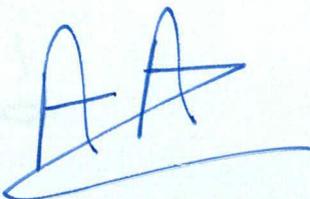
AFRICAN DEBT: FACTS

The factual material is seriously incomplete. In the morning I will try to get as much as possible of the following:

- i. What would be the public expenditure costs if we wrote off a third of our ECGD debt? (not that you are thinking of doing it, but you should know the figures)
- ii. What would be the costs of halving the interest rate on our ECGD debt? (ditto).
- iii. Have we completed writing off our aid loans? If not, why not?
- iv. How can we justify excluding Nigeria? Why is it not in the World Bank list - is it just because they have not taken on board the latest data for Nigeria's GNP per head? What line should you take in public if asked about Nigerian eligibility?
- v. How do we justify drawing a ring-fence around Africa? If relief was given to other countries who met the criteria, who would they be and how much would it cost us?



- vi. How much have each of the other G7 countries done in writing off aid loans? And how much more have they got to do?
- vii. What is the scale of other countries export-credit debt to the countries eligible for this relief? How much would it cost them (a) to write off a third of this (b) to give a 3% interest subsidy and (c) to halve the interest rate they charge? Is their debt owed primarily from just a few of these countries, and if so, which ones?
- viii. How would each of them be affected if Nigeria and/or Egypt were included in the list?
2. Are there any other points you want covered?

  
A C S ALLAN

FROM: A BOTTRILL

DATE: 15 JUNE 1988

MR A C S ALLAN

cc: Sir G Littler  
Mr Lankester  
Mr H P Evans  
Mr Mountfield  
Mr P G D Davis  
Mr Gieve  
Mrs Thomson**AFRICAN DEBT: FACTS**

The Chancellor asked for further information. The following answers have been compiled with the help of AEF1 and ECGD.

(i) The public expenditure cost of writing off a third of ECGD claims.

ECGD has almost £1 billion of principal claims outstanding on countries which currently qualify for the World Bank's special assistance programme for Africa or are being considered for it. (This excludes both Nigeria and Egypt.) In addition ECGD is due to receive interest payments of some £400 million over the life of these loans. If ECGD followed the French option and all repayments of principal and payments of interest came to be rescheduled, the public expenditure cost would be about £460 million spread over 10 to 15 years. This is very much a worst case since it is unlikely that all countries would reschedule or that all principal and interest would be rescheduled.

(ii) Cost of halving the interest rate of ECGD loans.

Both the French proposal for halving interest payments and the Chancellor's own suggestion for a flat reduction of 3 percentage points would apply to ECGD claims only as they were rescheduled. On the same basis as (i), the total amount of principal and interest which might be rescheduled over 10 to 15 years, would be a maximum of £1.4 billion. ECGD would normally charge LIBOR plus  $\frac{1}{2}$  per cent on rescheduled claims. At current interest rates

this would imply a rate of around 9 per cent yielding interest receipts of £126 million a year. This would be reduced by £63 million a year if interest rates were halved and £42 million a year if they were reduced by a flat 3 percentage points.

(iii) Has UK completely written-off aid loans

The UK has written off aid loans to all currently eligible countries (those with a GNP per head income of \$425 or less) except Zambia. The sum outstanding there is about £45 million. Aid loans there could only be written off in the context of an agreed IMF adjustment programme, the chances of which are at present limited. Nigeria is another possibility. Its eligibility for IDA, and hence the writing-off of aid loans, is currently under discussion. Were Nigeria to be declared eligible, and agreed an IMF programme, then about £5 million old aid debts could be written off as part of an aid package.

(iv) Can Nigeria be excluded from debt relief package?

In the long run, we may not be able to exclude Nigeria. It isn't included at present (a) because, as you inferred, its GDP per capita, on the 3-year moving average used by the IBRD, isn't down to \$425 yet, (b) it is not conforming to an IMF programme. On (a) it would probably qualify by next year, but the IBRD defined the list for purposes of the three-year SAP in November 1987 and Nigeria isn't included. The line to take with the press is, I suggest: 'No criteria yet agreed for debt relief. Any scheme should be limited, we believe, to the very poorest and most heavily indebted countries with an IMF adjustment programme. Although Nigeria has a very high level of debt, it has historically not been regarded as a poor country. For example, it is not eligible at present for IDA. Nor has it got an IMF programme in place at present. It has enormous natural resources. So inclusion of Nigeria is one of the longer-term questions we shall have to resolve with the other creditors after the Summit'.

We'll  
have  
some  
Crisp  
that!

(v)

Why a ring-fence around Africa?

*Answer their  
come name!  
(2 wr here)  
one)*

Countries outside Africa which have GDP per head a year of less than \$425 include Bangladesh, Bhutan, Burma, China, Haiti, India, Maldives, Pakistan and Sri Lanka. The borderline cases in Africa might be Nigeria and Egypt. The former is likely to become IDA-eligible with GNP per head below \$425. The latter has GNP per head of \$760 but is debt-distressed. ECGD's claims including principal and interest due on the main countries just outside the ring fence are:

	£m	GNP per head (1986)
Egypt	742	\$ 760
Nigeria	2896	\$ 640
Pakistan	25	\$ 350
India	750	\$ 270
China	790	\$ 300

*and Nigeria*

Only Egypt <sup>and Nigeria</sup> out of this group have had to reschedule their debt. Pakistan, perhaps, is the next most risky country. At this stage we avoid the problem by relying on the SAP list. If pressed it may be possible to point to the fact that most of the poor countries outside Africa have managed to avoid the need to reschedule and countries such as India and China have retained substantial access to commercial bank finance.

(vi) Other G7 countries' writing off aid loans.

*V. imp.*

A table showing writing off of aid loans by 5 of the G7 countries (excluding The US and Japan) is attached. (The figures should be treated as orders of magnitude rather than precise sums, particularly for Italy).

The US has passed legislation allowing aid loans to be written off, but has yet to grant any. Japan does not write off loans - its laws do not allow it. It has offered a partial substitute to 11 countries, and has reduced interest rates on loans to a further 7. The cost of these actions is about £30 million a year. Of the remaining G7 countries, Italy and France have done very little - less

than £120 million in the case of France, £38 million for Italy. FR Germany has a good record, over £1 billion in total, of which just over £600 million is for Africa. Canada has written off over £430 million in Africa, of which about £330 million was RTA'd last year.

At the end of 1986, outstanding aid loans to low-income African countries totalled about \$8 billion. During 1987 Canada converted some \$550 million into grants and has now written off all its aid loans. Total loans outstanding, therefore, are probably around \$7½ billion.

(vii) Other countries' export credits

The OECD estimates that official export credit agencies had some \$15 billion in principal outstanding to low-income African countries at the end of 1986. ECGD's claims were equivalent to about \$1.4 billion at end-1986 exchange rates - or slightly less than 10 per cent of the total. (I have attached a revised version of the table on low-income African countries' debt to show ECGD's claims in both dollar and sterling terms. The figures should all be treated with caution.) Within the total of export credit agencies' loans some \$0.8 billion are short-term and therefore typically not rescheduled. Allowing for this, agencies excluding the UK have some \$13 billion which could be rescheduled. Adding interest payments due might raise this to about \$18 billion. It would, therefore, cost other countries \$6 billion to write off a third and \$0.5 billion a year to lower interest rates by 3 per cent. The cost of halving interest rates depends on the average rate charged. Since we do not know the composition of claims by creditor or currency we can only guess at this. The GNP-weighted average of the G6 countries' LIBOR (excluding the UK) is currently about 6½ per cent so there might be little difference in the overall effects compared to a 3 per cent cut. The impact on creditors, however, would differ between low-interest and high-interest countries. I have minuted this separately.

(viii) Inclusion of Egypt and Nigeria?

We do not have detailed figures to hand on total export credits to Egypt and Nigeria. The principal outstanding to all export agencies appears to be of the order of \$12 billion in each. Allowing for future interest payments might increase this to about \$16 billion. This would imply a cost of about \$5 billion to write off a third or almost \$0.5 billion a year to lower interest rates by 3 per cent or halve them. Both effects would build up over 10 years or so. We are checking the figures urgently with the OECD in Paris. In the meantime, they should be treated with caution.

*A Bottrill*

**A BOTTRILL**

## Debt of low-income African countries

Country	\$m end 1986				
	Total debt	of which official	of which ECAs	of which ECGD (end-87)	
				\$m(1)	£m
Benin	1073	771	392	22	15
Burkina Faso	664	598	108	-	-
Burundi*	556	461	33	-	-
Central African Republic*	435	375	61	-	-
Chad <sup>†</sup>	179	157	33	-	-
Comoros <sup>†</sup>	161	108	2	-	-
Equatorial New Guinea <sup>†</sup>	164	40	6	-	-
Ethiopia	2196	1348	325	35	24
Gambia*	314	255	85	13	9
Ghana*	3285	2279	189	122	83
Guinea*	1530	938	388	9	6
Guinea-Bissau*	318	165	39	-	-
Kenya <sup>†</sup>	4791	3789	889	223	152
Lesotho	193	171	9	1	1
Liberia	1562	1196	254	24	16
Madagascar*	2958	2141	847	22	15
Malawi*	1115	1019	127	13	9
Mali <sup>†</sup>	1772	1051	132	15	10
Mauretania*	1807	795	248	9	6
Mozambique*	1379	853	365	84	57
Niger*	1493	837	278	9	6
Rwanda	457	381	24	1	1
Sao Tome*	34	27	2	-	-
Senegal*	3416	2250	816	15	10
Sierra Leone <sup>†</sup>	645	403	61	3	2
Somalia <sup>†</sup>	1815	1068	135	21	14
Sudan <sup>†</sup>	8616	5447	3087	243	165
Tanzania*	4224	2944	1287	176	120
Togo*	1183	1018	508	16	11
Uganda*	1191	951	120	22	15
Zaire*	6876	5964	3382	96	65
Zambia <sup>†</sup>	5146	3489	934	172	117
<b>Total (32)</b>	<b>61548</b>	<b>43289</b>	<b>15156</b>	<b>1366</b>	<b>988</b>

\* = eligible for World Bank SAP

<sup>†</sup> = Under review for SAP

(1) End-1986 £1=\$1.47





**CONFIDENTIAL**

*py*

From: Sir G.Littler  
Date: 17 June 1988

**CHANCELLOR**

*Mano Glum  
@ Tom's -  
White paper*

c.c. Mr Lankester  
Mr Evans  
Mr Mountfield  
Mr Bottrill  
Mrs Thomson

**AFRICAN DEBT**

I apologise for missing your meeting yesterday (the only time I could get hold of DTI to discuss GEMMS, etc).

2. Attached is a draft on the lines I understand you suggested yesterday. It locates the prospective new scheme in the context of your original proposals. But I have strong reservations about this - as a paper for your G7 colleagues.

3. We have two objectives. One is to keep the British label firmly in place; the other is to shape a workable scheme which is acceptable to us.

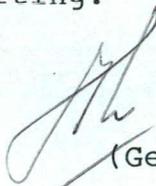
4. The second objective may not be easily achieved: we shall need an alliance with the French - with whom we have common cause vis-a-vis the US, etc - but we shall need to focus discussion by Finance Ministers on this. We can define the sort of framework we want (see second attachment). Ideally we should try to get this agreed in some such form as a letter from Wilson (Chairman) to the Paris Club, and with appropriate less detailed language in the Communique (see revised draft in third attachment).

5. On the first objective, we must think of different fora:

CONFIDENTIAL

- **Communique:** I have slipped in a reference to April 1987; I am sure we can do no more (last year Robert Armstrong could not get even that) - to mention the UK initiative explicitly will provoke demands for mention of all the others who will want their public prizes; you would be wasting time in trying to develop UK-oriented language among Finance Ministers based on the attached paper; which one?
- **Press Statements:** The Prime Minister and you have laid the ground already and must obviously repeat at Toronto: it is a good story, not least because it is obviously true that your continuing pressure was what forced the others to come forward with ideas - you will get credit in the UK press, and among most of the target ldc's, although I suspect there is no way of winning all the Francophone and other foreign press!
- **Plenary Meetings in Toronto:** The Prime Minister and you will again be right to recall your initiative in setting the scene.
- **Finance Ministers:** I fear that a paper like the first attachment would start discussion in an unbusinesslike mode. I would prefer to put in a practical paper, using the second page only and developing the detail rather more based on the second attachment.

6. We should have an opportunity to talk on the plane, with ample time to produce further drafting.

  
(Geoffrey Littler)

FROM: A BOTTRILL

DATE: 17 JUNE 1988

PS/CHANCELLOR

cc: Sir G Littler  
Mr Lankester  
Mr Mountfield  
Mr H P Evans  
Mr Gieve  
Mrs Thomson

## AFRICAN DEBT: CASH FLOW EFFECTS ON LDCs

You may be interested to have the effects on debtors' cash flows of the different schemes being considered. These are the same options as those illustrated in my annex to Peter Mountfield's note of 14 June.

## Comparison of debtors' cash flow position under alternative debt relief options on \$100m

	Paris Club base case	Longer maturities ↓	Lower interest rates					Debt cancellation	
			(a)	(b)	(c)	(d)	(e)	(a)	(b)
Grace/tenor	10/10	15/10	10/10	10/5	7/8	5/10	5/5	5/5	0/10
Interest rate	8	8	5	5	5	5	5	8	8
Years									
1-5	8	8	5	5	5	5	5	5	11
6-10	8	8	5	5	12	14	23	16	8
11-15	16	8	14	13	14	12			
16-20	12	16	12						
21-25	-	12							

2. The table illustrates the cash flow cost to debtor countries of paying market interest rates to countries such as the US. It will also be important, however, to ensure that the French give a grace period. Otherwise, repayments to them would impose a heavy cash flow burden on debtors immediately. Even with a 5-year grace period, cash flows to the French would rise sharply in years 6-10.

*P. Longram*  
PP. A BOTTRILL

FROM: A BOTTRILL

DATE: 19 JUNE 1988

PS/CHANCELLOR

cc: Sir G Littler  
 Mr Lankester  
 Mr Mountfield  
 Mr H P Evans  
 Mr Gieve  
 Mrs Thomson

*Some useful info  
 here: psc put the  
 France on the  
 portfolio for me*

**AFRICAN DEBT: CREDITORS' CLAIMS**

The Chancellor asked what information we have about other creditor countries' amounts at risk in African countries. I have now obtained unpublished figures compiled by the OECD from returns made by export credit agencies. The coverage is incomplete and the definition differs from that used in my annex to Peter Mountfield's note of 14 June. In particular, the present figures include future interest payments but exclude at least in some cases rescheduled debt. They should be treated with caution but may nevertheless give a qualitative impression of which creditors are most heavily exposed to particular debtors.

2. The Summit countries as a whole account for more than 80 per cent of the identified amounts at risk. France has the largest exposure and accounts for close to a third of the total with particularly large stakes in Kenya, Liberia, Senegal, Zaire, Mozambique, Sudan, Tanzania and Zaire. The United States have the next largest exposure with a very substantial stake in Zaire and smaller claims in Sudan, Zambia, Ethiopia and Kenya. The UK is close behind the US with our main exposure in Kenya, Tanzania, Ghana, Zambia, Zaire and Sudan. Other creditors' risks are fairly widely spread with Canada, Japan and Germany having relatively small stakes. (The Italian figures look to be questionable.)

3. On this basis, most of the countries in which the UK has important claims are either already on the World Bank's Special Assistance Programme (SAP) list or are being reviewed for it. The exception is Benin.

Among countries currently outside the ring-fence Egypt and Nigeria are the most important. The US has a particularly large stake in Egypt followed by France, the UK and Germany. The UK and France both have substantial claims on Nigeria followed by Germany and Japan. The US has a large stake in Pakistan.

ABAn U

A BOTTRILL

Export credit agencies' claims on low-income African countries \$m.

	Canada	France	Germany	Italy	Japan	UK	US	Others	Total	SAP list
Benin	-	129	4	-	-	138	-	269	540	
Burkina Faso										
Burundi										
Central African R.										
Chad										
Comoros										
Eg. Guinea										
Ethiopia	17	31	17	15	29	63	148	57	370	
Gambia										
Ghana	7	53	0	1	-	185	20	43	309	*
Guinea	1	123	3	-	-	3	56	38	224	*
Guinea-Bissau										
Kenya	65	675	133	-	9	453	117	185	1637	†
Lesotho										
Liberia	12	520	26	-	-	50	35	218	861	
Madagascar	27	75	10	-	17	6	40	28	203	*
Malawi										
Mali										
Mauritania	-	55	7	-	-	10	7	34	113	*
Mozambique	-	176	65	-	19	76	21	191	548	*
Niger										
Rwanda										
Sao Tome										
Senegal	6	299	3	-	-	35	16	84	443	*
Sierra Leone										
Somalia										
Sudan	12	162	15	-	36	121	248	92	686	†
Tanzania	46	142	12	-	22	194	58	101	575	*
Togo	-	61	5	-	-	82	1	14	163	*
Uganda										
Zaire	22	260	64	-	4	173	866	115	1504	*
Zambia	15	28	23	-	25	177	156	65	489	†
<b>Total (32)</b>	<b>230</b>	<b>2789</b>	<b>387</b>	<b>16</b>	<b>161</b>	<b>1766</b>	<b>1789</b>	<b>1534</b>	<b>8672</b>	
Bangladesh	0	117	1	-	66	40	30	20	274	
China	121	955	1025	-	2651	461	164	670	6047	
Egypt	203	3558	820	509	515	980	5221	2337	14143	
India	325	1135	513	-	96	1818	275	759	4921	
Nigeria	1	2902	1986	31	1307	2915	568	927	10637	
Pakistan	90	183	103	-	47	97	1453	61	2034	
<b>Total (6)</b>	<b>740</b>	<b>8850</b>	<b>4448</b>	<b>590</b>	<b>4682</b>	<b>6311</b>	<b>7711</b>	<b>4774</b>	<b>38056</b>	

\* SAP list.  
† SAP under review.

Source: OECD.

SUB-SAHARAN  
DEBT.

5/1

FROM: P MOUNTFIELD

DATE: 28 JUNE 1988

CHANCELLOR

cc: Economic Secretary  
Sir G Littler  
Mr Lankester  
Mr Evans  
Mr Bottrill  
Mr Walsh  
Mrs Thomson  
Ms Life  
Mr A Tyrie

AFRICAN DEBT

For your meeting on international business, on 29 June, you might like an update of the position following Toronto.

2. The Summit has given the Paris Club a deadline of "the end of the year" to produce a workable scheme. In practice I hope we can improve on this: there are 8 African debtors in the queue for the rest of the year to whom the new terms should be applied if possible. So we shall be trying to get agreement by September at the latest, which can if necessary be ratified at the time of the annual meetings (to make sure that the smaller creditors are politically committed to the plan).

3. The Paris Club is having a special two-day working meeting on 11 and 12 July. The Secretariat is circulating a paper in advance. I am trying to influence the content of the paper and offered to go to Paris specially later this week for that purpose. That did not work; the Secretariat are coming to see me instead, but only just before the meeting. So I have sent them a telex listing the points we want the paper to cover, with provisional indication of our line.

4. The points I have listed are:

(i) definition of the options. The communique language

is not quite tight enough. The note you circulated in Toronto is however very specific. I shall try to get this incorporated in the Secretariat paper; but I have repeated it in my telex, and copied it to the G7 Paris Club countries to stake out our position in advance. The important thing is to get the Americans hooked on 25 years, which Baker seems to have accepted, but the message has not got down the line;

(ii) subordination. The UK paper in Toronto missed out the technical stuff on this, because it was thought too complicated at that stage. I shall therefore try to work it into the Secretariat paper, or, as second best, circulate a note of my own. The key issue is the relative treatment of the three groups of creditors if there has to be a fresh rescheduling;

(iii) eligibility. Subject to your views, I propose to stick initially at the IBRD "Special Action Programme" list of 17 countries, but making sure that the French recognise that this includes a number of anglophone countries which, no doubt accidentally(!?) were missed off their list. You have acknowledged that Nigeria will have to be included eventually; but I am sure it would be wrong to say so in public yet. (We may eventually want to hold this incentive out in front of the Nigerians to bring them to the table, but not yet). I would like your covering authority to fall back on a slightly wider list if the consensus goes that way: probably, to the list of 27 countries originally proposed by the French (see table attached).

5. In addition, there are a number of minor technical points which will take a lot of time.

(iv) definition of starting point or "reference rate" for the interest rate abatement. (Probably, the rate applying to the last Paris Club agreement, where there is one);

(v) consolidation period: probably one year or 18 months, to run coterminously with an IMF SBA;

(vi) inclusion of previously-rescheduled debt. In principle, yes (where necessary to meet a financing gap, which it almost always will be). We want to get the coverage of the new-style agreements as wide as possible. If the financing gap is not wide enough to justify inclusion of PRD, then the country is not really "debt-distressed" and does not qualify anyway.

6. Domestically, we still have to sort out finally:

(vii) accounting arrangements between ODA and ECGD; and PES additions. I shall be reporting separately to the Chief Secretary about this, but probably not until the Autumn, when we know roughly the sums likely to be involved in the present financial year (if any). It does not affect the shape of the Paris Club agreement.

R1

P MOUNTFIELD



For "International basis" meeting.

CONFIDENTIAL

FROM: P MOUNTFIELD

DATE: 14 JULY 1988

- not available
1. SIR, ~~GEOFFREY~~ LITTLER
  2. CHANCELLOR

cc: Mr Lankester  
 Mr H P Evans  
 Mr Bottrill  
 Mr P Davis  
 Mrs Thomson

**PARIS CLUB: AFRICAN DEBT**

This week's special meeting reached a provisional consensus, ad referendum to capitals, on the way to implement the Toronto Agreement. I think it is a very satisfactory conclusion, and when the documents arrive will recommend that you approve it. Meanwhile a brief report may be of interest.

2. Trichet took the chair himself almost throughout, and handled the meeting with great skill to secure the maximum possible consensus. The Germans, although without final instructions, were similarly helpful and constructive. The smaller (non-Summit) creditors were either enthusiastic (Sweden, Switzerland) or co-operative (Austria, Netherlands, Denmark, Norway); only Spain and Belgium made problems. Japan was as usual enigmatic - and inadequately briefed, I think. Only USA was really difficult, operating on instructions which came direct from Baker who seems to be regretting or reinterpreting what he signed up to at Toronto.

3. The outcome will be a letter from the Chairman to the 17 delegations, asking them to commend the whole package to their governments and to report their reactions by (I think) September,

MOUNTFIELD  
 TO  
 CHIEF  
 14 JUL

CONFIDENTIAL

in time for the annual meetings. The package will include:

- (a) a standard draft text for future Paris Club agreements with the eligible countries, setting out the terms of the three separate options. The agreement will specify, each time, which creditors adopt which option. The options have been redefined - see below. We have all agreed the drafts ad referendum;
- (b) an agreed but confidential note about initial eligibility: this includes, by name, all the Commonwealth countries we wanted. The criteria are those of the World Bank SAP;
- (c) an agreed note defining the 'reference rate' from which interest rate reductions will be measured;
- (d) (in the text of the letter) a passage flagging up the question of 'subordination' as one to be addressed later if there needs to be a further re-rescheduling. This was the best I could get; see below.

4. The main points to note are:

- (i) the options have <sup>been</sup> redefined to give the UK and French versions approximately the same ex-ante net present value - 67% by definition for France, which is cancelling one-third of its debt and getting a market rate of interest on the rest. Also by definition, the US version is worth 100% ex-ante, since they are receiving a commercial rate of interest throughout;
- (ii) the UK concession is defined as a reduction of 3½ percentage points or (where this is lower) halving of the interest rate. I formally reserved your position on this, pointing out that you had chosen three percentage points because it enforced an equal contribution from high and low interest rate countries alike; and was the biggest reduction which could be achieved without producing negative interest rates. Trichet dealt with this by arguing that 3.5% helped to equalise the NPVs of the two options; while the low-interest-rate countries could be required to make

CONFIDENTIAL

a minimum contribution of 50%. This is an ingenious formula which I think we can accept; because coupled with the next point it will cost us very little more <sup>than your original proposal</sup> (Figures to follow with full submission);

(iii) this interest rate, when applied over an eight-year grace period and a total fourteen year repayment period, (instead of the US proposed at Toronto), produces an NPV of 67%. And France is prepared to accept a similar repayment period, for symmetry. (This increases French risk, by maintaining exposure for 14 years instead of 10; but does not alter the ex ante NPV.) Trichet proposed this, which is an important French concession, in order to put the French and British options onto exactly the same basis vis-a-vis the US group. At the same time he proposed that the US should accept a grace period of fifteen years, so that repayment of principal to US would start only when other creditors had been paid in full. This helps to equalise the risks of the three groups, as well as providing a smoother repayment profile for the debtor;

(iv) all this assumes that US accepts 25 years but to everyone's surprise the US delegate held out for 20 years and reserved Baker's position. Trichet politely told her that Baker had virtually signed up on 25 years at Toronto, but she was unable to budge. We may need your help in applying some pressure to Baker;

(v) even at 25 years, (compared with our 14) and with 15 years' grace, the US position would be relatively risk-free. I pointed out that the risks of default or of re-scheduling were greater in the middle years, from year 8 onwards when the first grace periods have run out and heavy repayments of principal begin. I said that an ex ante value of 100% for the US option was only comparable to our 67% if the US accepted a much heavier burden of risk. If that risk materialised, the US would have to accept the cost. This did not necessarily mean conceding formal subordination of US debt. Picking up an earlier US phrase, I said I only wanted the US to continue over time its recognition

CONFIDENTIAL

"that the usual 'pari passu' treatment of all creditors alike would not apply to these cases". I went on to suggest two alternatives. We could specify in advance the terms which would apply in any future re-rescheduling; I had detailed proposals which I could table (the ones we discussed with you earlier). Or if the US could not agree to that immediately we could at least flag up the problem in the Chairman's letter and note it as an issue to be resolved later in a way which would maintain fair burden-sharing between the two groups. The US would not even accept this, and insisted on woolly wording saying 'one group thought this, the other group thought that'. I accepted it in the end, because it gives you a chance to pressurise Baker before the final decisions are taken. France was a bit less helpful to the UK on this point (anxious to help the US within the consensus). I had to keep the meeting going into a second afternoon (with German support) to get even this solution adopted;

(vi) ODA loans will be treated differently - either written-off entirely by those countries prepared to do so, or rescheduled over 25 years at the original concessional rate of interest. (This is another big concession by France, which will write-off one-third and reschedule the rest.) I said we would probably accept this as a second-best, while still urging everyone to write-off ODA loans completely;

(vii) the note on eligibility <sup>initially</sup> ~~does not specifically~~ limits the new terms to Africa, <sup>but not specifically</sup> ~~or~~ to the criteria of the World Bank programme. Everyone recognised that they would have to be extended at some stage - perhaps <sup>(US dissenting)</sup> to Bolivia, which is due to be rescheduled this autumn. I said flatly that we wanted to exclude Egypt and Nigeria, at least at this time. Others wanted freedom to turn down a marginal case (like Kenya) which probably meets the tests but may not really need help and has avoided the need to reschedule so far. The list will not be published, and we were exhorted to keep it confidential.

CONFIDENTIAL

5. All in all, a fairly successful outcome, thanks to Anglo-French preparation and cooperation. I shall submit the final documents for your approval when they arrive, and when I have been over them in detail with departments.

R<sub>1</sub>

P MOUNTFIELD

CHANCELLOR

FROM: P MOUNTFIELD

DATE: 22 JULY 1988

cc: Chief Secretary  
 Economic Secretary  
 Sir P Middleton  
 Sir G Littler  
 Mr Lankester o/r  
 Mr Evans  
 Mr Bottrill  
 Mr P Davis  
 Mrs Thomson

*OK - this is a pit- Rat  
 No 3 options are a & when you  
 proposed with the US, & last year  
 Cont 15, content with line?  
 2/22/7*

PARIS CLUB: AFRICAN DEBT

I undertook to submit for your approval the "Chairman's summary" of the meeting I attended last week. Here it is.

2. It is very much on the lines reported in my minute of 14 July. At your meeting on 18 July, you said you were broadly content with this, provided the US gave way on the length of rescheduling (25 years) and on the principle of subordination. You said you were prepared to speak to Secretary Baker if necessary, to achieve this.

*Minutes on 'Brazil' folder - in car box*

3. Sir G Littler has since spoken to Mr Mulford, and tells me that Mulford wants more time. Similarly, the Economic Ministry in Bonn tell me that the FRG decision, although taken in principle, will not be announced until September (for the IMF meeting in Berlin). Nevertheless, the Chairman asks delegations to indicate their government's approval to the package at next week's Paris Club meeting.

4. There are two points of difficulty on the present draft, and one which needs clarification. They are marked A, B and C on the attached draft.

A

5. This is the key point: will the Americans go to 25 years? I suggest I make it clear that UK agreement to the package is conditional on this.

B

6. Subordination (though we must not call it by that precise legal term). The paragraph at the foot of page 1 is basically my draft, but I wanted all creditors to endorse it. The final sentence, though <sup>m</sup>imprecise, establishes the principle of subordination, and would have given us a peg on which to hang the argument if one of these deals came unstuck and had to be re-rescheduled. But the Americans insisted on attributing this view simply to "some creditors" and added their own offsetting sentence at the top of page 2. This is clearly unacceptable. I suggest you give me discretion to fight for the original version, or to fallback on some compromise which has the same sense, but to which the US are clearly committed. This is the point Sir G Littler has asked Mr Mulford to consider.

C

7. This sentence was included at the behest of the Japanese delegation. It is not at all clear what it means. I shall try to get this clarified. Provided that Japan accepts an obligation to do at least as much as is implied by one or other of the options, that should be good enough.

8. You need not read the rather curious Françlais of the agreed minute. The note on the reduction of the interest rate is as agreed in Paris. The graph simply shows the extent to which a debtor benefits from the new treatment (on the assumption that his debt is equally divided between the three groups). The final page sets out the eligible countries: as I told you, it includes all the anglophones in whom we were particularly interested.

9. At the meeting on Monday, you were anxious to ensure that one of the anglophones featured in the first list. The race is on between Tanzania and Uganda. I shall have a private word with the French and ensure that one or other of these features in the first group, probably in October. Provided one of their clients does as well, they will not make any difficulties. I just hope the IMF programmes can be approved in time.

10. On this basis, the total package seems entirely acceptable. If the Americans and Germans insist on having more time, I do not think we shall be asked to give a final answer next week. But, just in case, I should like your authority to say that we shall accept the package if the Americans, Germans and Japanese do. If not, I shall say, I shall need to consult you again.

11. May I so proceed, please?

RM

P MOUNTFIELD

WORKING GROUP ON THE POOREST AND MOST DEBT-DISTRESSED COUNTRIES

CHAIRMAN'S SUMMARY

—o\*o\*o—

The representatives of the creditor countries usually taking part in Paris Club sessions met in Paris on July 11 and 12, 1988 in order to work out new solutions for the debt treatment of the poorest and most heavily indebted countries.

During this meeting, a "menu" approach has been studied. According to this scheme, the creditor countries would agree to adopt one of three options for the consolidation of government loans and governments-backed credits granted to the poorest and most indebted countries :

- write-off one third of debt service obligations to be consolidated, with a repayment period of 14 years (including a 8 year grace period) for the amounts remaining due ;

(A) - consolidate at market rates, with a maturity period extended to 25 years (including a 14 year grace period), instead of 20 years at most presently ;

- consolidate at a preferential rate, which would be the market rate reduced by 3.5 percentage points or 50 % if 50 % is less than 3.5 points, on a maturity period of 14 years (including a 8 year grace period).

(C) The creditor countries could also choose to combine these options.

As regards official development aid loans, the amounts to be rescheduled or refinanced should be reimbursed on a period of repayment of at least (25) (20) years of which 14 year grace period. The rates and the conditions of interest should be at least as favourable as the concessional rates applying to those loans.

The representatives of the creditor countries taking part in the meeting have agreed that this approach would secure an adequate comparability of treatment between creditor countries.

(B) Some creditors underlined that the different treatment of the three groups involved a trade-off between immediate cost (groups A and C) and increased risk (group B). Those creditors noted that group B would be exposed to that risk between years 15 and 25, when groups A and C would no longer be involved. But they also noted that the risks of default or of re-scheduling were likely to be highest from year 8 onwards (at the conclusion of the grace period). They acknowledged that, if it should prove necessary to re-schedule these special agreements in that period, ways to maintain the trade-off between group A and C on the one hand, and group B on the other hand, should be looked at carefully.

Other creditors stated that the principle of equal treatment of the debt was to be applied in possible future reschedulings.

It was also noted that in principle, where re-scheduling should occur, special treatment of maturities having already benefited of the new special treatment should be avoided.

The documents annexed to this summary give precise details about the new approach ;

- document I : draft Agreed Minute (extracts) ;
- document II : statement about interest rate reduction in option C ;
- document III : an exemple of debt service profile with the "menu approach" ;
- document IV : eligible countries in Africa.

The different delegations underlined that the new measures would provide the poorest and most debt-distressed countries with a major debt relief, compatible with the various legal and financial constraints of the creditor countries.

They have agreed to submit this "menu" scheme to their respective Governments and to inform the Chairman of the Paris Club of the positions or decisions taken by their respective Governments on this scheme at the earliest opportunity, and not later than at the time of the end of July Paris Club session.

## 2. Terms of the consolidation

The debt relief will apply as follows :

### A/ As regards credits or loans granted or guaranteed by the Governments of ..... or their appropriate institutions

a) 33,33 % of the amounts of principal and of interest (excluding late interest) due from ... up to .... inclusive and not paid on loans and credits mentioned in paragraph 1 a) and 1 b) above will be canceled.

b) 66,67 % of the amounts of principal and of interest (excluding late interest) due from .... up to ... inclusive and not paid on loans and credits mentioned in paragraph 1 a) and 1 b) above will be rescheduled or refinanced.

c) Repayment by the Government of (debtor country) of the sums referred to in paragraph b) above will be made in 12 equal and successive semi-annual payments, the first payment to be made on (year 9) (end of the grace period) and the final payment to be made on (year 14) (end of the repayment period).

d) The rates and the conditions of interest on the rescheduling or refinancing arrangements covered by paragraph b) and c) above will be determined bilaterally between the Government of (debtor country) and the Government or appropriate institutions of the concerned Participating Creditor Countries on the basis of the appropriate market rate, without prejudice to the provisions of paragraph 4 below.

### B/ As regards credits or loans granted or guaranteed by the Governments of ..... or their appropriate institutions

a) 100 % of the amounts of principal and of interest (excluding late interest) due from ..... up to ..... inclusive and not paid on loans and credits mentioned in paragraph 1 a) and 1 b) above will be rescheduled or refinanced.

b) Repayment by the Government of (debtor country) of the corresponding sums will be made in 22 equal and successive semi-annual payments, the first payment to be made on (year 15) (end of the grace period) and the final payment to be made on (year 25) (end of the repayment period).

c) The rates and the conditions of interest applying on the rescheduling or refinancing arrangements covered by paragraph a) and b) above will be determined bilaterally between the Government of (debtor country) and the Government or appropriate institutions of the concerned Participating Creditor Countries on the basis of the appropriate market rate, without prejudice to the provisions of paragraph 4 below.

### C/ As regards credits or loans granted or guaranteed by the Governments of ..... or their appropriate institutions

a) 100 % of the amounts of principal and of interest (excluding late interest) due from ..... up to ..... inclusive and not paid on loans and credits mentioned in paragraph 1 a) and 1 b) above will be rescheduled or refinanced.

b) Repayment by the Government of (debtor country) of the corresponding sums will be made in 12 equal and successive semi-annual payments, the first payment to be made on (year 9) (end of the grace period) and the final payment to be made on (year 14) (end of the repayment period).

c) The rates and the conditions of interest on the rescheduling or refinancing arrangements covered by paragraph a) and b) will be determined bilaterally between the Government of (debtor country) and the Government or appropriate institutions of the concerned Participating Creditor Countries on the basis of the appropriate market rate reduced by 3.5 percentage points, or 50 % if 50 % is less than 3.5 percentage points, without prejudice to the provisions of paragraph 4 below.

### 3. Late interest

Late interest charges are those interest charges accruing between the contractual payment dates of principal and interest due and not paid, and a date to be fixed in the bilateral agreements concluded for the implementation of the present Minute.

### 4. Official development aid loans

As regards official development aid loans , the amounts to be rescheduled or refinanced according to paragraphs A, B and C should be reimbursed on a period of repayment of at least (25) (20) years of which 14 year grace period. The rates and the conditions of interest should be at least as favourable as the concessional rates applying to those loans.

OPTION C - REDUCTION OF INTEREST RATE

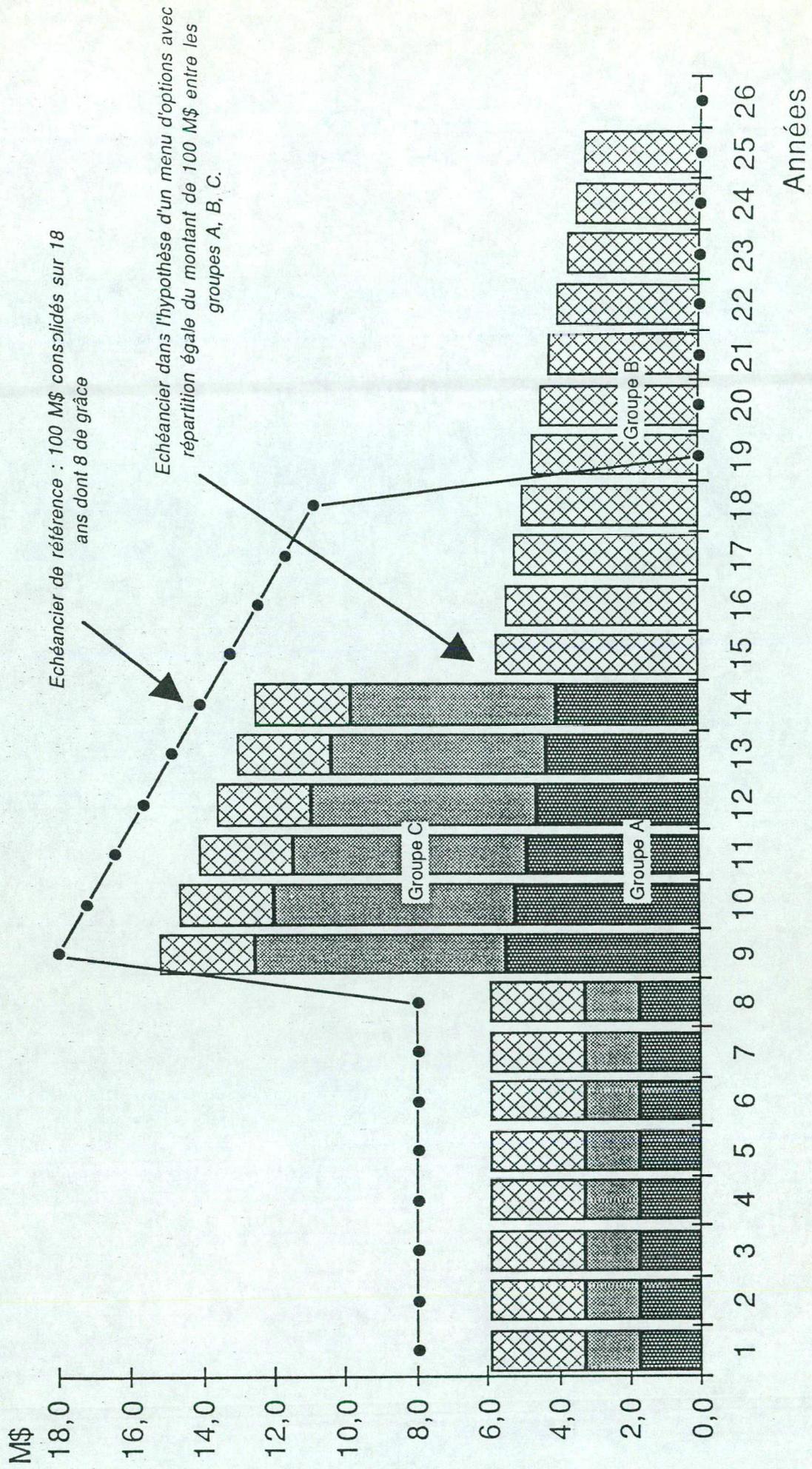
At present, it is clearly stated in the Agreed Minute that the interest rate applying to the consolidation is determined bilaterally on the basis of the appropriate market rate.

The precise reference rate for each creditor country and the margins are negotiated bilaterally.

In the new system, the only difference would be that the basis referred to in the Agreed Minute would become the "appropriate market rate reduced by 3.5 percentage points or 50 %, if 50 % is less than 3.5 percentage points".

Each creditor country would keep the same reference rate as usual. All the other creditor countries will be in a position to check that this reference has not been changed : according to the Agreed Minutes, each creditor country is allowed to require from any other creditor country a copy of its bilateral agreement.

Comparaison entre un échancier avec menu d'options et un échancier avec traitement privilégié actuel



F I C H E

---

OBJET : Pays africains éligibles à un menu d'options en Club de Paris.

1/ Comme pour l'allongement des durées de remboursement, les pays éligibles devraient être les pays les plus pauvres et les plus endettés qui mènent des programmes d'ajustement soutenus par la communauté internationale.

2/ Ces critères nous ont conduit jusqu'à présent à accorder un traitement privilégié en matière d'allongement des durées de remboursement aux 10 pays suivants :

GUINEE-BISSAU, MALAWI, MAURITANIE, MOZAMBIQUE, NIGER, OUGANDA, SENEGAL, SOMALIE, TOGO, ZAIRE.

3/ Il n'est pas étonnant de constater, étant donné la relative similitude des critères retenus par le Club de Paris et la Banque Mondiale, que ces pays figurent sur la liste des pays potentiellement éligibles au programme spécial de la Banque Mondiale pour les pays les plus pauvres et les plus endettés d'Afrique subsaharienne. Les autres pays figurant actuellement sur cette liste ou potentiellement éligibles à ce programme sont les suivants :

BENIN, BURUNDI, BURKINAFASO, CAP VERT, COMORES, DJIBOUTI, GUINEE-EQUATORIALE, ETHIOPIE, GAMBIE, GHANA, GUINEE, KENYA, LESOTHO, LIBERIA, MADAGASCAR, MALI, RCA, RWANDA, SAOTOME, SIERRA LEONE, SOUDAN, TANZANIE, TCHAD, ZAMBIE.

4/ Les critères retenus par les créanciers du Club de Paris pour l'éligibilité au traitement privilégié en matière d'allongement des durées ont été les suivants :

- important service de la dette rapporté aux recettes d'exportation ;
- critère de pauvreté, notamment éligibilité effective aux crédits de l'AID ;
- programme d'ajustement en cours avec le FMI et la Banque.
- besoin de rééchelonnement établi.

Ces critères pourraient être reconduits pour l'éligibilité au menu d'options.

RESTRICTED

From: Sir G. Littler  
Date: 28 July 1988

MR ALEX ALLAN

c.c. PS/Econ Sec  
Mr Lankester  
Mr Huw Evans  
Mr Mountfield  
Mr Tyrie

*Handwritten notes in red ink:*  
N/A... h/r  
mark...  
make...  
New...  
them...  
S...  
w...  
x...  
US...  
sk...  
M...  
can...  
n...  
...  
...

DEBT RELIEF AND THE ENVIRONMENT

Your minute of 27 July. I have checked the transcript of the main Toronto sessions, which accords with my memory that, though Chancellor Kohl certainly mentioned the environmental damage done in some African countries, he did not hint at any proposals of the kind mentioned in the Press Summary.

2. I would not be surprised, however, if something on these lines were to surface in Berlin. Tietmeyer told me he was very worried about likely demonstrations during the annual meetings from anti-IMF and anti-IBRD lobbies in Germany, some connected with the Green party. As the Chancellor knows, the environment is a real political issue there.

(Geoffrey Littler)

FROM: P MOUNTFIELD  
 DATE: 1 AUGUST 1988

PS/CHANCELLOR

cc: Economic Secretary  
 Sir P Middleton  
 Sir G Littler  
 Mr Lankester o/r  
 Mr Evans  
 Mr Bottrill o/r  
 Mr Walsh  
 Mr P Davis  
 Mrs Thomson

*Thanks. Let me know if I  
 need to make any changes.  
 P.M.*

DEBT OF THE POOREST

There was a further, inconclusive discussion of this in the Paris Club on 26 July. There is some danger of the Toronto compromise coming unstitched. It is clear that either different leaders left Toronto with different interpretations of the communique or that the rats have got at them since their return.

2. The Chairman made a valiant attempt to produce an acceptable compromise. This will be set out in a personal letter which he will be sending to each of the 17 delegations later this week, asking them to recommend it to their respective ministers, and to reply to him by 16 September. It requires each government to give a bit of ground in order to restore the consensus - in our case, by giving up our insistence on 'subordination'. I saw the letter in draft privately, and in fact rewrote bits of it. When it arrives, I shall submit it for approval (which I believe it deserves). So this is an interim report: more to follow.

RM

P MOUNTFIELD

PLP

FROM: MR P MOUNTFIELD  
DATE: 30 SEPTEMBER 1988

MR EVANS

cc: PS/Chancellor  
(personal)  
Mr Gieve  
Mr Lankester  
Mr Walsh  
Mr Bottrill  
Mrs Thomson

*\* \* \* Have a Sox  
a sample of  
completeness of  
EPR  
(in place of APP etc)*

*Minuted along with comments on EPR (Miss Edwards's minute of 27 Sept.)*

AFRICAN DEBT

I have now managed to clarify the German position following Berlin. I had to wait until the German Paris Club representative, Von Korff, returned to Bonn.

2. He was quite categorical about it. Germany has completely dropped its insistence upon "taking credit" for the write-off of old aid loans to 6 African countries, announced in June. Germany will now apply option C - the British version - to all 16 of the currently-eligible African countries, and to any more which later become eligible. The actual mechanism will be very slightly different from the British one: they will provide funds from the Aid Budget direct to Hermes (or KFW, I suppose), up to 50 per cent of the interest charged, on behalf of the debtor country: the debt will not formally be relieved by the original creditor. As I said in earlier briefing, I regard this as a technical detail. Von Korff is communicating this decision officially to Trichet on Monday, thus lifting the reservation he placed on the agreement at the last Paris meeting.

3. There remains one further problem: the two small Japanese amendments introduced at the last minute into the text of the Paris Club "Chairman's summary". (These are the two bits

underlined in the version dated 21 September, which I sent to you in Berlin.) Although both Germany and UK were content with these amendments, as was France, the US still has a formal reservation on them. But Milam has told Von Korff privately that he sees no difficulty now in lifting <sup>the</sup> The Paris meeting on Monday 3 October has been cancelled. Trichet will need to write formally to all the delegations to tell them that agreement has been reached. We should then be able to proceed, without any further delay, to reschedule the first two customers: probably <sup>the</sup> and Madagascar. With a bit of luck, Uganda should follow soon afterwards (we are still trying to unscramble the Uganda/Israel problem); but while Tanzania remains at odds with the IMF, there can be no progress there. So the Economic Secretary's promise that two commonwealth countries will be among the earliest beneficiaries may take a bit of time to honour. Early New Year, I would guess.

4. I shall let the Chancellor have a "completion report" after the successful negotiation of the first two cases.

*R*  
P MOUNTFIELD

FROM: MR P MOUNTFIELD

DATE: 31 OCTOBER 1988

CHANCELLOR OF THE EXCHEQUER

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

*Thanks.  
1 note X.  
APM/2  
B. J. T. Who is doing as a  
Bancrupt for my  
LA will have  
H. J. J. J.*

DEBT OF THE POOREST

The Paris Club last week concluded the first two agreements under the new "Toronto terms". As you know, the first was Mali (on Thursday); the second was Madagascar, on Friday.

2. Mali presented no problems. Madagascar was a little more difficult, because Japan was a creditor, and had not yet made up its mind which option to adopt. The agreement therefore contains a special provision, allowing Japan to make its mind up later. In the case of Madagascar this did not matter much, because the sums involved were small. I hope we can avoid it happening in future, because the IMF needs to know the value of the debt relief at the time it is agreed.

3. There are still one or two other loose ends. The very sensible tactics of the French Chairman (Trichet) have been to force through a couple of agreements first, and having created the precedent, to sew up the loose ends later. This is working very well, so far.

4. The main loose end is the problem of geographical coverage. Opinion is sharply divided on whether to limit the operation to

Africa, or to spread it to other comparable countries. The test case is going to be Bolivia, within the next month or two. I am seeing the Bolivian Ambassador tomorrow, and expect him to press hard for the UK to support his case for Toronto terms. I shall of course refuse to be drawn. Among creditors, there is a sharp division. The United States and Japan are strongly opposed to the inclusion of Bolivia; Spain, and a few smaller European creditors, are in favour. Since the Club proceeds by consensus, that means that Bolivia will probably be excluded, without the need for the UK to take a very firm position. But I shall seek your instructions on this point before the next meeting, having consulted the FCO.

5. You were anxious to get a commonwealth country into the first list. This did not prove possible, as you know. There is a good chance that Uganda will be the first, next month. But there is a bilateral problem with Israel, which I have tried hard to resolve. (See further telegram, below.) After that comes Tanzania, but there are serious problems at the IMF which will take some time to sort out yet.

6. You agreed on Friday a short "welcome" line to take in the Press. This duly appeared in Saturday's FT - cutting attached. You might also like to see the French version, in *Le Monde*. Although this gives most of the credit to the French, it does, pleasingly, acknowledge that the UK initiative played a part in getting this scheme on the road.

With the word "initiative" mistranscribed as "innovation". JF

It says hardly anything about the UK's role!  
JF

R1

P MOUNTFIELD

# OUT TELEGRAM

		Classification CONFIDENTIAL	Caveat	Precedence IMMEDIATE
ZCZC	1			
TC	2	CONFIDENTIAL		
CAVEAT	3			
FM	4	FM FCO		
TO	5	TO IMMEDIATE DAKAR		
TELNO	6	TELNO		
OF	7	OF 281600Z OCTOBER 88		
AND TO	8	INFO ROUTINE UKDEL IMF/IBRD WASHINGTON		
	9			
	10	SUMMARY		
	11	MALI IS FIRST COUNTRY TO BENEFIT FROM TORONTO TERMS IN		
	12	PARIS CLUB		
	13	DETAIL		
	14	Mali delegation led by Coulibaly (Minister of Finance Andtrade).		
	15	Nsouli (African department IMF) and usual representatives		
	16	of IMF, IBRD and UNCTAD also present. Although only five		
	17	countries participated as creditors most Paris Club members		
	18	present to observe proceedings.		
	19	2. It had been agreed in September that Mali qualified		
	20	for Toronto terms. Creditors did not argue with the Secretariat's		
	21	figures which showed residual financing gap even after		
	22	most favourable possible terms. They therefore agreed		
	23	that one hundred per cent of all arrears at 1 January 88		
	24	and one hundred per cent of principal and interest falling		
	25	due in the consolidation period, from 30 June 1988 to 31 October		
///	26	1989 should be rescheduled, as follows (individual creditor		
//	27	positions are confidential). France will cancel one third		
/	28	of amounts falling due. UK, Italy and Switzerland will		
	29			
YYYY			Catchword: reduce	
MAIN	File number	Dept	Drafted by (Block capitals) P MOUNTFIELD	Telephone no 270 4479
ADDITIONAL	Authorised for despatch by: <i>SJS 27/10 16/45</i>			
NNNN	For COD use only	Comcen reference	Telegram number	Processed by

OUT TELEGRAM (CONT)

Classification  
CONFIDENTIAL

Caveat

Precedence  
IMMEDIATE

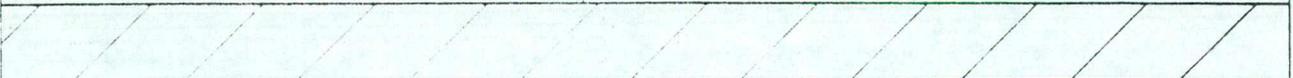
<<<< 1  
2  
3  
4  
5  
6  
7  
8  
9  
10  
11  
12  
13  
14  
15  
16  
17  
18  
19  
20  
21  
22  
23  
24  
25  
26  
27  
28  
29  
30  
/// 31  
// 32  
/ 33  
34

reduce moratorium interest rates by three point five percentage points (or halve interest rates, whichever is the less). These four countries will be repaid over fourteen years with eight years' grace. US and Netherlands rescheduled at market rates over twenty-five years with fourteen years' grace. Goodwill clause will encompass possible future ESAF.

3. FRG did not participate because only outstanding commercial debt had already been rescheduled on extended terms and at concessional rates of interest which are more favourable than those which would result from Toronto terms.

4. UK share of total was US dollars 17 million. But Mountfield made it clear that if Aircraft which comprises over half this was sold before bilateral signed outstanding debt would be reduced by sum realised.

5. Press release (by bag to Dakar) took credit for first Toronto deal, explains three options, but does not specify which creditors choose what. In answer to questions we shall say that UK chose to reduce interest rates.



For distribution order see Page      Catchword:

# Creditors agree Mali package <sup>FT 22.10.88</sup> x

By George Graham in Paris and Stephen Fidler in London

WESTERN creditor countries have moved swiftly to put into place the first debt-relief package for a poor African country under a recent debt-forgiveness initiative.

Mali, one of the world's poorest countries with per capita income of about \$200 (£113) a year, will be the first to benefit from the initiative, which offers a choice of debt-relief alternatives for creditors.

The main industrialised countries agreed in principle on the initiative at the Toronto summit in June, but the final accord did not come until last month's meeting of the Group of Seven in West Berlin.

Mali's agreement, affecting some \$70m of official debts, was finalised yesterday at a

meeting of the Paris Club of Western creditor nations. Six countries - the US, France, Italy, the Netherlands, the UK and Switzerland - took part in the agreement with Mali.

Mr Nigel Lawson, the UK Chancellor of the Exchequer, who played a significant role in setting the initiative in motion, yesterday welcomed the agreement.

He said: "I'm pleased that after 18 months of negotiation, our innovation to help the poorest African countries is bearing fruit. I expect Mali to be followed by other heavily-indebted countries, including some from the Commonwealth, in the next few months."

Creditors can choose between three options of debt

relief: rescheduling debt service payments at market rates over the unusually long period of 25 years; rescheduling over a 14-year period but at concessional interest rates; or cancelling outright a third of the debt service due, with the remainder rescheduled again over 14 years but at market rates.

The UK and Italy preferred the second option, cutting interest rates by 3½ percentage points or by half, if that would be less than 3½ per cent. The US, inhibited by legislation from cancelling debt, favoured rescheduling over 25 years, while France, as President François Mitterrand announced in Toronto, decided on the third option of cancelling a third of the debt.

Réunion des créanciers publics au Club de Paris

## Le Mali, premier bénéficiaire des résolutions du sommet de Toronto

Le Mali a obtenu jeudi 27 octobre de ses créanciers publics un allègement de sa dette de 17 milliards de francs CFA soit 340 millions de francs en application des mesures de soutien aux pays très pauvres dont le Club de Paris a été chargé. Les échéances en principal et en intérêt allant d'août 1988 à octobre 1989 seront, selon les créanciers, annulées du tiers, étalées sur vingt-cinq ans ou verront leurs taux d'intérêt réduits de 3,5 points par rapport aux taux du marché. Contraste des pays se présentant devant le Club de Paris, le Maroc avait obtenu mercredi 26 octobre un rééchelonnement de 730 millions de droits de tirages spéciaux (6 milliards de francs) des remboursements échus entre juillet 1988 et décembre 1989 selon des modalités plus classiques. Mais chacun espère, compte tenu des progrès réalisés par l'économie marocaine, qu'il s'agira du dernier exercice du Club de Paris avec ce pays.

L'un des pays les plus pauvres de la planète, le Mali, a joué les vedettes involontaires en devenant le premier champ d'application concret de la politique d'allègement de la dette, définie par les nations industrielles et orchestrée par le Club de Paris. Pour cet Etat africain géographiquement enclavé, aux prises avec tous les fléaux du développement, l'octroi d'une bouffée d'oxygène était devenu vital. Pour le forum des créanciers publics qui s'est penché sur son cas, l'occasion était venue d'apporter la preuve que la concertation internationale pouvait être efficace et rapide sur un sujet délicat.

La nécessité de venir en aide aux plus démunis s'était imposée depuis des mois. Des initiatives commençaient à fleurir à Londres, Ottawa ou Bonn, lorsque le président Mitterrand, au sommet des sept principaux pays industriels réunis à Toronto, en juin dernier, lança l'idée d'un « menu » de trois options pour alléger la dette des pays les plus pauvres : l'annulation d'une part de cette dette, la réduction des taux d'intérêt dont elle est assortie ou l'allongement des délais de remboursement. « Trois mois et trois jours plus tard », comme aime à le souligner le président du Club de Paris, Jean-Claude Trichet, un consensus permettait de lancer officiellement la machine à l'occasion de l'assemblée du Fonds monétaire international à Berlin, fin septembre. Un tour de force dont le directeur du Trésor français a quelque raison d'être satisfait.

Il lui fallait obtenir l'assentiment des 18 membres les plus actifs du forum qu'il préside, sur la base d'un accord passé à sept. Il devait surtout trouver une clé permettant d'établir des équivalences entre trois types d'efforts impossibles à comparer en termes purement financiers : annuler une part de la dette ou en bonifier les taux d'intérêt permet de réduire, en volume, l'endettement des bénéficiaires ; allonger les délais de paiements ne comporte guère d'élément de don. Les Etats-Unis ne pouvant, pour des raisons législatives, qu'envisager cette dernière solution, leurs partenaires ont admis de prendre en compte la part de risque qu'impliquent des rééchelonnements portés à vingt-cinq ans.

La Grande-Bretagne et l'Allemagne fédérale ont donné leur préférence à une réduction des taux de 3,5 points par rapport à ceux du marché. Si ces derniers tombaient en dessous de la barre de 7 %, c'est à une réduction de moitié qu'on assisterait. Quant à la France, elle s'en tient à la décision annoncée à Toronto par le chef de l'Etat d'annuler purement et simplement 30 % des échéances.

Le Mali se prêtait parfaitement à un premier exercice. Son revenu par habitant est dérisoire, 200 dollars par an. La sécheresse et le faible cours du coton — l'une des seules ressources du pays à l'exportation — ont encore aggravé une situation rendue intenable par une dette supérieure au revenu national, 1,6 milliard de dollars (9,8 milliards de francs) et dont les remboursements annuels avaient doublé en quatre ans pour passer de 46,3 millions de dollars en 1985 à 91,6 milliards en 1988, avant rééchelonnement.

Enfin, la troisième condition préalable fixée par les gouvernements créanciers, qui représentent la quasi-totalité de cette dette, avait été remplie. En août dernier, le FMI octroyait un crédit *stand by* de 12,7 millions de droits de tirage spéciaux (103 millions de francs). Préoccupé par l'enlisement des plus pauvres, en grande majorité des pays africains, le Fonds avait également accordé un prêt au titre de la facilité d'ajustement structurelle (FAS), une option aux conditions très douces, de 32,26 millions de DTS.

### Mission impossible

Cet assaut de bonne volonté ne porte pas sur des sommes impressionnantes. Il implique, en outre, de la part du Mali et de la part des autres pays amenés à bénéficier de la FAS comme des nouvelles règles du Club de Paris, un effort d'assainissement économique dont le coût social est difficile à amortir. Presque totalement démunis, le Mali a sans doute de sérieux progrès à faire en matière de gestion. Libéraliser la part connue de l'économie implique des compressions délicates de personnel. Mener une politique d'austérité dans un pays où l'espérance de vie est évaluée à quarante-sept ans tient de la mission impossible. Au moins le Mali pourra-t-il chercher une issue sur des bases moins absurdes qu'aujourd'hui.

D'autres pays bénéficieront de ce type d'allègement partiel. Mais l'importance même qu'a prise le Club de Paris illustre la gravité de la crise de la dette, déclenchée en août 1982 par la quasi-faillite mexicaine : depuis le 1<sup>er</sup> janvier 1983, plus de 80 milliards de dollars de dettes ont été rééchelonnés dans son enceinte.

FRANÇOISE CROUGNEAU.

## La Commission de Bruxelles veut taxer les photocopieurs japonais importés des Etats-Unis

BRUXELLES  
(Communautés européennes)  
de notre correspondant

Onze Etats membres sur les douze de la Communauté estiment avec la Commission européenne qu'il convient de frapper d'une taxe anti-dumping les photocopieurs japonais Ricoh qui sont assemblés en Californie puis exportés, notamment vers la Communauté. C'est ce qui est apparu, jeudi 27 octobre, lors de la réunion du « Comité de l'origine » qui rassemble des experts de la Commission européenne. Cependant, le représentant des Pays-Bas s'est exprimé contre une telle sanction, et la décision a été reportée à la fin novembre.

Selon les experts de la Commission qui enquêtaient sur place, l'origine japonaise des photocopieurs ne fait aucun doute. La quasi-totalité des pièces composant les machines sont importées du Japon et le montage en Californie ne suffit pas pour leur conférer valablement le label *made in USA*. L'enquête de la Commission a été déclenchée à la suite d'une plainte des producteurs de la CEE.

Les photocopieurs Ricoh importés directement du Japon sont déjà assujettis aux taxes anti-dumping à leur entrée dans la CEE, et le détournement par l'usine de montage californienne était un moyen pratique d'y échapper. On s'attend que, pour améliorer sa position à l'égard des règles du GATT, la firme américano-japonaise essaie d'accroître le « contenu local » de ses photocopieuses.

CONFIDENTIAL

070677  
MDHOAN 7716

CONFIDENTIAL  
FM FCO  
TO IMMEDIATE KAMPALA  
TELNO 326  
OF 281600Z OCTOBER 88  
INFO ROUTINE PARIS, TEL AVIV, THE HAGUE

UGANDA/PARIS CLUB

VARIOUS ATTEMPTS TO RESOLVE THE DEADLOCK AND ALLOW UGANDA TO RESCHEDULE ITS DEBTS AT THE PARIS CLUB IN DECEMBER ON CONCESSIONAL TORONTO TERMS.

DETAIL

FRENCH CHAIRMAN OF PARIS CLUB UK AND DUTCH HAVE ALL BEEN TRYING TO HELP. PROBLEM ARISES, AS IN 1984, BECAUSE ISRAEL HAD COMMERCIAL CLAIMS ON UGANDA, ARISING OUT OF EXPORTS OF ARMS AND OTHER GOODS TO AMIN GOVERNMENT FOR WHICH ISRAEL HAS NOT YET BEEN PAID. UGANDA HAS COUNTER CLAIM ON ISRAEL FOR DAMAGE DONE AT TIME OF ENTEBBE RAID. ISRAELI CLAIMS WERE INCLUDED IN 1984 PARIS CLUB AGREED MINUTE. BUT THE SUBSEQUENT BILATERAL AGREEMENT: WHICH WOULD IMPLEMENT AGREED MINUTE, HAS NOT YET BEEN SETTLED. AS A RESULT, ISRAEL HAS THE RIGHT TO INVOKE CREDITOR SOLIDARITY AND BLOCK THIS YEAR'S PARIS CLUB AGREEMENT, EVEN THOUGH IT HAS NO NEW CLAIMS AND WILL NOT BE A SIGNATORY THIS YEAR.

2. UGANDA WOULD BE THE FIRST COMMONWEALTH COUNTRY TO BENEFIT FROM TORONTO TERMS (MALI BEING THE FIRST, ON 27 OCTOBER). WE WOULD THEREFORE LIKE TO HELP. FRENCH SHARE THIS AIM, AND ASKED US IF WE COULD MEDIATE. WE FELT WE HAD INSUFFICIENT INFLUENCE IN ISRAEL TO AGREE. HOWEVER, ODA PROVIDED POUNDS STERLING 40,000 TO UGANDA TO FUND A CONTRACT WITH MORGAN GRENFELL WHO WERE ENGAGED TO QUANTIFY AND RECONCILE THE DIFFERENT CLAIMS. LATER, NETHERLANDS (WHO REPRESENT ISRAEL AT IMF) UNDERTOOK THE TASK OF DIPLOMATIC MEDIATION, BUT APPARENTLY WITHOUT SUCCESS AT THIS STAGE.

3. MORGAN GRENFELL TELL US (PLEASE PROTECT) THAT ISRAEL IS READY TO MEET UGANDA TO DISCUSS ISRAELI CLAIMS, BUT THAT UGANDA REFUSES TO MEET UNLESS ITS COUNTER CLAIM IS DISCUSSED AT SAME TIME. THEY BELIEVE THEIR UGANDAN CLIENTS DO SO LARGELY FOR DOMESTIC POLITICAL REASONS. THEY ALSO BELIEVE THAT ISRAEL WILL THREATEN TO BLOCK DECEMBER PARIS CLUB, WHICH GIVES THEM LEVERAGE OVER UGANDA.

4. MOUNTFIELD (TREASURY) REPORTED THIS TO DUTCH REPRESENTATIVE (MRS VAN EE) AND TO CHAIRMAN OF PARIS CLUB (LAJEUNESSE)

CONFIDENTIAL

070677  
MDHOAN 7716

AT THIS WEEK'S MEETING. CHAIRMAN ASKED HIM TO EXPLAIN SITUATION TO KIYONGA, UGANDAN MINISTER OF FINANCE, WHO WAS ALSO IN PARIS FOR CONSULTATIVE GROUP.

5. MOUNTFIELD THEREFORE VISITED KIYONGA ON 27 OCTOBER IN PARIS SEMI COLON YOU JOINED HIM. HE EMPHASISED UK WISH TO SEE UGANDA BENEFIT QUICKLY FROM TORONTO TERMS, BUT WARNED KIYONGA OF ISRAELI THREAT. HE ADDED THAT UK HAD INVOKED CREDITOR SOLIDARITY IN PAST (OVER ARGENTINA) AND WOULD FIND IT DIFFICULT TO RESIST ISRAELI DEMAND. ON PAST FORM, OTHER CREDITORS WOULD ALSO BACK ISRAEL. HE THEREFORE SUGGESTED THAT IF UGANDA WANTED AN EARLY AGREEMENT WITH PARIS CLUB, KIYONGA SHOULD CONSIDER MODIFYING HIS INSISTENCE ON SIMULTANEOUS NEGOTIATION, WITHOUT DROPPING ITS COUNTER CLAIM ALTOGETHER. FOR EXAMPLE THERE COULD BE TWO PARALLEL BUT FORMALLY SEPARATE NEGOTIATIONS. KIYONGA WAS GRATEFUL FOR THIS WARNING, BUT EMPHASISED POLITICAL DIFFICULTY OF DROPPING HIS CLAIM ON ISRAEL.

6. MOUNTFIELD LATER REPORTED BACK TO FRENCH AND DUTCH, AND INVITED FRENCH TO CONSIDER A DIPLOMATIC DEMARCHE TO ISRAEL IN AN ATTEMPT TO REMOVE THEIR VETO. TRICHET WAS RELUCTANT, AND HOPED THAT DUTCH MEDIATION WOULD BE SUCCESSFUL.

HOWE

YYYY

DISTRIBUTION

137

MAIN 136

.MONETARY  
ERD [-]

NENAD  
EAD

ADDITIONAL 1

MR WICKS NO 10 DOWNING ST

NNNN

PAGE 2  
CONFIDENTIAL

## DETAIL

2. On 28 September Madagascar met Paris Club creditors to discuss terms for the rescheduling of medium term debts. The Madagascar delegation was led by Pascal Rakatomovo and the request for rescheduling was supported by presentations from the IMF, IBRD and UNCTAD.

The terms agreed provided for rescheduling of:

- (1) 100% of new medium term maturities of principal and interest falling due between 1 March 1988 and 31 December 1989.
- (2) 100% of repayment of principal and interest falling due between 1 March 1988 and 31 December 1989 under bilateral agreements concluded under the 1981, 1982 and 1984 Paris Club *Agreements*.

### ~~AGREEMENTS~~

Rescheduling of amounts falling due under the 1986 and 1987 bilateral was declined by the creditors as were movement of the contract cut off date and removal of the de minimis threshold.

4. Madagascar was the second country to be accorded the concessional terms proposed at the Toronto Summit. Creditors chose the following options regarding repayment.

- (1) One third principal write off.

Commercial interest rate over 14 years (including 8 years grace): France

- (2) Commercial rates over 25 years (including 14 years grace): Belgium, Spain, USA

- (3) Interest rate subvention over 14 years (including 8 years grace): Austria, Canada, GFR, Italy, Sweden, Switzerland, UK.

5. Despite previous discussions the Japanese were unable to finalise their position in respect of all categories of debt. They adopted the 25 year option in respect of ODA loans which will be repaid at interest rates no less favourable than those applying to the original loans. However whilst signing the Agreed Minute they reserved their position on commercial credits and will declare their choice of option as soon as possible (within 1 month). It was understood that the problems within the Japanese system should be resolved before any further Toronto style Agreements will need to be signed so the deferment of choice from the menu should not recur.

6. The creditors agreement to consolidate debts until 31 December 1989 is dependent upon the IMF agreeing to the establishment of ESAF to replace the SBA expiring on 30 June 1989. If the ESAF arrangement is not approved by 31 March 1989 debt will only be consolidated until 30 June 1989.

7. The Madagascar had requested rescheduling of principal and interest payments under all five of their previous Paris Club agreements but creditors did not consider this justified in view of the size of the financing gap.

8. Copy of Agreed Minutes will follow by bag.

CONFIDENTIAL

FROM: A R H BOTTRILL  
DATE: 16 November 1988

CHANCELLOR

cc Chief Secretary  
Economic Secretary  
Sir P Middleton  
Sir G Littler  
Mr Anson  
Mr Lankester  
Mr Mountfield  
Mr Evans  
Mr H G Walsh  
Mrs Thomson

NIGERIA

The IMF Managing Director Camdessus has told Frank Cassell in Washington that he is not prepared to put forward a programme on the basis of the Nigerians' existing proposals. He is only prepared to consider a shadow programme which would not involve the IMF putting in its own money.

2. Camdessus' position is helpful to the extent that it exonerates the UK from the blame for the failure to agree a Fund programme. It also confirms our view that Nigeria's present policies are inadequate. The FCO, however, may still argue that we should nonetheless try to mount a rescue operation.

3. Our initial reaction to the idea of a shadow programme is negative. It is difficult to envisage the Nigerians agreeing further measures. Paris Club creditors would not accept it as a basis for rescheduling. The absence of Fund money would increase the burden placed on government bilateral creditors and the figures would not add up.

4. The difficulties of mounting a rescue operation remain as set out in your letter to the Foreign Secretary earlier today. We have told FCO officials of Camdessus' attitude since it may affect their advice to the Foreign Secretary on his reply.

A R H BOTTRILL



CONFIDENTIAL

4. Secondly, and contrary to the popular view and to Treasury thinking of the 1960s, tying does not mean a lower resource cost to the UK. On the contrary, it may even involve higher resource costs over the medium-term compared with untying. The argument, which is exactly analogous to one of the arguments for protection, is that tying protects the balance of payments. Like a tariff or an export subsidy, it improves the current account in the short-run without the terms of trade loss implicit in a more competitive real exchange rate. But it does this by shifting resources into relatively inefficient lines of activity. The efficiency gains from not tying may outweigh the terms of trade gain from tying, certainly over the medium term. In any event, the direct effect on the current account of tying is relatively small, even in the short run. It is impossible to put a firm figure on it, but it would only be a fraction - and almost certainly a small one - of the total £550 million value of tied aid procurement.

5. The arguments in favour of continued tying are industrial/commercial and political. The former is essentially a special interest argument. There are a few large companies whom tying suits very well - particularly in the construction and engineering sectors. As with any form of protection, they would complain if tying was ended. There is the further argument that tying creates a foothold for British industry in the country concerned, which then leads on to genuinely commercial exports. I believe there is very little in this in regard to the aid programme proper, but there may be something in it in regard to ATP money (which, unlike ordinary aid, is supposed to be - though often is not - directed to markets where there is a good prospect of follow-on business).

6. The political argument in favour of tying can, I think, be greatly overstated - particularly at a time when the economy is suffering from overheating. Nonetheless, there will be many people who will argue we are forgoing export business and jobs unnecessarily. Businessmen will complain that, as long as others have at least some of their aid tied, the untying would put them at a disadvantage. On the other hand, untying would be widely welcomed by the aid lobby and would go some way to countering the criticism that in GNP ratio terms our aid programme is near the bottom.

CONFIDENTIAL

7. Although the supposed benefits of ATP are often exaggerated (particularly when, as in the disgraceful Malaysian case, we are supporting exports in a "natural" UK market), for political and commercial reasons I do not think it is worth trying to stop it at this point in time. As for the rest of the aid programme, our paper offers two options: a quick, sharp untying or a more gradualistic approach. I would strongly favour the former, though the latter may be the most that you can get colleagues to accept. I see no point in making our untying dependent on others: we are, as pointed out earlier, one of the worst offenders amongst donors and we should be doing this in any event.

8. ODA officials are well aware of the merits of untying and recognise that it would help with meeting the main objectives of overseas aid. Mr Patten is said to be wary of it because of his fear that it would lose political support for the aid programme. Sir Geoffrey Howe's views are unknown. Lord Young will no doubt be torn between his liberal trading instincts and the anti-liberal views of his Trade Minister and the industrial lobby. The Prime Minister will certainly take some convincing.

9. If you agree that it would be right to press for untying, there are two ways in which we might proceed. You could write to the Foreign Secretary and to Lord Young in the first instance, without bringing the Prime Minister in at this stage. I attach a draft minute. The drawback to this approach is that Lord Young might get in first and persuade Sir Geoffrey to take a negative line. Alternatively, and I think better, I could write to my opposite number in ODA with your authority, saying that you are minded to write to the Foreign Secretary and Lord Young and asking him to sound out Mr Patten who in turn would no doubt consult Sir Geoffrey. In that way, we would try to get Sir Geoffrey committed before Lord Young is brought in and we would have some idea of how fast the FCO and ODA are willing to proceed.

*for*   
T P LANKESTER

DRAFT MINUTE TO:

FOREIGN SECRETARY  
CC - LORD YOUNG

AID TYING

It seems to me that it is time we untied our aid programme.

2. We pride ourselves on the quality of our aid. In most respects, I am sure this is correct. However, we have one of the worst records amongst donors for tying our aid. I understand that the major part of the bilateral programme is tied to the purchase of British goods. I think there can be little doubt that this significantly reduces the value of our aid to the recipients. Not only must it mean higher costs in many instances (if that were not the case, what would be the point of tying?); I am sure that the equipment and materials supplied do not always fit in with what the recipient really requires; and undoubtedly tying adds to the administrative burden not only for HMG but also for hard pressed recipient governments. In short, there must be a strong case in terms of "value for money" for untying.

3. Nor do I think there is a convincing economic case, from the UK's point of view, for tying. Tying is essentially a form of protection, and I do not regard it as any better than say a tariff or an export subsidy as a means of protecting the balance of payments. The direct impact of untying on the current account would in any case be pretty small. To put it bluntly, continued tying fits in very badly with the leading role we have been taking in promoting a more liberal international trading system and with our general approach to the single market. I understand, incidentally, that aid tying has been challenged by the Commission in Brussels.

CONFIDENTIAL

4. I do not underestimate the political and industrial arguments against a move to untying. But I think we should recognise the latter for what they largely are - the special interest arguments of a few leading firms in the construction and capital goods sectors. Though I have never been an enthusiast for the ATP, I can accept that - when properly applied - this can act as a "loss leader" for genuinely commercial business. But as for the rest of the bilateral programme, I do not believe the industrial arguments should be allowed to hold sway.

5. As for the political arguments, I should have thought that a move to untying would be widely welcomed by the aid lobby and by developing countries.

6. I attach a paper prepared by my officials which sets out the argument in greater detail. It offers two options: early untying at a stroke and a more gradualistic approach. I can see that the latter might be easier to handle politically, but I think on the merits the former is definitely to be preferred.

7. I would be interested in your views and David Young's views.

## UNTYING OVERSEAS AID (BY SOURCE)

### Introduction

1. The policy of tying overseas bilateral aid to UK procurement dates back to the origins of the aid programme. It was conceived when political perceptions and economic conditions were different from those of to-day; and it sits ill with the present Government's belief in a free market economy, its unease with interventionism, and its concern about international debt, the quality of aid and value for money from public spending. But paradoxically the UK now formally ties twice as much bilateral aid as the DAC average and a bigger proportion of its bilateral or indeed total aid programme than any other OECD country except Italy and Austria, and exercises detailed administrative control over even the smallest components of aid contracts. This note considers the case for untying aid and concludes that untying - by source, not by use - is worth serious consideration.

### Present policy

2. Tying (by source) applies to all UK bilateral aid, whether project aid or programme aid. (ATP, whether used in mixed credits or to soften loans, is by definition tied.) DTI will however allow a degree of waiver under severely restricted conditions. Multilateral aid is not tied by source, and as it has risen as a proportion of the aid programme, so has the proportion of untied aid increased.

3. The policy has however remained essentially the same, so far as our records reveal, from the beginning. ODA unquestionably has the lead responsibility for it - though DTI behave as if their interests were paramount. The policy was formally - though not very vigorously - reaffirmed soon after the Government took office in 1979. In a statement to both Houses on the outcome of the Government's aid policy review, on 20 February 1980, the then Foreign Secretary and Minister for Overseas Development said that "the greater part of our bilateral aid is tied to procurement in the United Kingdom and so provides valuable orders for British firms". Ironically the Government's response to the Foreign Affairs Committee in October 1987 went further. In its second report on "Bilateral Aid: Country Programmes" the Committee said that "we do not recommend a significant relaxation of the present guidelines on tying of bilateral aid". The Government observed that it "welcomes this recommendation. Goods and services funded by bilateral aid should generally be British and be provided by British firms." While it went on to say that "the ODA is also required to achieve value for money for the taxpayer and the recipient country", it added at DTI's insistence that "this is generally best achieved by domestic competitive tendering". The FAC, in its most recent report on FCO/ODA expenditure, noted with concern the greater degree of tying implicit in the increase in programme aid - which is more heavily tied than project aid. It observed that the UK ties much more aid than most donors, and said it intends to return to the question of tying.

4. The original reason for the policy was apparently to mitigate the effects of overseas aid expenditure on the balance of

payments. But the validity of this is questioned below, and indeed it is no longer advanced as a reason for tying: that is now seen mainly as the supposed benefit to British business, or more cynically, the desirability of keeping the industry lobby on side.

### Practical effects of tying

5. The total value of UK procurement from bilateral aid in 1987 was around £550 million out of a total bilateral aid programme of just over £700 million. This represents 0.55% of British non-oil exports of goods and services, and 0.9% of exports of manufactures.

6. The most significant effect of source tying is loss of value for money - especially where there is little or no competition within the UK - because of the absence of international competitive bidding. Quantitative estimates must be treated with caution in view of the shortage of up-to-date empirical evidence; but the evidence that is available suggests that tying reduces the real value of aid to the recipient by around 15%-20%. DTI will in fact consider allowing goods with significant foreign content to be supplied for projects if the cost saving exceeds 20% - though they are not obliged to do so. ODA have hitherto met the requirements of the Central Unit on Purchasing in respect of improved value for money, but it will be impossible for them to make significant further progress if they are precluded from competitive procedures by the tying rules, and they will be unable to meet the "more demanding" targets recommended by the Public Accounts Committee..

7. The second effect is restriction of choice. This is aggravated by the increasing practice of incorporating foreign components in nominally British manufactures, such as motor vehicles. It not only prevents the use, at times, of the most suitable materials or technology; it is also an impediment to UK participation in projects where materials, equipment, spares or maintenance have to meet requirements which already exist. Choice of projects is thus to some extent constrained. Perversely, the restrictions on UK content can prevent the supply of suitable, high quality goods with a UK trademark, sought by the recipient, and lose UK business a valuable "shop window". They can also preclude the rehabilitation of UK equipment if minor but key components are of foreign origin.

8. These constraints bear not only on ODA and their procurement agents but also on UK main contractors.

9. Supplies for programme aid can have up to 10% of foreign content. But this limit is applied item by item: DTI are extremely reluctant to apply it generally to a tranche of programme aid, so that for example 20% of the items by value could have up to 50% of foreign content. It is becoming increasingly difficult to find UK items with less than 10% foreign content and the effect of this rule is to slow down disbursement of programme aid where speed of disbursement is crucial to its effectiveness in improving the recipient's balance of payments.

10. A further effect is the administrative burden on ODA, and the consequent cost, of operating the Aid Tying Rules. These

originated when aid was disbursed by ECGD on behalf of the Treasury. They are rigid and complex and leave almost no discretion to ODA - as is shown by the attached algorithm. The rules have been reviewed three times since 1979 and are under review again between ODA and DTI with Treasury participation. But the Minister for Trade is resolutely blocking even minor simplifications of procedure; and the rules seem likely to remain well out of step with the spirit of the FMI and the Treasury's objective of improving efficiency and reducing running costs.

11. Finally, there is the administrative and policy burden on the recipient. Aid tying inevitably complicates the administration of tightly constrained foreign exchange budgets. It requires control arrangements, including import licences, which in other fora such as the IMF and the World Bank we argue strongly against, on the grounds that import demand is best determined and allocated with minimum government intervention.

### The Economics

12. In economic terms, the tying of aid is likely to involve a reduction in its real value to the receiving country as described in paragraph 6. Suppliers in the donor country are able to win contracts which they would not have won in open world competition. They are able to charge above the world price with the difference offset by the aid element. This much is fairly common ground.

13. More contentious are the supposed benefits to the donor country. These rest typically on the claimed lower balance of payments cost that tied aid imposes on the donor country compared

to untied aid . This stems from an expected improvement in the donor country's terms of trade as a result of its suppliers being able to charge above world prices for the exports supported by aid.

14. This argument, however, was framed largely against a Keynesian background where it was assumed that domestic demand and hence output might have to be held back because of a balance of payments constraint. It ignores the resource costs of supporting inefficient industries at the expense of efficient industries.

15. A gift of aid will ultimately have to be matched by a corresponding increase in the UK's net exports (ie exports less imports). Some of the resources for this will be released, whether aid is tied or not, as long as taxes are raised to finance the aid. Tying aid to procurement in the UK is superficially an attractive way of securing higher exports. However, insofar as the UK firms that get the aid-financed contracts would not have won them in open competition with foreign rivals, tying represents a form of protection of inefficient firms. It leads to resources being tied up in activities in which the UK does not have a comparative advantage, and means that overall UK production of goods and services is less than if market forces had been allowed to operate freely.

16. Where all countries decide to untie their aid, the export orders lost on UK-financed projects to more efficient foreign firms may be balanced broadly by additional orders for UK firms from aid projects financed by other countries. As these orders will have been gained in open competition, the UK will be using

its resources more efficiently and thus secure an overall gain in output. A given volume of aid can be achieved with less loss of UK domestic demand and welfare.

17. Even where the UK unties unilaterally, UK firms will still win some of the aid-financed contracts (and will be encouraged to improve their efficiency to win more of them). There may also be some increase in exports to third countries which win contracts to supply aid projects and use the proceeds to increase their imports from the UK. Some fall in sterling's real exchange rate may, nevertheless be needed to induce an increase in net exports. With exports and imports now amounting to well over £200 billion a year, the proportionate change needed is very small and the exchange rate change should be tiny. There may still be a net gain for the UK as exports are produced by efficient firms without the implicit subsidy provided by tying.

18. In short, once the full additional resource costs are taken into account the economic case for tying aid is undermined not only from the point of view of the recipient country but also that of the donor.

### The Politics

19. The international institutions have, for obvious reasons, always favoured untying by source. This is true not only of those with heavy developing country representation but also for example of the DAC. Until a decade ago the proportion of aid untied by most of the major donors grew roughly in the same proportion as their contributions to multilateral aid. But since then it has

continued to grow disproportionately, leaving the UK, as has been noted, near the bottom of the league. There are naturally suspicions that some aid which is nominally untied is so managed as to favour donor procurement. But there is doubt about the evidence for this. France's procurement performance is probably due mainly to her traditional ties with the Francophone countries which receive most of her aid, just as the UK does well with Anglophone countries with which we have strong ties. Japan, the massive growth in whose aid programme is largely untied, is frequently the object of suspicion; but to the Japanese, tying usually means choosing a Japanese main contractor, who is then free to sub-contract or buy where ever he wishes. Moreover the Japanese authorities now use the Crown Agents for procurement of untied aid. FRG and the US are avowedly liberal: the US has recently proposed to the DAC that all bilateral capital aid should be untied by source - and its Omnibus Trade Law provides for retaliation against tying by other donors.

20. Within the EC the statutory position appears to be that tied aid means tied to EC, not national, procurement (though Member States contend otherwise on the grounds that procurement is really by third countries). The Commission has challenged ODA on this issue. Hostilities are for the moment suspended but will undoubtedly be resumed as 1992 approaches. There must be some danger, when the concept of a separate UK market ceases to have meaning to the Community, that the EC will espouse a tying policy more in keeping with the attitudes of its more protectionist southern members than the UK's - ie one in which member states would have access to each other's aid but third countries would have none. In such an event third countries would undoubtedly

deny EC firms access to their untied aid. UK firms might therefore find themselves bound by an EC policy which they could do little to change, which would allow them to take advantage of (say) French aid but exclude them from untied US and Japanese aid which would be commercially much more attractive. If the UK had already adopted a policy of untying we would be in a position, in alliance perhaps with FRG, to counter this possibility.

21. Tying becomes a particular issue in negotiations on international collaborative ventures such as the World Bank's Special Programme of Assistance for Sub-Saharan Africa. In that instance the aim of the World Bank is to persuade donors to untie as much of their contributions as they will. The US and FRG have untied almost all of their contributions; the UK has offered to untie if others do so (although the DTI are trying to restrict this to 50%) and this is justified on the grounds that where we have strong historical, political and trading links we tend to get more procurement from a multinational pool of untied aid than the arithmetic of our contribution warrants. Under the Special Facility for Sub-Saharan Africa we contributed 6.3% of the pool but got 15.5% of the procurement (next in line was France with a 12.1% contribution and 14.1% of the procurement; Japan contributed 16.7% and got 6.5%).

22. Domestically, there is no doubt about the voluble support for aid tying from industry. But it is difficult to know how deep it goes beyond those companies that benefit directly from aid orders and their representatives. Neither we nor ODA have a breakdown of the industrial composition of aid procurement, but we suspect it is heavily concentrated in the capital goods

industries, notably electricals, vehicles and water-supply. However that may be, industry has a stronger and more insistent voice than other commentators on aid, and this no doubt accounts to a large extent for the strong enthusiasm for tying on the industry side of DTI. ODA also feel that untying would lose them valuable support for the aid programme from industry and the back benches. On the other hand, the effectiveness of UK aid is an important defence of the comparatively small size of our programme, and the tying of a relatively high proportion of it weakens that defence. The number of informed commentators who are conscious of this is admittedly small, but it is notable that a recent Marplan poll found that only 21% thought that the most important reason for aid was to create trade opportunities.

23. ATP needs to be considered separately. By common consent it is the least defensible part of the aid programme. Even the FAC feels that it has no place there and should be transferred to DTI. But that would make difficulties internationally: it would be seen by competitors as an aggressive move and a U-turn on multilateral disarmament; and objections would be raised to classifying DTI money as oda and counting it in our GNP percentage figure. Moreover the evidence suggests that ATP is a very inefficient economic instrument; to hand it over to DTI might weaken control. But it enjoys very strong support - at least among the tiny number of its major clients. Irrespective of the size of the constituency for its retention, it would be difficult to get rid of it while competitor countries have similar provisions which they use aggressively. Although disciplines have been tightened by international agreement with a view to limiting the use of tied aid credits, the road to multilateral disarmament

is long and slow. Interestingly the UK beneficiaries of ATP are usually ready to argue a special case for substantial foreign content if they believe that this will secure a contract for them.

### Options for change

24. The ultimate ideal is complete untying by all donors, or at least all major donors. The course which by its shock effect would most powerfully serve this aim, would be most consistent with the Government's free market position and would most improve the quality of our aid, is immediate and complete untying of all our aid - except perhaps ATP. This would of course arouse strong opposition on the industry side. But even half measures would arouse strong opposition, and indeed the less radical the opening proposal the more composed and confident the opposition might be. There is a tactical case for setting our initial sights unnervingly high. Also it obviously would allow maximum room for compromise and probably a better chance of an acceptable fallback position.

25. If however a softer approach were thought likely to be more successful, there would be a strong case for proposing gradual untying. The UK could still play a useful part in working towards a general liberalisation if we formally reversed our present policy. We would then be able to associate with other favourably inclined donors - eg the US and the FRG - in a programme of untying and of encouraging others to follow by a combination of leading and urging. A step by step process in which we did not get too far in front of the competition would also be less alarming to domestic critics. But a firm link between the rate of UK untying and those of competitors would risk indefinite delay.

26. Gradual untying could be accomplished across the board or selectively. In a selective approach, programme aid would be the most urgent case for treatment (it is already subject to an unrealistically rigorous tying regime). A start could be made by applying the requirement for a minimum of 90% UK content to the total aid package instead of individual items within it (this would win immediate support in ODA). The minimum percentage could then be decreased in stages - for example by 10% a year. The UK could take a lead position on untying in co-financing arrangements with multilateral institutions.

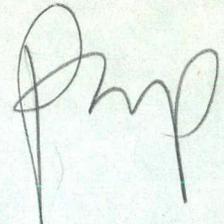
27. Project aid could be progressively untied in parallel. But if it were necessary to concede a delay, a start could be made with small projects. Around 40-50 per cent of projects are below £100,000 in value and together they account for well under one per cent of total project aid but give rise to 95% of all requests from ODA to DTI for waiver of project aid tying. A further stage in the process, if necessary, could be to apply the tying requirement, Japanese-fashion, only to the appointment of a UK main contractor.

28. There remains ATP. In view of the difficulties referred to earlier, the best prospect is probably to keep ATP in the aid programme but seek gradually to reduce the size of the provision. The mixed credit element has remained at £66 million for several years; growth has been confined to the addition of the soft loans facility in 1986. The Chief Secretary and Mr Patten agreed in this year's Survey discussions that the working of the facility should be reviewed early in 1989, in anticipation of DTI requests

for its renewal when it runs out late in 1990. Resisting renewal will not be easy, as there is a real demand for soft loans as an alternative to mixed credits, and they have the meretricious attraction of reducing immediate pressure on the ATP budget as funding is spread forward over 20 or so years.

### Conclusions

29. It seems clear that the Treasury should propose, for collective consideration, that bilateral overseas aid should be untied by source. We would favour proposing early and complete untying, except of ATP. If a more gradual approach were preferred, the modalities would need to be worked out by consultation but the Treasury's aim should be a firm, comprehensive programme with a clear, short timetable.



**CONFIDENTIAL**

**FROM: P G F DAVIS**  
**DATE: 18 NOVEMBER 1988**

**PS/CHANCELLOR**

cc Sir G Littler  
Mr Lankester  
Mr Mountfield  
Mr May  
Mr Tyrie

**AID TYING**

Please withdraw the note entitled "Untying Overseas Aid (by source)" covered by Mr Lankester's submission of 17 November, and substitute the attached version incorporating some changes requested by Sir G Littler, mainly to avoid causing unnecessary irritation in DTI.



**P G F DAVIS**

18.11.88.

**UNTYING OVERSEAS AID (BY SOURCE)**Introduction

1. The policy of tying overseas bilateral aid to UK procurement dates back to the origins of the aid programme. It was conceived when political perceptions and economic conditions were different from those of to-day; and it sits ill with the present Government's belief in a free market economy, its unease with interventionism, and its concern about international debt, the quality of aid and value for money from public spending. But paradoxically the UK now formally ties twice as much bilateral aid as the DAC average and a bigger proportion of its bilateral or indeed total aid programme than any other OECD country except Italy and Austria, and exercises detailed administrative control over even the smallest components of aid contracts. This note considers the case for untying aid and concludes that untying - by source, not by use - is worth serious consideration.

Present policy

2. Tying (by source) applies to all UK bilateral aid, whether project aid or programme aid. (ATP, whether used in mixed credits or to soften loans, is by definition tied.) DTI will however allow a degree of waiver under severely restricted conditions. Multilateral aid is not tied by source, and as it has risen as a proportion of the aid programme, so has the proportion of untied aid increased.

3. The policy has however remained essentially the same, so far as our records reveal, from the beginning. The policy was formally - though not very vigorously - reaffirmed soon after the Government took office in 1979. In a statement to both Houses on the outcome of the Government's aid policy review, on 20 February 1980, the then Foreign Secretary and Minister for Overseas Development said that "the greater part of our bilateral aid is tied to procurement in the United Kingdom and so provides valuable orders for British firms". Ironically the Government's response to the Foreign Affairs Committee in October 1987 went further. In its second report on "Bilateral Aid: Country Programmes" the Committee said that "we do not recommend a significant relaxation of the present guidelines on tying of bilateral aid". The Government observed that it "welcomes this recommendation. Goods and services funded by bilateral aid should generally be British and be provided by British firms." While it went on to say that "the ODA is also required to achieve value for money for the taxpayer and the recipient country", it added at DTI's insistence that "this is generally best achieved by domestic competitive tendering". The FAC, in its most recent report on FCO/ODA expenditure, noted with concern the greater degree of tying implicit in the increase in programme aid - which is more heavily tied than project aid. It observed that the UK ties much more aid than most donors, and said it intends to return to the question of tying.

4. The original reason for the policy was apparently to mitigate the effects of overseas aid expenditure on the balance of payments. But the validity of this is questioned below, and

indeed it is no longer advanced as a reason for tying: the reason now given is the supposed direct benefit to British firms of having exclusive access to this overseas business.

#### Practical effects of tying

5. The total value of UK procurement from bilateral aid in 1987 was around £550 million out of a total bilateral aid programme of just over £700 million. This represents 0.55% of British non-oil exports of goods and services, and 0.9% of exports of manufactures.

6. The most significant effect of source tying is loss of value for money - especially where there is little or no competition within the UK - because of the absence of international competitive bidding. Quantitative estimates must be treated with caution in view of the shortage of up-to-date empirical evidence; but the evidence that is available suggests that tying reduces the real value of aid to the recipient by around 15%-20%. DTI will in fact consider allowing goods with significant foreign content to be supplied for projects if the cost saving exceeds 20% - though they are not obliged to do so. ODA have hitherto met the requirements of the Central Unit on Purchasing in respect of improved value for money, but it will be impossible for them to make significant further progress if they are precluded from competitive procedures by the tying rules, and they will be unable to meet the "more demanding" targets recommended by the Public Accounts Committee.

7. The second effect is restriction of choice. This is aggravated by the increasing practice of incorporating foreign components in nominally British manufactures, such as motor vehicles. It not only prevents the use, at times, of the most suitable materials or technology; it is also an impediment to UK participation in projects where materials, equipment, spares or maintenance have to meet requirements which already exist. Choice of projects is thus to some extent constrained. Perversely, the restrictions on UK content can prevent the supply of suitable, high quality goods with a UK trademark, sought by the recipient, and lose UK business a valuable "shop window". They can also preclude the rehabilitation of UK equipment if minor but key components are of foreign origin.

8. These constraints bear not only on ODA and their procurement agents but also on UK main contractors.

9. Supplies for programme aid can under present rules have up to 10% of foreign content. But this limit is applied item by item: DTI are extremely reluctant to apply it generally to a tranche of programme aid, so that for example 20% of the items by value could have up to 50% of foreign content. It is becoming increasingly difficult to find UK items with less than 10% foreign content and the effect of this rule is to slow down disbursement of programme aid and speed of disbursement can often be crucial to its effectiveness in improving the recipient's balance of payments.

10. A further effect is the administrative burden on ODA, and the consequent cost, of operating the Aid Tying Rules. These

originated when aid was disbursed by ECGD on behalf of the Treasury. They are rigid and complex and leave almost no discretion to ODA - as is shown by the attached algorithm. The rules have been reviewed three times since 1979 and are under review again between ODA and DTI with Treasury participation. But the DTI have been opposing even minor simplifications of procedure; and the rules seem likely to remain well out of step with the spirit of the FMI and the Treasury's objective of improving efficiency and reducing running costs.

11. Finally, there is the administrative and policy burden on the recipient. Aid tying inevitably complicates the administration of tightly constrained foreign exchange budgets. It requires control arrangements, including import licences, which in other fora such as the IMF and the World Bank we argue strongly against, on the grounds that import demand is best determined and allocated with minimum government intervention.

### The Economics

12. In economic terms, the tying of aid is likely to involve a reduction in its real value to the receiving country as described in paragraph 6. Suppliers in the donor country are able to win contracts which they would not have won in open world competition. They are able to charge above the world price with the difference offset by the aid element. This much is fairly common ground.

13. More contentious are the supposed benefits to the donor country. These rest typically on the claimed lower balance of payments cost that tied aid imposes on the donor country compared

to untied aid . This stems from an expected improvement in the donor country's terms of trade as a result of its suppliers being able to charge above world prices for the exports supported by aid.

14. This argument, however, was framed largely against a neo-Keynesian background where it was assumed that domestic demand and hence output might have to be held back because of a balance of payments constraint. It ignores the resource costs of supporting inefficient industries at the expense of efficient industries.

15. A gift of aid will ultimately have to be matched by a corresponding increase in the UK's net exports (ie exports less imports). Some of the resources for this will be released, whether aid is tied or not, as long as taxes are raised to finance the aid. Tying aid to procurement in the UK is superficially an attractive way of securing higher exports. However, insofar as the UK firms that get the aid-financed contracts would not have won them in open competition with foreign rivals, tying represents a form of protection of inefficient firms. It leads to resources being tied up in activities in which the UK does not have a comparative advantage, and means that overall UK production of goods and services is less than if market forces had been allowed to operate freely.

16. Where all countries decide to untie their aid, the export orders lost on UK-financed projects to more efficient foreign firms may be balanced broadly by additional orders for UK firms from aid projects financed by other countries. As these orders will have been gained in open competition, the UK will be using

its resources more efficiently and thus secure an overall gain in output. A given volume of aid can be achieved with less loss of UK domestic demand and welfare.

17. Even where the UK unties unilaterally, UK firms will still win some of the aid-financed contracts (and will be encouraged to improve their efficiency to win more of them). There may also be some increase in exports to third countries which win contracts to supply aid projects and use the proceeds to increase their imports from the UK. Some fall in sterling's real exchange rate may, nevertheless be needed to induce an increase in net exports. With exports and imports now amounting to well over £200 billion a year, the proportionate change needed is very small and the exchange rate change should be tiny. There may still be a net gain for the UK as exports are produced by efficient firms without the implicit subsidy provided by tying.

18. In short, once the full additional resource costs are taken into account the economic case for tying aid is undermined not only from the point of view of the recipient country but also that of the donor.

### The Politics

19. The international institutions have, for obvious reasons, always favoured untying by source. This is true not only of those with heavy developing country representation but also for example of the DAC. Until a decade ago the proportion of aid untied by most of the major donors grew roughly in the same proportion as their contributions to multilateral aid. But since then it has

continued to grow disproportionately, leaving the UK, as has been noted, near the bottom of the league. There are naturally suspicions that some aid which is nominally untied is so managed as to favour donor procurement. But there is doubt about the evidence for this. France's procurement performance is probably due mainly to her traditional ties with the Francophone countries which receive most of her aid, just as the UK does well with Anglophone countries with which we have strong ties. Japan, the massive growth in whose aid programme is largely untied, is frequently the object of suspicion; but to the Japanese, tying usually means choosing a Japanese main contractor, who is then free to sub-contract or buy where ever he wishes. Moreover the Japanese authorities now use the Crown Agents for procurement of untied aid. FRG and the US are avowedly liberal: the US has recently proposed to the DAC that all bilateral capital aid should be untied by source - and its Omnibus Trade Law provides for retaliation against tying by other donors.

20. Within the EC the statutory position appears to be that tied aid means tied to EC, not national, procurement (though Member States contend otherwise on the grounds that procurement is really by third countries). The Commission has challenged ODA on this issue. Hostilities are for the moment suspended but will undoubtedly be resumed as 1992 approaches. There must be some danger, when the concept of a separate UK market ceases to have meaning to the Community, that the EC will espouse a tying policy more in keeping with the attitudes of its more protectionist southern members than the UK's - ie one in which member states would have access to each other's aid but third countries would have none. In such an event third countries would undoubtedly

deny EC firms access to their untied aid. UK firms might therefore find themselves bound by an EC policy which they could do little to change, which would allow them to take advantage of (say) French aid but exclude them from untied US and Japanese aid which would be commercially much more attractive. If the UK had already adopted a policy of untying we would be in a position, in alliance perhaps with FRG, to counter this possibility.

21. Tying becomes a particular issue in negotiations on international collaborative ventures such as the World Bank's Special Programme of Assistance for Sub-Saharan Africa. In that instance the aim of the World Bank is to persuade donors to untie as much of their contributions as they will. The US and FRG have untied almost all of their contributions; the UK has offered to untie if others do so (although the DTI are trying to restrict this to 50%) and this is justified on the grounds that where we have strong historical, political and trading links we tend to get more procurement from a multinational pool of untied aid than the arithmetic of our contribution warrants. Under the Special Facility for Sub-Saharan Africa we contributed 6.3% of the pool but got 15.5% of the procurement (next in line was France with a 12.1% contribution and 14.1% of the procurement; Japan contributed 16.7% and got 6.5%).

22. Domestically, there is no doubt about the voluble support for aid tying from industry. But it is difficult to know how deep it goes beyond those companies that benefit directly from aid orders and their representatives. Neither we nor ODA have a breakdown of the industrial composition of aid procurement, but we suspect it is heavily concentrated in the capital goods

industries, notably electricals, vehicles and water-supply. However that may be, industry has a stronger and more insistent voice than other commentators on aid, and this no doubt accounts for some of the pressure in favour of tying. ODA also feel that untying would lose them valuable support for the aid programme from industry and the back benches. On the other hand, the effectiveness of UK aid is an important defence of the comparatively small size of our programme, and the tying of a relatively high proportion of it weakens that defence. The number of informed commentators who are conscious of this is admittedly small, but it is notable that a recent Marplan poll found that only 21% thought that the most important reason for aid was to create trade opportunities.

23. ATP needs to be considered separately. By common consent it is the least defensible part of the aid programme. Even the FAC feels that it has no place there and should be transferred to DTI. But that would make difficulties internationally: it would be seen by competitors as an aggressive move and a U-turn on multilateral disarmament; and objections would be raised internationally to classifying DTI money as oda and counting it in our GNP percentage figure. In spite of evidence that ATP is a very inefficient economic instrument, it enjoys very strong support - at least among the small number of its major clients; and it would be difficult to get rid of it while competitor countries have similar provisions which they use aggressively. Although disciplines have been tightened by international agreement with a view to limiting the use of tied aid credits, the road to multilateral disarmament is long and slow. Interestingly the UK beneficiaries of ATP are usually ready to argue a special case for substantial foreign content if they believe that this will secure a contract for them.

Options for change

24. The ultimate ideal is complete untying by all donors, or at least all major donors. The course which by its shock effect would most powerfully serve this aim, would be most consistent with the Government's free market position and would most improve the quality of our aid, is immediate and complete untying of all our aid - except perhaps ATP. This would of course arouse strong opposition on the industry side. But even half measures would arouse strong opposition, and indeed the less radical the proposal the more composed and confident the opposition might be. There is a tactical case for setting our initial sights high. Also it obviously would allow maximum room for compromise and probably a better chance of an acceptable fallback position.

25. If however a softer approach were thought likely to be more successful, there would be a strong case for proposing gradual untying. The UK could still play a useful part in working towards a general liberalisation if we formally reversed our present policy. We would then be able to associate with other favourably inclined donors - eg the US and the FRG - in a programme of untying and of encouraging others to follow by a combination of leading and urging. A step by step process in which we did not get too far in front of the competition would also be less alarming to domestic critics.

26. Gradual untying could be accomplished across the board or selectively. In a selective approach, programme aid would be the most urgent case for treatment (it is already subject to an unrealistically rigorous tying regime). A start could be made by

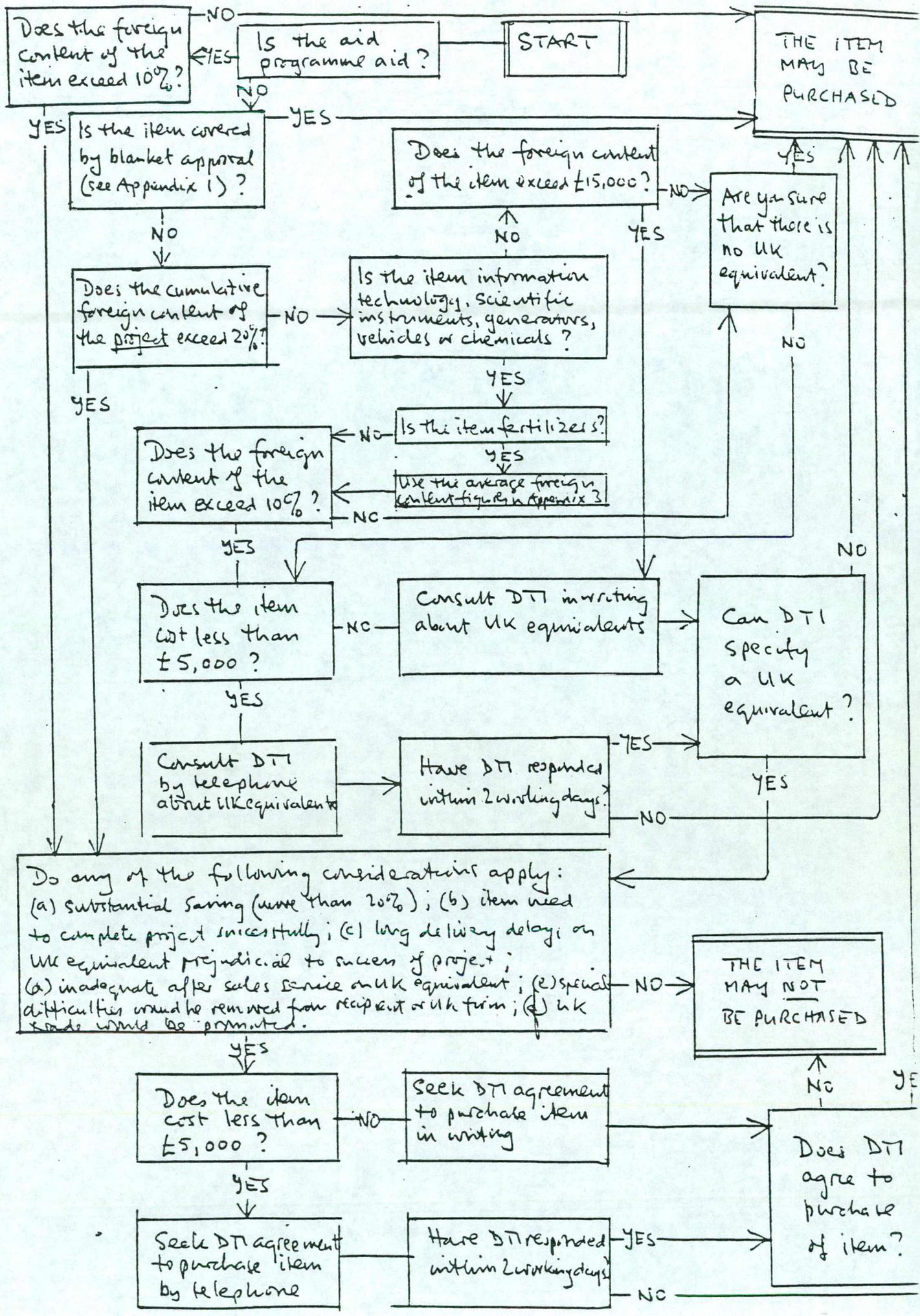
applying the requirement for a minimum of 90% UK content to the total aid package instead of individual items within it (which ODA would be likely to welcome). The minimum percentage could then be decreased in stages - for example by 10% a year. The UK could take a lead position on untying in co-financing arrangements with multilateral institutions.

27. Project aid could be progressively untied in parallel. But if it were necessary to concede a delay, a start could be made with small projects. Around 40-50 per cent of projects are below £100,000 in value and together they account for well under one per cent of total project aid but give rise to 95% of all requests from ODA to DTI for waiver of project aid tying. A further stage in the process, if necessary, could be to apply the tying requirement, Japanese-fashion, only to the appointment of a UK main contractor.

28. There remains ATP. In view of the difficulties referred to earlier, the best prospect is probably to keep ATP in the aid programme but seek gradually to reduce the size of the provision. The mixed credit element has remained at £66 million for several years; growth has been confined to the addition of the soft loans facility in 1986. The Chief Secretary and Mr Patten agreed in this year's Survey discussions that the working of the facility should be reviewed early in 1989, and that could be the occasion for deciding on the best course.

Conclusions

29. The Treasury propose in the light of the arguments in this paper that bilateral overseas aid should be untied by source. Their strong preference is for early and complete untying, except of ATP, which should be reviewed separately. If a more gradual approach were preferred, there should still be a firm, comprehensive programme with a clear and short timetable.





the department for Enterprise

The Rt. Hon. Lord Young of Graffham  
Secretary of State for Trade and Industry

The Rt Hon Nigel Lawson MP  
Chancellor of the Exchequer  
HM Treasury  
Parliament Street  
LONDON SW1P 3AG

Department of  
Trade and Industry

1-19 Victoria Street  
London SW1H 0ET

Switchboard  
01-215 7877

Telex 8811074/5 DTHQ G  
Fax 01-222 2629

18/11 ✓

CH/EXCHEQUER	
REC.	18 NOV 1988
ACTION	Mr BOTTRILL
COPIES	EST. EST. SIR P. MIDDLETON, SIR G. LITTLE, Mr ANSON, Mr SCHULTZ, Mr LANKESTER, Mr HURNBULL, Mr LOMAX, Mr MOUNTFIELD, Mr H. P. EVANS, Mr P. G. F. DAVIS, Mr WALSH, Mr THOMPSON, Mr TAYLOR.

Direct line 215 5422  
Our ref DW5ATN  
Your ref  
Date 18 November 1988

*Nigel*

**NIGERIA**

Thank you for copying to me your minute of 15 November to the Foreign Secretary.

I think it would be helpful for us to discuss the issues and I do not think Treasury officials should raise the matter with the IMF in the manner you propose, prior to that discussion.

At first reading, it would seem premature to assume that the concessional finance package, necessary for the second option set out by officials, could not be put together internationally and should not even be attempted. Certainly, I would not wish to see action taken which would inevitably damage our long term commercial and political relations with a country as important as Nigeria, without first having carefully considered all the options open to us.

I am copying this letter to the Prime Minister and to Geoffrey Howe.

*Geoffrey Howe*

YOUNG  
TO  
CX  
18 NOV





10 DOWNING STREET  
LONDON SW1A 2AA

CH/EXCHEQUER	
REC.	21 NOV 1988
ACTION	Mr BOTTRILL
COPIES TO	EST. EST. SIR P. MIDDLETON, SIR G. LITTLE, Mr MOUNTFIELD, Mr H. P. EVANS, Mr P. G. F. DAVIS, Mr WALSH, Mr Thompson, Mr THRE

20 November, 1988.

*[Handwritten signature]*

From the Private Secretary

*WPA:*

*Dear Alex,*

*Ch. A most unhelpful conclusion. And it simply leaves open the question of who pays for any package. We are seeking advice from officials. For latest developments in Washington, see ltr. in enclosed folder.*

**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.

*WPA  
21/11*

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

*Yours sincerely,  
C.D. Powell*

(C.D. Powell)

**POWELL  
TO  
ALLAN  
20 NOV**

Alex Allan, Esq.,  
Foreign and Commonwealth Office.

CONFIDENTIAL

FROM: P MOUNTFIELD  
DATE: 22 November 1988

*Conker to  
Lankester  
CSI - Mr  
Lankester  
Mr L*

CHANCELLOR

cc. Chief Secretary  
Economic Secretary  
Sir Peter Middleton  
Sir Geoffrey Littler  
Mr Anson  
Mr Lankester o/r  
Mr Turnbull  
Mr Evans  
Mr Bottrill  
Mr P Davis  
Mrs Thomson  
Mrs Chaplin  
Mr Call

*Ch. Foreign Sec's letter will not  
arrive until tomorrow. I have asked  
PS/CST to ensure that he sees these  
pps, so that he can give you his  
views on the use of the Reserve.  
Would you then be content to leave  
negotiations to him? (see Recommendation in last para). 25/22/11*

NIGERIA

The Foreign Secretary is writing tonight, suggesting a UK contribution of £60 million in 1989-90 (and more in later years) towards an international rescue package. He is not prepared to make any contributions, so this would be a call on the Reserve. The conditions, as before, are that the Nigerians agree to a stronger adjustment programme; and that other donors also contribute.

**Background**

All this was set out in Mr Lankester's submission of 14 November. He then posed a choice between letting Nigeria default, or trying to mount a rescue. Your letter tried to get the Foreign Secretary to make the first move. He strongly urged a rescue. The Prime Minister agreed. Neither addressed the question of cost, which has now surfaced.

**State of Negotiations**

Mr Lankester has been pursuing with the IMF and IBRD. He has now agreed with us and Mr Cassell the main lines on which we should ask the IMF to strengthen the programme. These are:

- (a) Fiscal: a further 2% of GDP fiscal adjustment in the 1989 budget, with an unspecified further move in 1990.

MOUNTFIELD  
TO  
CX  
22 NOV

- (b) Devaluation of the naira from about N4.5 to N6=\$1 or more.
- (c) A timetabled path towards positive real interest rates by end-1989.

We think this is the bare minimum necessary to return Nigeria towards viability; it may be too little if the oil price stays at present levels. On the other hand, it is the maximum which we believe Nigeria will do, even if bribed with an aid package. It seems consistent with the Prime Minister's instructions ('the minimum requirements for a programme we could support'). FCO officials agree. WE recommend you endorse this proposal.

### Aid Package

To secure Nigerian acquiescence, the Fund believe it will be necessary to put together a financing package to which the UK should contribute largely. We consider the minimum plausible package is \$250 million in 1989; to which the minimum UK contribution would be around \$100 million - say £60 million. We would try to help the IBRD orchestrate contributions from all the other donors, starting with \$100 million more from Japan (which is already assumed by IMF to put in \$250 million). Possible donors include US, France, FRG, Italy, Scandinavians. It will require a big diplomatic effort.

### FCO/ODA Contribution

The Foreign Secretary says (predictably, and consistent with his line in PES) that he can't afford any of this from his 1989-90 programme. We feel he should make at least some effort. Mr Anson, with whom I have discussed this, agreed with me we should ask for £20 million. (Having discussed further with ODA, I now think this may be too high: say £15 million). On the other hand, Mr Lankester, on the phone from Washington, urges that we should not hold up a decision beyond tomorrow while Ministers argue about funding.

## Timing

The urgency is that the IMF mission leader leaves for Lagos tonight. Washington is closed on Thursday for Thanksgiving. He cannot play for time too long in Lagos without losing credibility. And he cannot press for a stronger programme without a clear indication that the UK (as major creditor) is prepared to lead in putting an aid package together. Hence Mr Lankester's anxiety for an urgent decision.

## Recommendation

Subject to the Chief Secretary's views, I think you (or he, if you prefer) should ask the Foreign Secretary to chip in £20 million, offering £40 million from the Reserve (with similar contributions, in principle, in later years). This could be done by telephone. In the end it will come down to horse-trading; your fallback position might be £15 million, or even £10 million, from the Foreign Secretary.

RM

P MOUNTFIELD



Ch. see CST's views, behind

23/11

CONFIDENTIAL

EXCHEQUER

23 NOV 1988

23/11

Mr BOTTRILL  
CST, EST,  
SIR P. MIDDLETON,  
SIR G. LITTLER,  
Mr ANSON, Mr SCHOLAR,  
Mr LANKESTER,  
Mr TURNBULL, Mrs LOMAX,  
Mr MOUNTFIELD, Mr H. BEVANS,  
Mr P. E. F. DAVIS, Mr WALSH,  
Mrs THOMPSON, Mr TYRIE

FCS/88/202

CHANCELLOR OF THE EXCHEQUER

23/11/88.

Nigeria

1. In order to carry forward the policy now agreed with the Prime Minister of trying to help put together both a sound economic programme and an external financial package for Nigeria, we need quickly to take a view on the amount of aid we will be ready to contribute and how we will find the money if we are successful.

2. We need to settle our position speedily in order to give a firm indication to the IMF that we can contribute on the basis of a stronger programme and give them some idea of how much we have in mind. This will help the IMF team in its further negotiations with the Nigerians over the next week or two; and other potential donors need to be mobilised. The Nigerian Government budget is only five weeks away. Without being confident of our capacity to fund a significant aid contribution, we can neither give a positive signal to the IMF nor encourage the Nigerians to take the necessary further adjustment measures.

/3.

CONFIDENTIAL

HOWE  
TO  
CX  
23 NOV



CONFIDENTIAL

3. As to the level of our contribution, the paper produced by Treasury officials, which you circulated, recognised that we will need to play a fairly prominent part if there is to be a hope of success. The figure of £60 million per year of British aid mentioned in that paper should be about right, and is the minimum needed to unlock the significant amounts we need from other donors. On present assessments, which are of course subject to the oil price, we must expect this assistance to be required in each of the next two or three years. Clearly we would not provide aid unless the Nigerians adopt a satisfactory programme and maintain it, and are prepared to use IMF funds. Nor would we provide aid unless enough other key Western countries also participated so that a satisfactory overall aid financing package was available.

4. Nigeria was explicitly set aside from our PES bids this year. I have looked at the pressures on the agreed aid programme for next year following the PES settlement. The most I will have available to allocate as programme aid in support of adjustment policies in the whole of sub-Saharan Africa, ie all the other countries in dire straits apart from Nigeria, next year is £114 million. This is substantially less than the amount we were able finally to mobilise this year (£137 million) after using the exceptional rollover of EC underspending in 1987-88. We need to maintain our help for IMF-endorsed adjustment programmes already under way in sub-Saharan Africa and

/our

CONFIDENTIAL



**CONFIDENTIAL**

our aid to the Front Line States - which plays a crucial part in our Southern Africa strategy. This means that I cannot find the £60 million we need to play our part in an international financing package from within the existing PES allocation for aid.

5. I hope you and John Major can agree, therefore, that the £60 million can be additional. I propose that we agree that our contribution be accommodated from the Reserve in 1989/90 and would form an agreed PES bid in the next survey.

6. I am sending copies of this minute to the Prime Minister, David Young and John Major.

A handwritten signature in black ink, appearing to be 'G. Howe', written in a cursive style.

(GEOFFREY HOWE)

Foreign and Commonwealth Office

23 November 1988

**CONFIDENTIAL**

CONFIDENTIAL



FROM: P T WANLESS  
DATE: 23 November 1988

PS/CHANCELLOR

cc: Economic Secretary  
Sir Peter Middleton  
Sir Geoffrey Littler  
Mr Anson  
Mr Lankester  
Mr Turnbull  
Mr Mountfield  
Mr Evans  
Mr Bottrill  
Mr P Davis  
Mrs Thomson  
Mrs Chaplin  
Mr Call

*[CST is from ...  
& still ...  
Chaplin!]*

**NIGERIA**

The Chief Secretary has seen Mr Mountfield's submission of 22 November.

2 The Chief Secretary doubts whether the Foreign Office will be able to provide more than £10 million towards an international rescue package and he has noted that the balance will need to come from the Reserve. He thinks that it would be bearable to allow a claim of £40 million on the Reserve as part of a £50 million total package.

3 The Chief Secretary's <sup>general</sup> view is that Nigeria is important: we should help them.

*P. Wanless.*

PETER WANLESS  
Assistant Private Secretary

WANLESS  
TO  
PS/CX  
23 NOV

FROM: P MOUNTFIELD  
DATE: 2 DECEMBER 1988

CHANCELLOR

cc: Sir G Littler  
Mr Lankester  
Mr Evans  
Mr Bottrill

*Ch. content?  
2/12*

**NIGERIA: MESSAGE TO PRESIDENT BABANGIDA**

You said at today's meeting that you would like to see the text of the proposed letter.

2. I attach the version which has already been submitted to the Foreign Secretary. I have asked the Foreign Office to make it clear that it is still subject to your approval too. It will not go to No.10 until both ministers are content.

3. Stripped of diplomatic language, the key phrase is in the penultimate paragraph, which points firmly to the need for Nigeria to be ready to take an IMF drawing if the position deteriorates further.

4. If you are content, perhaps Mr Allan could tell the Foreign Secretary's Private Secretary, so that the draft can be sent to No.10 to await the Prime Minister's return from Rhodes.

*OK as [unclear]  
Not [unclear] a draft  
improvements (tho' it is);  
will [unclear] that on  
\$100m can [unclear] condition  
a Mrs Chappin R,  
whether of course  
it is.*

*RM*

P MOUNTFIELD

PRIME MINISTER

PM5AAF

HE General Ibrahim B Babangida  
 President  
 Commander-in-Chief  
 Armed Forces of Nigeria

I should like to say how delighted I am that you and Maryam will be coming to Britain on a State Visit next May. I recall with great pleasure my own visit to Nigeria in January.

~~Taking advantage of our agreement in January to keep~~  
~~in close touch with one another privately, I wanted also~~  
 wanted to let you know that I have been following closely the  
 great efforts you have been making to carry forward your  
 economic adjustment programme. I welcome in particular  
 your determination to seek an agreement with the IMF on a  
 good programme. I understand too from the Chancellor,  
 Nigel Lawson, and from my Private Secretary, Charles  
 Powell, who both saw Alhaji Abubakar Alhaji in London  
 this week, that you have personally decided to take  
 further measures to strengthen the programme which you  
 have been discussing with the IMF. I hope very much that  
 this will result in an agreement with the IMF on a  
 sufficiently strong programme to enable us to persuade  
 others on the IMF Executive Board to support it.

I do not underestimate the difficulties which your quest for a self-reliant economy poses. Your actions show, if I may say so, great political courage. I want to assure you that we for our part are anxious to do all we can to assist you in your task. With this in mind, we are working very hard behind the scenes both with the IMF and with other governments. In particular, on the assumption that a satisfactory programme can be worked out, we are taking the lead in putting together with others a package of assistance to help you to fill your anticipated financing gap. Our own contribution to such a joint effort would be \$100 million.

You are of course the best judge of what is feasible in Nigerian political terms. But I am sure you will understand, <sup>that</sup> ~~however~~, our efforts <sup>to seek a path together an</sup> ~~to pull in other donors~~ <sup>adjoining package</sup> ~~to add to the bilateral concessional financing we have~~ ~~offered~~, may need some clear demonstration on your part that you are willing <sup>if necessary</sup> to draw on all the funds available to you.

I hope that you will share with me your thoughts on the way ahead. It would help us in the coming weeks to influence others to support your efforts if I could have the clearest possible insight into your plans for the future. In the meantime, I look forward to welcoming you to Britain next May.

CONFIDENTIAL

033202  
MDADAN 9566

CONFIDENTIAL

FM LAGOS

TO IMMEDIATE DESKBY 050830Z FCO

TELNO 1197

OF 050700Z DECEMBER 1988

AND TO IMMEDIATE DESKBY 050830Z ODA, TREASURY (FOR PS/CHANCELLOR,

AND TO IMMEDIATE DESKBY 050830Z LANKASTER AND MOUNTFIELD)

AND TO IMMEDIATE UKDEL IMF/IBRD WASHINGTON

AND TO PRIORITY ABIDJAN, BONN, COPENHAGEN, OSLO, OTTAWA, PARIS,

AND TO PRIORITY STOCKHOLM, THE HAGUE, TOKYO, UKREP BRUSSELS,

AND TO PRIORITY KHARTOUM, ABU DHABI, RIYADH, ROME.

YOUR TELS NOS 21 AND 22 TO RHODES: NIGERIA - IMF

#### SUMMARY

1. PRESIDENT BABANGIDA DEEPLY GRATEFUL FOR HMG'S INITIATIVE AND HELP BUT ASKS WHETHER IN TIME AVAILABLE 1 SMALL CHANGE COULD BE MADE TO TEXT OF YOUR PROPOSED STATEMENT IN PARLIAMENT.

#### DETAIL

2. ACTION TAKEN WITH AHMED, GOVERNOR OF CENTRAL BANK, ON EVENING OF 3 NOVEMBER. AHMED SAID HE WAS HAPPY WITH TEXT IN SECOND TUR AND THAT HE WOULD SHOW IT TO PRESIDENT BABANGIDA WHOM HE WOULD BE SEEING LATER THE SAME EVENING.

3. AHMED TELEPHONED ME ON THE 4TH. THE PRESIDENT HAD BEEN VERY HAPPY INDEED WITH HMG'S INITIATIVE AND COMMITMENT, AND WOULD BE SENDING A MESSAGE OF THANKS TO THE PRIME MINISTER AT THE APPROPRIATE MOMENT. BABANGIDA HAD CAREFULLY READ TEXT OF YOUR PROPOSED STATEMENT AND HAD LIKED MOST OF IT, APART FROM 2 ELEMENTS: THE REFERENCE TO THE VERY SHARP FALL IN NIGERIANS' REAL INCOME (WHICH HE FEARED WOULD BE MISINTERPRETED AND EXPLOITED BY CRITICS OF THE STRUCTURAL ADJUSTMENT PROGRAMME AS EVIDENCE THAT THE PROGRAMME HAD REDUCED THE POPULATION TO POVERTY), AND THE FREQUENCY OF THE REFERENCES TO THE IMF. AHMED HAD EXPLAINED TO BABANGIDA THAT WE HAD SHOWN THEM THE TEXT AS A COURTESY RATHER THAN FOR COMMENTS OR SUGGESTIONS FOR AMENDMENT, WHICH MIGHT NOT BE POSSIBLE AT THIS LATE STAGE: AND AHMED ACCEPTED THAT WE WOULD NOT BE ABLE TO REMOVE OR REDUCE THE REFERENCES TO THE IMF, WHICH WERE INTEGRAL TO THE STATEMENT. BUT HE ASKED IF THERE MIGHT BE TIME TO SUBSTITUTE FOR THE FIRST 2 SENTENCES: 'NIGERIA'S FOREIGN EXCHANGE EARNINGS HAVE BEEN SEVERELY AFFECTED FOR SOME TIME BY THE FALL IN THE OIL

PRICE AND ITS HEAVY DEBT BURDEN MAKES IT INCREASINGLY DIFFICULT FOR IT TO MEET ITS COMMITMENTS,' OR WORDS TO THAT EFFECT. I SAID THAT I WOULD REPORT THE PRESIDENT'S REACTIONS AND HIS OWN SUGGESTION BUT THAT I COULD NOT PROMISE THAT THE TEXT COULD BE CHANGED AT THIS SHORT NOTICE. (COMMENT: BABANGIDA MAY BE RIGHT IN FEARING THAT THE PASSAGE IN QUESTION COULD BE USED AGAINST HIM AND HIS POLICIES, AND IF SO IT WOULD CLEARLY BE DESIRABLE, IF STILL FEASIBLE, TO MAKE THE CHANGE SUGGESTED, OR SOMETHING LIKE IT. BUT IF THIS CANNOT BE DONE IN THE TIME AVAILABLE, THE NIGERIANS WILL HAVE NO GROUNDS FOR SURPRISE OR COMPLAINT. GRATEFUL FOR INFORMATION BY TELEGRAM ON WHETHER AND IF SO WHAT CHANGES ARE MADE TO THE TEXT, SO THAT IF POSSIBLE I MAY TELL AHMED BEFORE THE STATEMENT IS MADE.)

4. AHMED PROMISED TO REPORT FIRST THING ON 5 NOVEMBER TO AAA, WHO HAD NOT BEEN AVAILABLE OVER WEEK-END. I SHALL ALSO TRY TO SEE HIM AS SOON AS POSSIBLE BUT HE IS HEAVILY COMMITTED TO BUDGET MEETINGS.

5. ACCOUNT OF REST OF CONVERSATION WITH AHMED IS IN MIFT (NOT TO ALL).

BARDER

YYYY

DISTRIBUTION

11

ADVANCE 11

. MONETARY  
MR BAYNE  
MR CARRICK  
HD/ERD  
HD/ECD(E)  
HD/ODA

RESIDENT CLERK  
~~MR LAVELLE CABINET OFFICE~~  
~~PS/CHANCELLOR TREASURY~~  
~~MR LANKASTER TREASURY~~  
MR MOUNTFIELD TREASURY

NNNN

*The job is done  
clearly  
auto up \$150 m, our offer  
to Washington*

CONFIDENTIAL  
FM FCO  
TO IMMEDIATE LAGOS  
TELNO 825  
OF 081630Z DECEMBER 88

INFO PRIORITY ABIDJAN, COPENHAGEN, OSLO, OTTAWA, PARIS, ROME  
INFO PRIORITY STOCKHOLM, THE HAGUE, TOKYO, UKREP BRUSSELS  
INFO PRIORITY WASHINGTON, KHARTOUM, ABU DHABI, RIYADH, KUWAIT  
INFO PRIORITY UKDEL IMF/IBRD WASHINGTON

ABIDJAN FOR SUTHERLAND AFDB  
MY TELNO 698 : IMF: NIGERIA: LOBBYING

1. WE ARE CONSCIOUS THAT THE NIGERIANS APPEAR SO FAR TO HAVE DONE LITTLE THEMSELVES TO PRESS THEIR CASE WITH POTENTIAL DONOR GOVERNMENTS FOR ASSISTANCE TO HELP BRIDGE THEIR FINANCING GAP. THEY HAVE TO UNDERSTAND THAT WE CANNOT DO ALL THE WORK FOR THEM.

2. WE LEAVE YOU TO JUDGE WHOM BEST TO APPROACH, BUT SEE ADVANTAGE IN YOUR TAKING THE NIGERIANS THROUGH THE GIST OF OUR LOBBYING INSTRUCTIONS TO DATE (THE RELEVANT PARTS OF MY TELNOS 679, 817, 820, 821 AND 698 TO BONN). YOU SHOULD NOT GO INTO DETAIL ABOUT DONORS' RESPONSES, BUT SHOULD MAKE THE FOLLOWING GENERAL POINTS. IT IS ALWAYS HARD LATE IN THE YEAR FOR DONORS TO ACCOMMODATE REQUESTS IN DRAWING UP THEIR AID BUDGETS FOR THE FOLLOWING YEAR. OUR OWN CONTRIBUTION MUST DEPEND ON OTHERS MAKING UP THE DIFFERENCE NEEDED TO HELP TO CLOSE THE ANTICIPATED FINANCING GAP IN 1989. WE HAVE MOUNTED A HIGH LEVEL LOBBYING CAMPAIGN TO PRESS NIGERIA'S CASE. BUT FROM OUR INITIAL SOUNDINGS WE JUDGE THAT MANY DONORS HAVE NOT YET APPRECIATED THE SCALE OF NIGERIA'S ADJUSTMENT EFFORTS, NOR THE EXTENT OF THE DETERIORATION IN ITS PER CAPITA INCOME. A MESSAGE TO DONORS THAT SQUARELY ADDRESSES THESE TWO POINTS MIGHT WELL HAVE SOME IMPACT. TO BE EFFECTIVE, IT WOULD HAVE TO PLEDGE CONTINUING COLLABORATION WITH THE IFIS. IT WOULD CLEARLY ALSO HELP IF THE NIGERIANS COULD BRING THEMSELVES TO INDICATE THAT THEY WOULD CONTEMPLATE A DRAWING FROM THE FUND IN CERTAIN CIRCUMSTANCES. BUT IF THEY FEEL UNABLE TO DO SO AT THIS STAGE, OUR ADVICE WOULD BE FOR THEM TO REMAIN SILENT ON THE MATTER RATHER THAN REHEARSE THE REASONS FOR NOT MAKING A DRAWING IN A WAY THAT WOULD ONLY ALIENATE POTENTIAL DONORS.

3. YOU MAY WISH TO DISCUSS WITH THE NIGERIANS WHERE BEST THEY MIGHT DIRECT THEIR LOBBYING EFFORTS. THE JAPANESE ARE CLEARLY A

KEY PRIORITY. SEEN FROM HERE IT WOULD ALSO BE PARTICULARLY USEFUL IF IN ADDITION TO OTHER WESTERN DONORS THEY WERE TO LOBBY SOME OF THEIR FELLOW OPEC MEMBERS - RIYADH, ABU DHABI AND DUBAI (WHERE WE HAVE LOBBIED) AND KUWAIT (WHERE WE HAVE NOT).

4. IT IS OF COURSE FOR THE NIGERIANS TO CONSIDER AT WHAT LEVEL TO MAKE THEIR APPROACHES. LAST YEAR'S EXPERIENCE SUGGESTS IT WOULD NOT BE WISE FOR AHMED OR AAA TO BE SENT ON LOBBYING VISITS AT THIS STAGE. THEY ARE NEEDED IN LAGOS TO FINALISE THE BUDGET. OUR OWN VIEW IS THAT MESSAGES FROM BABANGIDA WOULD CARRY MOST WEIGHT. IN ANY EVENT, YOU SHOULD SAY THAT WE HOPE ANY NIGERIAN LOBBYING WILL BE FREE-STANDING. LINKING IT TO OUR OWN EFFORTS WOULD, WE BELIEVE, BE COUNTERPRODUCTIVE.

HOWE  
YYYY

DISTRIBUTION

134

MAIN 134

MONETARY  
ERD [-]

WAD

NNNN

CONFIDENTIAL

CHANCELLOR

From: T P Lankester  
Date: 13 December 1988

CC

Economic Secretary  
Sir P Middleton  
Sir G Littler  
Mr Scholar  
Mr Olding-Smee  
Mr Mountfield  
Mr Evans  
Mr Davis  
Mr Bottrill  
Mr Walsh  
Mrs Thomson  
Mr Tyrie

**NIGERIA**

When I was in Washington at the end of last month, the Deputy Managing Director of the Fund, who has been handling the Nigerian negotiations, asked me if I would explore with the Chairman of the Nigerian Steering Committee (Larkman of Barclays) the scope for some debt reduction by the commercial banks.

2. I do not propose to do this in the terms suggested, but I do think it would be worth talking to the banks about the problems that lie ahead.

3. This note describes the background to the Deputy Managing Director's request, and suggests a line that I might take.

4. The Fund essentially has two problems vis a vis the banks. Firstly, although they have agreed a generous rescheduling of principal, the banks are not prepared to contribute any new money to the financing of the 1989 programme - with the result that all of the financing (over \$2 billion) will be provided by the public sector. The banks are expecting to receive all of their interest due in 1989, whereas less than half of the interest due to the public sector creditors is going to be paid. As of now, the prospects of the banks putting in new money in 1990 do not look much better.

*Very reluctant to attend to OK, provided*  
*no attack is press banks*  
*(except job for an amount)*  
*Ch. Agree line in para 10?*  
*14/12*  
*check*

5. Secondly, Nigeria simply has too much debt for its now much reduced GNP and export level. Even if the banks were willing to put in new money, it would not make all that much sense from Nigeria's standpoint; and without some debt reduction, Nigeria's task in returning to some sort of viability over the medium term is going to be very hard.

6. There is thus a severe problem of inadequate burden sharing (by the private sector) and over-indebtedness. If the banks could persuade themselves (or be persuaded) to provide some debt relief, this would not only provide some sharing of the burden in the near term but would also improve the chances of restoring Nigeria to viability in the medium term.

7. It is one thing of course to say that some debt reduction by the banks would be desirable; it is quite another to say how this might be achieved.

8. The Nigerians are running a debt conversion scheme. But so far this has resulted in only \$40 million being converted. The Nigerians have no spare foreign exchange to use for buying in debt, and the prospects for a truly spontaneous, market-related reduction of debt on any scale do not look promising (though we will press the Nigerians further on this). Furthermore, I see little prospect of a negotiated debt write-down - whether or not Nigeria goes on servicing the bank debt, the banks have little or no incentive to offer or accept a write-down. Can and should pressure be brought to bear on the banks by the official creditors?

9. I am sure it would be quite wrong for all the usual moral hazard reasons for us to bring any pressure on the banks to undertake debt reduction. However, I believe it would be desirable for the banks to have before them our analysis of the facts and prospects on the basis of which they could be better placed to decide what to do. If they were to conclude in due

course that some contribution from them by way of new money or - better still - debt reduction is necessary to safeguard their interests, so much the better. If they do not, they will have to take the possible consequences.

10. I would propose to talk to Larkman on the following lines:

- i. I would show him the table attached to this note.
- ii. Point to the large 1989 and subsequent financing requirements, and show him that all the new money is being provided by the public sector in 1989.
- iii. The public sector creditors decided to go ahead in 1989 without a contribution from the banks in that year because of the need to get Nigeria back on track quickly. The level of finance being provided by the public sector in 1989 is exceptional. Cannot assume it will be sustained in 1990 and beyond. Understand that the IMF and World Bank are unhappy that the banks have not contributed more (though we all appreciate the generous rescheduling that has been agreed).
- iv. Indicate that we understand the banks' reasons for not wishing to put in new money. But the official creditors will not be willing to meet as high a proportion of Nigeria's financing needs in 1990 and beyond as in 1989.
- v. New money, interest capitalisation, some form of debt or debt servicing reduction would be needed (simply as a matter of arithmetic) if the banks are to meet a higher proportion of the burden in future.
- vi. Ask Larkman to give some idea as to the banks' likely approach, which I would report back to Washington.

11. Of course, there is a risk that, however carefully presented, the banks will still regard this as overt pressure by the UK authorities. But on balance, I believe it right that they be made aware of the Fund's and our concerns.

12. An alternative would be to leave all discussions with the banks to the IMF and the Nigerians. A presentation by the IMF would arguably carry less moral hazard risk. On the other hand, relations between the IMF and the banks on Nigeria have not been too good: some ground-clearing by us before the IMF start a new dialogue with the banks (as I am sure they will want to) to consider what happens beyond 1989 could be helpful. Also, I think it would be somewhat awkward to have to tell the Deputy Managing Director that we are not prepared to talk to the banks at all.

T

T P LANKESTER

1989  
**Capital Account:**  
Net Change in Exposure (and Aid) \$bn

(a) London Club	-0.1
(b) Paris Club	1.0
(c) Multilaterals	1.0
(d) Official transfers (aid)	0.35
All "officials"	
(b) + (c) + (d)	2.35

Interest \$m

	<u>Expected to be Paid</u>	<u>Due</u>	<u>Interest Paid as Proportion of Interest Due</u>
(a) London Club	438	438	100
(b) Paris Club	296	1146	26
(c) Multilaterals	277	277	100
(d) Other official creditors	123	203	60
All "officials"			
(b) + (c) + (d)	696	1626	43

CONFIDENTIAL

061740  
MDLIAN 1698

CONFIDENTIAL  
FM PARIS  
TO PRIORITY LAGOS  
TELNO 04  
OF 131153Z DECEMBER 88  
INFO ROUTINE FCO, UKDEL IMF/IBRD WASHINGTON

*Handwritten signature in red ink, possibly "M. Mountfield".*

FROM MOUNTFIELD  
NIGERIA: PARIS CLUB DISCUSSION 12 DECEMBER

SUMMARY

1. THE IMF ANNOUNCED BROAD DETAIL OF THE SBA PROGRAMME AGREED WITH NIGERIA. UK SOUGHT SUPPORT FOR AID PACKAGE BUT NO FIRM RESPONSES GIVEN. CERTAIN CREDITORS ATTITUDES INDICATE PROBLEMS FOR PARIS CLUB DISCUSSION WHICH IS NOW LIKELY TO TAKE PLACE IN FEBRUARY.

DETAIL

2. IMF PROGRAMME. THE IMF REPORTED THAT THE MANAGING DIRECTORS HAD NOW AGREED THE TERMS OF A STRENGTHENED SBA PROGRAMME AFTER REJECTING INITIAL NIGERIAN PROPOSALS. (TERMS AS IN EARLIER UKDEL TELEGRAMS.) THE PROGRAMME IS LIKELY TO BE PUT TO THE IMF BOARD END-JANUARY AND RESCHEDULING CONSIDERED BY THE PARIS CLUB AT THE MEETING BEGINNING ON 27 FEBRUARY.

3. THE IMF CONCEDED THAT THE PROGRAMME WAS NOT PERFECT BUT BELIEVED THAT IT CORRECTED THE MISTAKES MADE IN 1988 BUDGET. HOWEVER THE PROGRAMME STILL ENVISAGED MASSIVE DEBT RELIEF AND OTHER FUNDING TO CLOSE THE FINANCING GAP (UNSPECIFIED) EVEN ON THE STAFF'S ASSUMPTION OF A US DOLLARS 14.50 OIL PRICE.

4. THE IBRD REPORTED THAT A US DOLLARS 500M TRADE INVESTMENT AND POLICY LOAN WAS TO BE DISCUSSED BY THE BOARD ON 20 DECEMBER. IF APPROVED, US DOLLARS 125M OF THIS WOULD BE DISBURSED BEFORE THE END OF 1988. THE IBRD ALSO REPORTED THAT A PRELIMINARY MEETING OF THE CONSULTATIVE GROUP WAS TO BE HELD ON 9 JANUARY IN LONDON.

5. AID PACKAGE. THE UK (MOUNTFIELD) DESCRIBED THE PROGRAMME AS REALISTIC AND ONE THAT HAD THE FULL SUPPORT OF THE NIGERIAN GOVERNMENT AND THE PRESIDENT. IT CLEARLY INVOLVED SOME DIFFICULT MEASURES AND THE UK HOPED THAT OTHER CREDITORS WOULD DEMONSTRATE THEIR SUPPORT FOR NIGERIA BY PARTICIPATING IN THE CONSULTATIVE GROUP AND FOLLOWED THE UK'S INITIATIVE ON THE PROVISION OF CONCESSIONAL FINANCE.

6. THE UK ARGUED THAT THE CLUB WOULD HAVE TO CONSIDER GENEROUS RESCHEDULING TERMS IN FEBRUARY BUT TORONTO TERMS WOULD NOT BE SOUGHT AND WOULD NOT MAKE MUCH DIFFERENCE TO THE CASH FLOW IN 1989. THE UK ALSO NOTED THAT THE IMF HAD ASSUMED THAT THE NEW CONSOLIDATION PERIOD WOULD BEGIN ON 1 JANUARY 1988. IN THEORY THIS REQUIRED THE NIGERIANS TO CLEAR ARREARS DUE TO CREDITORS UP TO 30 JUNE 1988. THE UK DOUBTED THAT THIS WAS FEASIBLE AND SUGGESTED THAT CREDITORS SHOULD BE PREPARED TO RESERVE THEIR POSITIONS ON ARREARS.

7. THE US AND FRG REPORTED THAT THE REQUEST FOR AID PARTICIPATION WAS BEING CONSIDERED BY THEIR GOVERNMENTS BUT THEY WERE NOT YET IN A POSITION TO REPLY. JAPAN CONFIRMED THAT THEIR OFFER OF CO-FINANCING WAS CONDITIONAL UPON A NEW PARIS CLUB SETTLEMENT.

8. POSSIBLE PROBLEM AREAS. BOTH THE US AND FRG WERE CONCERNED AT NIGERIA'S CONTINUED RELUCTANCE TO DRAW UNDER THE SBA WHEN CREDITOR GOVERNMENTS WERE BEING ASKED TO CONTRIBUTE CONCESSIONAL FINANCING AND AGREE GENEROUS RESCHEDULING. THE NIGERIANS REFUSAL TO DRAW UNDER THE SBA WOULD MAKE IT DIFFICULT TO AGREE ANY ADDITIONAL AID INPUT. THE IMF GAVE NO INDICATION OF ANY CHANGE IN NIGERIAN ATTITUDES.

9. FINANCIAL REALITIES WILL MEAN THAT THE NIGERIANS WILL HAVE TO RESCHEDULE ARREARS DUE UNDER DEBT AGREEMENTS PRIOR TO 1 JULY 1988. THIS RAISES THE QUESTION OF INEQUALITY OF PAYMENTS TO CREDITORS. THE PARIS CLUB SECRETARIAT DISTRIBUTED A QUESTIONNAIRE ASKING DETAILS OF PAYMENTS MADE TO EACH CREDITOR. ALTHOUGH BY NO MEANS UP TO DATE THE UK SEEMS TO HAVE RECEIVED MORE THAN MOST AND A NEW SETTLEMENT MAY INVOLVE PAYMENTS BY NIGERIA TO LESS FORTUNATE CREDITORS TO ACHIEVE A DEGREE OF EQUALITY.

10. THE NETHERLANDS REPORTED DIFFICULTIES IN FINALISING THE 1986 BILATERAL FOR THEIR ODA LOANS. THIS WILL PROBABLY HAVE TO BE RESOLVED IF A NEW SETTLEMENT IS TO BE REACHED IN FEBRUARY. SWITZERLAND REPORTED CONTINUED PROBLEMS OVER DEBT LIST RECONCILIATION. YOU SHOULD URGE AHMED TO RESOLVE THESE TWO QUESTIONS TO AVOID DIFFICULTIES AT FEBRUARY MEETING.

COMMENT

11. RELUCTANCE TO DRAW UNDER THE SBA IS LIKELY TO BE THE MAIN OBSTACLE TO ANOTHER SETTLEMENT. CREDITORS APPEAR RESIGNED TO CONSIDERING GENEROUS (BUT NOT CONCESSIONAL) TERMS BUT US AND FRG ARE UNLIKELY TO AGREE THESE UNLESS THE NIGERIANS MAKE A GESTURE BY DRAWING UNDER THE SBA.

FERGUSSON

YYYY

DISTRIBUTION

133

MAIN

132

.MONETARY

WAD

ADDITIONAL

1

MR WICKS NO 10 DOWNING ST

NNNN

FROM: P MOUNTFIELD  
DATE: 16 DECEMBER 1988

CHANCELLOR

cc: Chief Secretary  
Economic Secretary  
Sir P Middleton  
Sir G Littler  
Mr Wicks o/a  
Mr Lankester  
Mr Evans  
Mr Bottrill  
Mr P Davis  
Mrs Thomson

*Ch. Content for "letters" along the lines proposed to issue?*

*28/16/12*

*OK - one ✓  
two minor  
changes*

**NIGERIA - PROGRESS REPORT**

You have been following the various telegrams in the last few days, but you might like a comprehensive note of the state of play.

- (a) The programme itself. Nigeria has now signed the Letter of Intent. We have not yet received a text from Washington. But we understand that it is on the lines already forecast. The Nigerian budget is due out before Christmas, and we shall need to scrutinise it carefully to make sure there has been no back-sliding.
- (b) Debt rescheduling. Inside the Paris Club, there is now general acceptance that there will have to be an exceptionally-generous (but conventional, rather than concessional) debt rescheduling operation. The Nigerians do not help themselves by failing to agree

with their creditors on the exact list of debts concerned.

There are also renewed rumblings from the uninsured trade creditors, who fancy themselves badly done-by. (Answer: they should have insured themselves with Export Credit agencies, and paid the premium. There is a limit to what we can do for them now.)

Mr Lankester will be talking to Barclays on the lines you have just approved.

- (C) Aid package. The responses so far are, as you noted, disappointing. Our own position remains clear: UK will contribute \$100 million to a total package of \$250 million or more; but our offer lapses if we cannot assemble at least \$150 million from other sources. The most worrying feature is the apparent Japanese reluctance to commit the figures (\$250 million over this year and next) already allowed for in the IMF arithmetic. The chances of screwing another \$100 million or so out of them next year now look a bit thinner as a result. My own guess is that they will in the end commit their \$250 million and a bit more, but not necessarily in time for the 9 January Consultative Group. The demonstration effect of a big Japanese contribution will be useful, but it may take time (and further diplomatic efforts) to persuade them. The US and France both seem likely to contribute, but on a very small scale. We have had no response from FRG yet. Again, further lobbying would help. The Nigerians themselves are approaching the Saudis; some back-up from here would help.

2. The FCO have therefore planned a fresh round of lobbying, with letters both from the Foreign Secretary to his counterparts, and - if you agree - from you to the G7 Finance Ministers plus the Saudi Finance Ministers. I understand that you did not have a chance to raise the question at ECOFIN, and you may therefore wish

to send the letter to some of the non-G7 Finance Ministers as well (Netherlands, Belgium and Spain would be the obvious targets).

3. I attach the draft letter, in the terms in which it has been agreed with the FCO at official level. It needs minor variations for the different recipients: if you are content with the draft, I can submit individual lead-in paragraphs for some of the recipients. I also attach the speaking note which posts would use in delivering the letters.

RM

P MOUNTFIELD

CONFIDENTIAL

BA 9/12

073314  
MDHIAN 5967

CONFIDENTIAL  
FM WASHINGTON  
TO IMMEDIATE FCO  
TELNO 2994  
OF 160510Z DECEMBER 88  
INFO PRIORITY LAGOS, TOKYO, PARIS, STOCKHOLM, HMT, RIYADH, ODA

AMENDED DISTRIBUTION

(per Brady p/p)

*1 with spec to [unclear]  
or Jan 10.*

(ODA FOR AINSCOW, HMT FOR LANKESTER)

OUR TELNO 2977

US/NIGERIA

SUMMARY

1. CROCKER REMAINS SYMPATHETIC TO NIGERIAN CASE, BUT WARNS THAT MONEY IS SCARCE. ALSO LINGERING IRRITATION WITHIN THE WHITE HOUSE AT BABANGIDA'S TRIPLE REFUSAL TO VISIT WASHINGTON THIS YEAR. SUGGESTS HIGH-LEVEL APPROACH FROM CHANCELLOR TO BRADY. POSSIBLE FOLLOW-UP BY YOU WITH BAKER AFTER INAUGURATION.

DETAIL

2. AT LUNCH TODAY WITH CROCKER AND FREEMAN, MUNRO AND I REVERTED TO THE QUESTION OF A US CONTRIBUTION TO A FINANCIAL PACKAGE FOR NIGERIA. CROCKER (WHO RETURNED TO WASHINGTON LATE ON 14 DECEMBER) HAD GIVEN IT FURTHER THOUGHT. WHILE HE AND THE AFRICAN BUREAU REMAINED SYMPATHETIC TO OUR ECONOMIC AND POLITICAL CASE, THERE WERE TWO PARTICULAR PROBLEMS. FIRSTLY, MONEY WOULD BE VERY DIFFICULT TO FIND FROM WITHIN THE AID PROGRAMME. TO HELP NIGERIA WOULD INVOLVE ROBBING PETER TO PAY PAUL. SECONDLY, THERE WAS STILL IRRITATION, MUCH OF IT IN THE WHITE HOUSE, AT BABANGIDA HAVING THREE TIMES THIS YEAR REFUSED THE PRESIDENT'S (AND FIRST LADY'S) INVITATION TO VISIT WASHINGTON. FREEMAN COMMENTED THAT THIS WAS SEEN AS A SNUB TO THE WHITE HOUSE AND THE WHOLE REPUBLICAN RIGHT.

3. CROCKER SAID THAT DESPITE THIS, THE ECONOMIC SIDE OF THE ADMINISTRATION WAS STILL SYMPATHETIC TO NIGERIA. AN APPROACH TO THEM MIGHT BE EFFECTIVE (ALTHOUGH THEY WOULD NOT BE ABLE TO GIVE A DETAILED ANSWER FOR ABOUT 2 MONTHS). HE SUGGESTED THAT A FURTHER APPROACH BE MADE AT CABINET LEVEL IN THE FORM OF AN EARLY MESSAGE FROM THE CHANCELLOR TO BRADY. BRADY'S CONTINUATION IN OFFICE WOULD BE A HELP HERE. HE ADDED THAT IT MIGHT ALSO BE USEFUL FOR YOU TO WRITE TO SHULTZ.

4. I AGREE WITH CROCKER'S ASSESSMENT THAT A HIGH-LEVEL APPROACH IS NOW NEEDED AND RECOMMEND IN THE FIRST INSTANCE AN EARLY MESSAGE FROM THE CHANCELLOR TO BRADY. WE SHOULD HOLD A

CONFIDENTIAL

073314  
MDHIAN 5967

SEPARATE MESSAGE FROM YOU IN RESERVE UNTIL BAKER TAKES CHARGE  
NEXT YEAR, BY WHICH TIME POLITICAL MEMORIES OF BABANGIDA'S  
BEHAVIOUR SHOULD HAVE FADED.

ACLAND

YYYY

DISTRIBUTION

135

MAIN 134

.MONETARY

WAD

ADDITIONAL 1

MR WICKS NO 10.

NNNN

PAGE 2  
CONFIDENTIAL

FROM: P G F DAVIS  
DATE: 21 December 1988

- 1. MR LANKESTER *1 very much hope you can agree to this*
- 2. CHANCELLOR *this*

cc: Chief Secretary  
 Economic Secretary  
 Sir P Middleton  
 Sir T Burns  
 Mr Byatt  
 Mr Monck  
 Mr Evans  
 Mr Mountfield  
 Mr Bottrill  
 Mr May  
 Mr Tyrie

*Ch/ Agree P*  
*DF 21/12*  
*OK*

**NIGERIA: UNTYING THE NEW AID**

Although we are putting off our general proposals for untying aid, as you requested, until circumstances are more propitious, we were envisaging that the additional aid recently agreed for Nigeria would need to be untied by source. But DTI have written to us saying that they would expect it to be tied to UK goods and services. We propose not to agree.

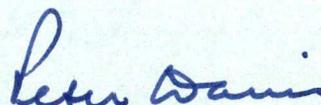
2. There is of course a general policy that bilateral aid should be tied, and DTI seek to apply this with inappropriate severity to programme aid. But occasionally they agree (grudgingly) to derogations, and there is good reason for having a derogation here. We have gone to extraordinary lengths in putting up new money for Nigeria because the situation is desperate and a great deal hangs on its early solution. It would not be sensible to reduce the effectiveness of the aid, and increase the risk of failure, by imposing administrative restrictions on the Nigerians which would tend to slow up disbursement. We have discussed this point with ODA and they are equally concerned that fast-disbursing bop support should live up to its name.

3. It is not as if tying is likely to make any difference in the end to the amount of business that comes back to the UK. The Nigerians have a preference for buying British, and where suitable British goods and services are available, would be likely to buy

them without compulsion. It would not be sensible to hold up procurement while the UK sat in judgement on every case where suitable British supplies could not be found, as happens when aid is tied - you will recall the algorithm.

4. Moreover, if we can persuade other donors to untie, not only will that improve the effectiveness of the package but it is likely to produce further business for the UK, funded by others' contributions. The best way to achieve a general untying is to take the lead ourselves. But experience with the World Bank's Special Programme for Africa shows that making the untying of our aid conditional on others following suit is apt to be troublesome. Some donors, notably Japan, will agree readily but some may have difficulty. We do not want to put obstacles in the way of getting other donors to contribute by pressing them too hard to untie.

5. With the merits of the argument all on our side, and as we have put up most of the money as an addition to the collectively-agreed aid programme, we do not see why we should not insist on sensible conditions for its use. Are you content for us so to proceed?



P G F DAVIS

CONFIDENTIAL  
FM PARIS  
TO IMMEDIATE FCO  
TELNO 1321  
OF 211706Z DECEMBER 88  
INFO IMMEDIATE LAGOS, UKDEL IMF/IBRD WASHINGTON  
INFO ROUTINE ROME, TOKYO, WASHINGTON, RIYADH  
INFO SAVING OTTAWA, THE HAGUE, BRUSSELS, MADRID, COPENHAGEN  
INFO SAVING OSLO, STOCKHOLM, ABIDJAN

*still a million  
notes from the  
tangible needs  
of assistance  
amb. White S.*

YOUR TELNOS 791 AND 720 TO BONN : NIGERIA

SUMMARY

1. MESSAGES DELIVERED. STILL NO FIRM NEWS OF FRENCH CONTRIBUTION BUT INFORMAL INDICATION THAT IT MAY BE DOLLARS 10 MILLION. FRENCH CONTINUE TO MAKE LINKAGE WITH HELP FOR THE IVORY COAST.

DETAIL

2. ACTION TAKEN ON 20 DECEMBER WITH THE TRESOR AND QUAI. GUIBERT (BEREGOVY CABINET) WAS AWARE OF OUR CONCERN ON THE ISSUE. HE AGREED IT WAS AN IMPORTANT SUBJECT. WE COULD EXPECT THAT FRANCE WOULD MAKE A CONTRIBUTION, ALTHOUGH HE WAS NOT IN A POSITION TO NAME A FIGURE. IT MIGHT BE MORE THAN JUST SYMBOLIC (OUR TELNO 1263). HE WOULD CONSULT M. BEREGOVY AND HOPED TO LET THE CHANCELLOR HAVE A PROMPT REPLY.

3. NORMAND (DUMAS' CABINET) WAS MORE FORTHCOMING. HE SAID THAT, AS ROCARD HAD RECENTLY MADE CLEAR TO SASSOU NGUESSO AND BONGO IN PARIS, 1988 WAS PROVING TO BE A PARTICULARLY DIFFICULT YEAR FOR AFRICA AND AN EXPENSIVE ONE FOR FRANCE. THERE WERE MOUNTING DEMANDS FOR EMERGENCY FINANCIAL ASSISTANCE, NOT ALL OF WHICH COULD BE MET. BUT THE FRENCH RECOGNISED THAT THERE WAS A STRONG CASE FOR A CONTRIBUTION TO NIGERIA. ASKED FOR A FIGURE, NORMAND (PLEASE PROTECT) SAID THAT HE UNDERSTOOD INFORMALLY FROM SAMUEL LAJEUNESSE (TRESOR) THAT FRANCE WOULD OFFER DOLLARS 10 MILLION. BUT WE NEEDED TO AWAIT FORMAL CONFIRMATION FROM THE TRESOR. BEREGOVY AND/OR DUMAS WOULD REPLY TO OUR MESSAGE IN DUE COURSE.

4. NORMAND ADDED THAT THE FRENCH QUOTE GESTURE UNQUOTE TO NIGERIA WAS BEING MADE ON THE ASSUMPTION THAT WE WOULD RESPOND POSITIVELY WHEN FRANCE SOUGHT OUR HELP FOR ONE OF ITS AFRICAN CLIENTS, EG IVORY COAST. WE ARGUED THAT THE CASE FOR HELPING NIGERIA STOOD ON ITS OWN MERITS AND THAT, IN CONTRAST PERHAPS TO HOUPHOUET-BOIGNY, BABANGIDA

WAS AT LEAST TRYING TO PURSUE SENSIBLE ECONOMIC POLICIES. THERE WAS ALSO THE POINT ABOUT NIGERIA'S IMPORTANCE FOR REGIONAL STABILITY. NORMAND REPLIED THAT, AS FAR AS THE FRENCH WERE CONCERNED, THE ARGUMENT ABOUT REGIONAL STABILITY APPLIED EQUALLY FORCEFULLY TO THE COTE D'IVOIRE.

5. WHEN I GAVE THE FRENCH POLITICAL DIRECTOR LUNCH TODAY, I ALSO MENTIONED OUR APPROACH ON NIGERIA. HE WAS AWARE OF OUR REQUEST IN GENERAL TERMS AND OF OUR GROUNDS FOR REGARDING NIGERIA AS A SPECIAL CASE BUT IMMEDIATELY LAUNCHED INTO A GLOOMY DESCRIPTION OF THE FINANCIAL PROBLEMS FACING FRANCE'S FRIENDS IN WEST AFRICA, SENEGAL AND THE IVORY COAST BEING ONLY THE TWO MOST CONSPICUOUS CLAIMANTS FOR MASSIVE FRENCH ASSISTANCE.

FERGUSSON

FCO PLEASE PASS SAVING ADDRESSEES

YYYY

DISTRIBUTION

138

MAIN 129

.MONETARY

WAD(-)

ADDITIONAL 1

MR WICKS NO 10.

SAVING 8

OSLO  
STOCKHOLM  
ABIDJAN  
OTTAWA

THE HAGUE  
BRUSSELS  
MADRID  
COPENHAGEN

NNNN



*Il Ministro del Tesoro*

CH/EXCHEQUER	
REC.	05 JAN 1989 ✓ 5/1
ACTION	Mr BOTTRILL
COPIES TO	EST. EST.
	Sir P. MIDDLETON, Mr WICKS, Mr ANSON, Mr SCHOLAR, Mr LANKESTER, Mr LOMAX, Mr MOUNTFIELD, Mr H. P. EVANS, Mr DAVIS, Mr WALSH, Mr THOMPSON, Mr THORPE

PWP

Rome, 24 December 1988

Dear Colleague,

I thank you for your message concerning the IMF programme and the special aid package for Nigeria.

I am fully aware of the importance of Nigeria for the economy of the whole region and of the urgency of an initiative to alleviate the enormous Nigerian debt.

As budgetary problems in Italy are particularly difficult I am not in a position to press the Ministry of Foreign Affairs to support an aid package which would require additional resources from the Italian Treasury. Anyway, I shall not fail to keep contacts with Minister Andreotti to see what Italy can do for Nigeria.

With my best wishes for Christmas and the New Year.

Giuliano Amato

The Rt Hon. Nigel Lawson  
Chancellor of the Exchequer  
H.M. Treasury  
Great George Street  
London SW 1

LETTER FROM  
AMATO



*Il Ministro del Tesoro*

Rome, 24 December 1988

Dear Colleague,

I thank you for your message concerning the IMF programme and the special aid package for Nigeria.

I am fully aware of the importance of Nigeria for the economy of the whole region and of the urgency of an initiative to alleviate the enormous Nigerian debt.

As budgetary problems in Italy are particularly difficult I am not in a position to press the Ministry of Foreign Affairs to support an aid package which would require additional resources from the Italian Treasury. Anyway, I shall not fail to keep contacts with Minister Andreotti to see what Italy can do for Nigeria.

With my best wishes for Christmas and the New Year.

*Giuliano Amato*  
Giuliano Amato

The Rt Hon. Nigel Lawson  
Chancellor of the Exchequer  
H.M. Treasury  
Great George Street  
London SW 1

CH/EXCHEQUER	
REC.	29 DEC 1988
ACTION	MR BOTTRILL ✓ 29/12
COPIES TO	CST, EST SIR P MIDDLETON MR WICKS, MR ANSON MR SCHOLAR, MR LASKATER MRS LOMAX, MR COLENG-SMEE MR MOUNTFIELD, MR EVANS MR DAVIS, MR WAUGH MR THOMSON, MR TYRIE



*Il Ministro del Tesoro*

✓

Rome, 24 December 1988

Dear Colleague,

I thank you for your message concerning the IMF programme and the special aid package for Nigeria.

I am fully aware of the importance of Nigeria for the economy of the whole region and of the urgency of an initiative to alleviate the enormous Nigerian debt.

As budgetary problems in Italy are particularly difficult I am not in a position to press the Ministry of Foreign Affairs to support an aid package which would require additional resources from the Italian Treasury. Anyway, I shall not fail to keep contacts with Minister Andreotti to see what Italy can do for Nigeria.

With my best wishes for Christmas and the New Year.

Giuliano Anato

The Rt Hon. Nigel Lawson  
Chancellor of the Exchequer  
H.M. Treasury  
Great George Street  
London SW 1

CH/EXCHEQUER	
REC.	29 DEC 1988
ATTN	MR BOTTRILL ✓ 29/12
COPIES TO	CST, EST SER P MIDDLETON MR WICKS, MR ANDSON MR SCHOLAR, MR LASKETER MRS LOMAX, MR COLENG-SME MR MOUNTFIELD, MR EVANS MR DAVIS, MR WAIN MR THOMSON, MR TYRRE

LETTER FROM  
RUDING

The Hague, December 28, 1938



MINISTER  
VAN  
FINANCIËN

CH/EXCHEQUER	
REC.	30 DEC 1938
ACTIEF	MR BOTTRILL
COPIES TO	CST, EST, SIR P. M. OCLETON, MR LICKS, MR ANSON, MR SCHOLAR, MR LANKESTER, MRS LOMAX, MR MOUNTFIELD, MR EVANS, MR DAVIS, MR WALSH, MR THOMPSON, MR TYRRE

The Rt Honourable Nigel Lawson, PC MP  
Chancellor of the Exchequer  
H.M. Treasury  
Great George Street  
GB-London SW1P 3AG  
United Kingdom

✓ H.  
*[Handwritten signature]*

BFB88/633

Re: Your request for participation in a special aid package for Nigeria

*Dear Nigel,*

Your letter, which reached me through the British embassy in the Hague, clearly conveyed to me a sense of urgency with respect to the need for Nigeria to enter into a standby agreement with the International Monetary Fund as soon as possible. I am convinced that it is of the utmost importance that Nigeria makes substantial progress in dealing with its financial and economic difficulties, not only because of the alarming decline in its per capita income, but also because a positive Nigerian experience might serve as an example for other debt-distressed countries in the region.

Nonetheless, I seriously question the need for a special aid package of \$ 300 million to make the standby agreement between Nigeria and the IMF effective. It would not be the first time that Nigeria, to my mind unjustifiably, would enter into an agreement with the Fund without using the substantial amount of money it has available. I understand that the agreement which has now been negotiated offers scope for drawings of up to \$ 600 million. Part of this amount might be used by Nigeria to close this year's financing gap, while the remainder might be added to its reserves at a later stage.

It is also of interest to note that Nigeria's income per capita has decreased so much that it has now become IDA eligible, and it is consequently also entitled to draw on the Fund's Enhanced Structural Adjustment Facility.

Besides the above, Nigeria's payments record with regard to its official bilateral debts to the Netherlands has been very poor. In addition, the Netherlands' aid programme for the medium term does not allow for a contribution to the financing of Nigeria's adjustment programme. Therefore, the Netherlands is not in a position to participate in an aid package for Nigeria.

In view of the above, I regret having to inform you that the Netherlands will not participate in the informal aid group meeting for Nigeria in London on January 9, next year.

*with personal regards.*

*H.O. Ruding*

H.O. Ruding